Pakistan Institute
of Public Finance Accountants

# Corporate Sector

# Model Solutions

## Winter Exam-2017

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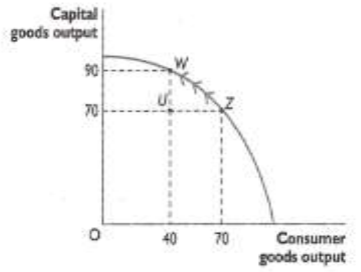
# Business Economics

## (Level-2)

**Q.1. (a)** **Opportunity cost:** It is the value of the next best alternative that is sacrificed to attain something. In every decision that an economic agent makes, there will be some alternate use for his scarce resources. The production possibility curve bows outward as a result of the law of increasing cost. 06




*Production possibility frontier*

The law of increasing costs takes place when society uses more resources to produce any specific good. This causes increased opportunity cost with each additional unit produced of that specific good (increasing amounts of the other good have to be given up). The reason is simply that, as a nation, certain resources are better suited for producing some goods then they are for other goods. Some resources would be better adapted for use with investment goods, for instance, than consumption goods. Resources are generally not perfectly adaptable for producing both categories of goods (consumption vs. investment). Therefore, increasing the output of a particular good must use less efficient resources than those already used.

**(b)** **Free Market Economy:** Free market refers to an economy where the government imposes few or no restrictions and regulations on buyers and sellers. In a free market, participants determine what products are produced, how, when and where they are made, to whom they are offered, and at what price—all based on supply and demand. 04

**Drawbacks of Free Market Economy**

1. Inequalities of income will lead to socially undesirable resource allocation.
2. Ignores social costs of production and consumption decisions.
3. Danger of emphasis on luxuries rather than necessities.
4. Danger of the growth of monopolies

**Total Marks 10**

**Q.2. (a)** **Price Elasticity of demand:** The degree of responsiveness of quantity demanded of a particular good to change in its price is called price elasticity of demand. 06

**Price elasticity of demand** = $\frac{\%\ change\ in\ Quantity\ demanded}{\%\ change\ in\ price}$

**Determinants of Price Elasticity of Demand**

1. **Nature of the commodity:** The elasticity of demand for necessities of life is generally inelastic because due to increase in price, the demand for necessary commodities does not contract generally proportionately. However, for comforts and luxuries the elasticity of demand is elastic.

2. **Number of substitutes:** If more substitutes are available for a product it would be easier for consumers to shift from one product to another and consequently more elastic their demand would be. On the other hand in absence of substitutes, the demand of a product is inelastic.

**Time:** Some goods are demanded in emergency for example lifesaving medicines. Their demand cannot be postponed. Therefore, demand elasticity is inelastic However; goods like houses, motor cars have elastic demand because consumers can take enough time to adjust their demand. 06

**(b)** 04

| Price of a slice of Pizza **(Rs)** | Quantity demanded of Pizza( Slices) |
|---|---|
| 100 | 60 |
| 80 | 90 |

Price elasticity of demand = $\frac{\Delta Q}{Q1+Q2/2} \div \frac{\Delta P}{P1+P2/2}$

$= \frac{30}{60+90/2} \div \frac{-20}{100+80/2}$

$= \frac{30}{75} \div \frac{-20}{90}$

= - 1.8

PED > 1 ( Elastic demand)

**Total Marks 10**

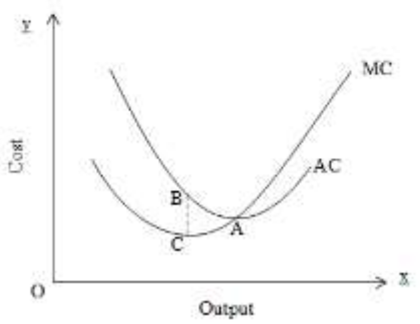
**Q.3. (a)** 05

| Price (Rs.) | Quantity Demanded | Total Revenue | Marginal Revenue | Total Cost(Rs.) | Marginal Cost |
|---|---|---|---|---|---|
| 20 | 0 | **0** | **-** | 4 | **-** |
| 16 | 1 | **16** | **16** | 10 | **6** |
| 12 | 2 | **24** | **8** | 14 | **4** |
| 10 | 3 | **30** | **6** | 20 | **6** |
| 7 | 4 | **28** | **-2** | 28 | **8** |
| 4 | 5 | **20** | **-8** | 40 | **12** |
| 0 | 6 | **0** | **-20** | 54 | **14** |

The profit maximizing point of a firm is that where MC=MR. So, the profit maximizing output is Q=3 and profit maximizing price is P=10

**(b)** <u>**Relationship between Marginal Cost and Average Cost**</u> 05

- When average cost falls, marginal cost may increase or decrease but less than average cost.
- When average cost is minimum, marginal cost is equal to average cost.
- When average cost increases , marginal cost is greater than average cost.




**Total Marks 10**

# Winter Exam-2017
# Solutions – Economics

**Q.4. (a)** **Perfect Competition:** A market structure in which a large number of small firms compete each other with homogenous products. Under perfect completion a firm is a small part of whole industry and it cannot influence the price. A firm decides only its output level at market price to maximize profit. It has following characteristics: 04

i. A large no of buyers and sellers
ii. Free entry and exit
iii. Perfect knowledge about market
iv. Homogenous products
v. Factors' mobility
vi. Negligible transport cost
vii. If the above characteristics exist in any market, it is called perfect market and competition among the firms is called perfect completion.

**(b)** **<u>Advantages of a monopoly</u>** 06

**i.** A monopolist can get benefit of economies of scale. This is the argument for natural monopolies and is the reason why many governments promote them.

**ii.** By running a monopoly with the ability to produce at large scale, a firm can then operate internationally at a much more competitive rate.

**iii.** A monopolist can use its supernormal profits to fund technological improvement, such as investment in R&D.

**<u>Disadvantages of a monopoly</u>**

Despite the above positives, there are also a number of disadvantages that come with the monopoly market structure.

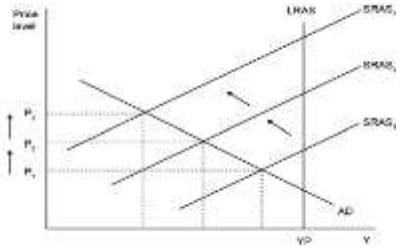
**i.** Under monopoly output is restricted in the market and Price is higher than in a competitive market.

**ii.** There is consumer exploitation under monopoly. A monopolist does not very much consider the consumer choice and charges higher prices.

**iii.** Different types of inefficiencies exist if a firm is operating as a monopolist. i,e Technical inefficiency, Productive inefficiency and X inefficiency.

**Total Marks 08**

**Q.5. (a)** 04




As cost increases, it shifts back the SRAS, thereby increasing the price level in the economy.

**(b)** The following measures can be suggested to PAKLAND economy to control over cost push inflation: 06

**i.** **Limit wage increases:** wages can be a significant input cost, and so by keeping wages low, this will assist in reducing the upward pressure on final prices.

ii. **Limit cost of utilities**: as noted earlier, another significant input cost is energy, and so the Government of PAKLAND can reduce the increase of these prices to temper inflation.

iii. **Reduce cost of imports**: this can be done by allowing the domestic currency to appreciate in relation to the currency it is importing from, thereby reducing the costs of domestic firms.

**(c)** **Expansionary and Contractionary Fiscal Policy:** 04

In recessionary phase government increases its expenditures and reduces tax in order to increase the aggregate demand, it is called expansionary fiscal policy. This policy is applied to increase economic growth and employment level in the economy.

To control inflation government decreases its expenditures and increases tax, it is called Contractionary Fiscal Policy. This policy is applied to control price level and to improve balance of payments.

**Total Marks 14**

**Q.6. (a)** **Effect on consumption:** Consumption level is inversely related with rate of interest. By increasing the rate of interest, consumption decreases and vice versa. 04

**Effect on Saving:** Saving is directly related with rate of interest. By increasing the rate of interest, saving level increases. And by decreasing the rate of interest saving level decreases.

**(b)** 06

| Year | Output (Y) | Stock of Capital | Net Investment | Depreciation | Gross Investment |
|---|---|---|---|---|---|
| (0) | (100) | **(300)** | **-** | **-** | **-** |
| 1 | 100 | **300** | **0** | **30** | **30** |
| 2 | 130 | **390** | **90** | **30** | **120** |
| 3 | 160 | **480** | **90** | **39** | **129** |
| 4 | 190 | **570** | **90** | **48** | **138** |
| 5 | 220 | **660** | **90** | **57** | **147** |

**Total Marks 10**

**Q.7. (a)** **Nominal and Real GDP:** GDP calculated at current year prices is called nominal GDP whereas GDP calculated at base year prices is called real GDP. 04

To get real GDP from nominal GDP, Nominal GDP is divided by price index and multiplied by 100.

Real GDP = $\frac{\text{Nominal GDP}}{\text{Price Index}} \times 100$

**(b)** i. **GDP at market prices** **= C + I + G + (X-M)** 08
= 20,000 +4500 + 6000 + (6450 -6240)
= Rs.30,710 m

**GDP at factor cost** **= GDP at market prices – Indirect taxes + Subsidies**
= 30,710 – 3200 + 300
= Rs. 27, 810 m

ii. **GNP at factor cost** **= GDP at factor cost + Net Income from abroad**
= 27,810 + 340
= Rs.28,150 m

**iii. National Income at factor cost = GNP at factor cost – Depreciation of capital**
= 28,150 – 1500
= Rs.26,650 m

**Total Marks 10**

**Q.8. (a)** **Appreciation and Depreciation of Currency:** In floating exchange rate system, if the value of a currency increases in terms of other currencies it is called appreciation of currency whereas if the value of currency decreases in terms of other currencies it is called depreciation of currency. 04

Yesterday Trade: Rs 105 = 1 $
Price of Rs in terms of $= 1/ 105 = 0.0095

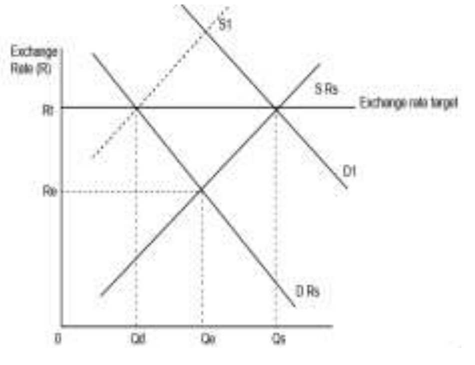
Today's Trade: Rs 110 = 1$
Price of Rs in terms of $ = 1/110 = 0.0090
It means Pak Rs. is depreciating and US $ is appreciating.

**(b)** Foreign exchange rate is determined through demand for and supply of currency. To make the value of Rupee stable central bank can either influence the demand or supply of currency. 06
The following measures can be taken in this regard:

i. **Raising the domestic interest rate:** Raising the interest rate attracts speculative funds from abroad and increases demand for rupees.

ii. **Intervention purchasing or selling of currency by a central bank:** A central bank offers to buy or sell domestic currency at a set price. This means the rate will not fall or rise above this rate.

iii. **Structural adjustments to the behaviour of the economy:** Policy action to remove the sources of the trade deficits which are causing the rate to depreciate.




Government wishes the rate to be at Rt. Policy options are:
- Increase the domestic interest rate and hence shift the demand curve for rupees to D1.
- Purchase the surplus rupees of Qs-Qd using foreign exchange reserves.
- Deflate the economy to reduce the demand for imports. This will shift the supply curve of rupees back to S1.

**Causes of Current account deficit in Pakistan:** 10

1. **Narrow export base:** Pakistan is basically an agrarian country, the major exports are therefore agricultural products such as rice, cotton, leather, fish etc. Our export base has remained narrow and that too concentrated in relatively low value added products.
2. **Consumption:** Due to ever rising number of population and consumption habits, Pakistan has remained a consumption oriented country.
3. **Lack of automated machinery:** Due to the reduced level of technological advancements in the production process the production has faltered and the decline in the quality has subsequently affected the exports.
4. **Political instability:** The uncertainty that has prevailed in the country over the years on the political scene has impacted the efficiency of the industries.
5. **Foreign debt:** Pakistan has obtained loan from multiple countries for which it regularly pays off the interest as well, the interest payments too have affected the balance of payment very adversely.

**Corrective measures**

1. **Establishment of labour intensive industries:** Since labour is cheaper in Pakistan therefore labour intensive industries can be set up and the products from such industries could be exported.
2. **Export tariffs:** Reducing export duties will help us make our exports competitive in the international market. Foreign countries may prefer to buy our products because of reduced prices.
3. **Joint ventures:** Another relevant solution may be to establish joint ventures with the foreign investors. This can actually give a boost to our sales outside the country.
4. **Controlled imports:** Imports of all luxury items should be discouraged and only the needed items should be imported.
5. **Immoral activities:** Many Pakistanis have brought a bad name to the country's trade practices by getting engaged in immoral activities such as exporting goods of inferior quality than specified in the agreement. Government needs to exercise strong control over it.

**Total Marks 20**

**Q.9. There are three main categories of money that can be used within an economy.**

a) **Commodity money**: has value even if it wasn't used as money (also known as intrinsic value). The most common is gold, as this is said to hold value aside from its monetary properties, as it is used in jewellery, and other goods.

b) **Commodity-backed money**: differs slightly from commodity money. Whilst commodity money uses the commodity itself, commodity-backed money can be exchanged for the commodity on demand. The most famous case of this is the Gold Standard.

c) **Fiat money**: is money with no intrinsic value. The value comes solely from the fact that the government has decreed that it has money for that purpose. It is used by most countries, as it can be designed to allow a stricter adherence to money's main functions.

**Total Marks 06**

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# Business Laws

(Level-2)

# Winter Exam-2017
# Solutions – Business Law



**Ans.1** Sec 132 of the Companies Act 2017: Annual General Meeting:-

1a) Every company, shall hold, an annual general meeting within sixteen months from the date of its incorporation and thereafter once in every calendar year within a period of one hundred and twenty days following the close of its financial year: Provided that, in the case of a listed company, the Commission, and, in any other case, the registrar, may for any special reason extend the time within which any annual general meeting, shall be held by a period not exceeding thirty days.

1b) In the case of a public listed company unless articles provide for a larger number, not less than ten members present personally, or through Video-link who represent not less than twenty five percent of the total voting power, either of their own or as proxies.

2) An annual general meeting shall, in the case of a listed company, be held in the town in which the registered office of the company is situate or in a nearest city: Provided that at least seven days prior to the date of meeting, on the demand of members residing in a city who hold at least ten percent of the total paid up capital or such other percentage as may be specified, a listed company must provide the facility of video- link to such members enabling them to participate in its annual general meeting.

3) The notice of an annual general meeting shall be sent to the Commission, members and every person who is entitled to receive notice of general meetings at least twenty-one days before the date fixed for the meeting:

Provided that in the case of a listed company, such notice, in addition to its being dispatched in the normal course, shall also be published in English and Urdu languages at least in one issue each of a daily newspaper of respective language having nationwide circulation.

4) Nothing in this section shall apply to a single member company.

5) Any contravention or default in complying with requirement of this section shall be an offence liable-

**(a)** in case of a listed company, to a penalty of level 2 on the standard scale; and

**(b)** in case of any other company, to a penalty of level 1 on the standard scale

**Total Marks 10**

**Ans.2** According to Sec 16(b): **Personal profits earned by partners**. — Subject to contract between the partners- (b) if a partner carries on any business of the same nature as and competing with that of the firm, he shall account for and pay to the firm all profits made by him in that business. So in this current scenario Aslam would be responsible to compensate the firm for loss sustained by the firm.

**Total Marks 10**

**Ans.3 (a)** Section 154 (d) of the Companies Act 2017: A listed company shall have not less than seven directors. **02**

**(b)** Sec 38 of the Companies Act 2017: Alteration of Articles.—(1) Subject to the provisions of this Act and to the conditions contained in its memorandum, a company may, by special resolution, alter its articles and any alteration so made shall be as valid as if originally contained in the articles and be subject in like manner to alteration by special resolution: **04**

Provided that, where such alteration affects the substantive rights or liabilities of members or of a class of members, it shall be carried out only if a majority of at least three fourths of the members or of the class of members affected by such alteration, as the case may be, exercise the option through vote personally or through proxy vote for such alteration.

**(c)** Sec 71 of the Companies Act 2017. Limitation of time for issue of certificates. — **04**

**(1)** Every company shall issue certificates of shares or other securities within thirty days after the allotment of any of its shares or other securities and ensure delivery of the certificates to the person entitled thereto at his registered address.

**(2)** Any violation of this section shall be an offence liable to a penalty of level 1 on the standard scale.

**Total Marks 10**

**Ans.4** General Scenario: Taimur enters into a contract with Saeed, to deceive him by misrepresenting his business affairs and accounts. Saeed did not check the accounts when Taimur offered him to do so. After a few months Saeed realized the true state of affairs. The business is not profitable as Taimur told him.
Rights and duties of Taimur:
**Taimur committed Fraud, which may amount to an offence of cheating.**
According to sec 17 of Contract Act 1872 "Fraud" means and includes any of the following acts committed by a party to a contract, or with his connivance, or by his agent, with intent to deceive another party thereto or his agent, or to induce him to enter into the contract:- (1) the suggestion, as a fact, of that which is not true, by one who does not believe it to be true; (2) the active concealment of a fact by one having knowledge or belief of the fact; (3) a promise made without any intention of performing it; (4) any other act fitted to deceive; (5) any such act or omission as the law specially declares to be fraudulent. Explanation – Mere silence as to facts likely to affect the willingness of a person to enter into a contract is not fraud, unless the circumstances of the case are such as, regard being had to them, it is the duty of the person keeping silence to speak, or unless his silence is, in itself, equivalent to speech.

**Rights and duties of Saeed:**
According to section 19 of Contract Act 1872: When consent to an agreement is caused by coercion, fraud or misrepresentation, the agreement is a contract voidable at the option of the party whose consent was so caused. A party to a contract, whose consent was caused by fraud or misrepresentation, may, if he thinks fit, insist that the contract shall be performed, and that he shall be put in the position in which he would have been if the representations made had been true. Exception.–If such consent was caused by

misrepresentation or by silence, fraudulent within the meaning of section 17, the contract, nevertheless, is not voidable, if the party whose consent was so caused had the means of discovering the truth with ordinary diligence. Explanation – A fraud or misrepresentation which did not cause the consent to a contract of the party on whom such fraud was practiced, or to whom such misrepresentation was made, does not render a contract voidable. Now Seed has three options,

- The contract becomes voidable at the option of the Saeed.
- Saeed may insist on performance of the contract.
- Saeed may entitle to claim damages.

**Total Marks 10**

**Ans.5** According to Sec 27(b): Liability of firm for misapplication by partners.— A firm in the course of its business receives money or property from a third party, and the money or property is misapplied by any of the partners while it is in the custody of the firm, the firm is liable to make good the loss. So according to this section firm would be responsible to pay back the loan used by Mr. Ajmal.

**Total Marks 10**

**Ans.6** **Sec 45 of Sale of Goods Act 1930. "Unpaid seller" defined.**

(1) The seller of goods is deemed to be an "unpaid seller" within the meaning of this Act--- (a) when the whole of the price has not been paid or tendered; (b) when a bill of exchange or other negotiable instrument has been received as conditional payment, and the condition on which it was received has not been fulfilled by reason of the dishonor of the instrument or otherwise.

(2) In this Chapter, the term "seller" includes any person who is in the position of a seller, as, for instance, an agent of the seller to whom the bill of landing has been endorsed, or a consignor or agent who has himself paid, or is directly responsible for, the price.

**Sec 46 of Sale of Goods Act 1930. Unpaid seller's rights.**

(1) Subject to the provisions of the Act and of any law for the time being in force, notwithstanding that the property in the goods may have passed to the buyer, the unpaid seller of goods, as such, has by implications of law--- (a) a lien on the goods for the price while he is in possession of them; (b) in case of the insolvency of the buyer a right of stopping the goods in transit after he has parted with the possession of them; (c) a right of re-sale as limited by this Act.

(2) Where the property in goods has not passed to the buyer, the unpaid seller has, in addition to his other remedies, a right of withholding delivery similar to and co-extensive with his rights of lien and stoppage in transit where the property has passed to the buyer.

**Total Marks 10**

**Ans.7** Following are the main sources of Law: **04**

**(a)**

1. Legislation
2. Precedents
3. Customs
4. Agreements

**(b)** In criminal cases the burden of proof remains constant and never shifts. The burden of proof in criminal cases is always on the prosecution, and the prosecution has to prove its case beyond any reasonable doubt. **04**

**Total Marks 08**

**Ans.8** According to sec (12)(2)

**(a)** It is stated that a condition is a stipulation essential to the main purpose of the contract, the breach of which gives rise to a right to treat the contact as repudiated. So at the time of entering into contract Amir clearly mentioned his condition for purchasing of a van. Here Babar breaches the condition which gives rise to repudiate the contract because it is not warranty.

However it may be treated as a warranty under the following conditions:
According to Sec (13) : When condition to be treated as warranty,---

(1) Where a contract of sale is subject to any condition to be fulfilled by the seller, the buyer may waive the condition or elect to treat the breach of the condition as a breach of warranty and not as a ground for treating the contract as repudiated.

(2) Where a contract of sale is not severable and the buyer has accepted the goods are part thereof the breach of any condition to be fulfilled by the seller can only be treated as a breach of warranty and not as a ground for rejecting the goods and treating the contract as repudiated, unless there is a term of the contract, express or implied, to that effect.

(3) Nothing in this section shall affect the case of any condition or warranty fulfillment of which is excused by law by reason of impossibility or otherwise.

**Total Marks 10**

**Ans.9** In this scenario the contract between Sana and Saima is a valid contract. Both parties agreed to refer the matter to arbitrator in case of dispute .It is not the violation of legal right to restraint of legal proceeding. According to sec 28, **Agreements in restraint of legal proceedings void.** Every agreement, by which any party thereto is restricted absolutely from enforcing his rights under or in respect of any contract, by the usual legal proceedings in the ordinary tribunals, or which limits the time within which he may thus enforce his rights, is void to that extent.

*Exception 1*. **Saving of contract to refer to arbitration dispute that may arise.** This section shall not render illegal a contract by which two or more persons agree that any dispute which may arise between them in respect of any subject or class of subjects shall be referred to arbitration, and that only the amount awarded in such arbitration shall be recoverable in respect of the dispute so referred.

*Exception* 2. **Saving of contract to refer questions that have already arisen.** Nor shall this section render illegal any contract in writing, by which two or more persons agree to refer to arbitration any question between them which has already arisen, or affect any provision of any law in force for the time being as to references to arbitration

**Total Marks 08**

**Ans.10** Sec 85 of the Companies Act 2017:

Power of company to alter its share capital.—

(1) A company having share capital may, if so authorized by its articles, alter the conditions of its memorandum through a special resolution, so as to–

(a) increase its authorized capital by such amount as it thinks expedient;

(b) consolidate and divide the whole or any part of its share capital into shares of larger amount than its existing shares;

(c) sub-divide its shares, or any of them, into shares of smaller amount than is fixed by the memorandum:

(d) cancel shares which, at the date of the passing of the resolution in that behalf, have not been taken or agreed to be taken by any person, and diminish the amount of its share capital by the amount of the share so cancelled:

Provided that, in the event of consolidation or sub-division of shares, the rights attaching to the new shares shall be strictly proportional to the rights attached to the previous shares so consolidated or sub-divided:

Provided further that, where any shares issued are of a class which is the same as that of shares previously issued, the rights attaching to the new shares shall be the same as those attached to the shares previously held.

(2) The new shares issued by a company shall rank pari passu with the existing shares of the class to which the new shares belong in all matters, including the right to such bonus or right issue and dividend as may be declared by the company subsequent to the date of issue of such new shares.

(3) A cancellation of shares in pursuance of sub-section (1) shall not be deemed to be a reduction of share capital within the meaning of this Act.

(4) The company shall file with the registrar notice of the exercise of any power referred to in sub-section (1) within fifteen days from the exercise thereof.

(5) Any violation of this section shall be an offence liable to a penalty of level 1 on the standard scale.

**Total Marks 10**

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# Cost Accounting

## (Level-2)

**Q.1. (a)** **Single Overhead Rates:**

**(i) On Direct Labour Cost basis**

$$= \frac{\text{Total F.O.H. cost}}{\text{Total Labour cost}} \times 100$$ **(01)**

$$= \frac{[(100{,}000 + 150{,}000 + 400{,}000)]}{[(100{,}000 + 25{,}000 + 200{,}000)]} \times 100$$ **(01)**

$$= \frac{\text{Rs. } 650{,}000}{\text{Rs. } 325{,}000} \times 100$$ **(01)**

$$= 200\% \text{ of D.L.C}$$

**(ii) On Direct Labour Hours basis**

$$= \frac{\text{Total F.O.H. cost}}{\text{Total Labour Hours}} \times 100$$ **(01)**

$$= \frac{\text{Rs. } 650{,}000}{(20{,}000 + 10{,}000 + 20{,}0000)}$$

$$= \frac{400{,}000}{200{,}000} \times 100 \text{ Hours}$$ **(01)**

$$= \frac{\text{Rs. } 650{,}000}{50{,}000 \text{ Hrs}} = \text{Rs. 13 per hour}$$ **(01)**

**(b) Overhead Rates for Each Department**

(1) On the Basis of Direct Labour Cost **(03)**

| Formula | P | Q | R |
|---|---|---|---|
| $\frac{\text{Total FOH}}{\text{Total D.L.C}} \times 100$ | $= \frac{100{,}000}{100{,}000} \times 100$ <br> $= 100\%$ | $= \frac{150{,}000}{25{,}000} \times 100$ <br> $= 600\%$ | $= \frac{400{,}000}{200{,}000} \times 100$ <br> $= 200\%$ |

(2) On the Basis of Direct Labour Hours **(03)**

| Formula | P | Q | R |
|---|---|---|---|
| $\frac{\text{Total F.O.H}}{\text{Total D.L.Hours}}$ | $= \frac{\text{Rs. } 100{,}000}{20{,}000 \text{ Hts.}}$ <br> Rs. 5/ D.L.H. | $\frac{\text{Rs. } 150{,}000}{10{,}000 \text{ houses}}$ <br> Rs. 15/ D.L.H | $\frac{\text{Rs. } 400{,}000}{20{,}000 \text{ hours}}$ <br> Rs. 20/D.L.H. |

**(c) (i) Applying F.O.H. on single (plant wide) rate.**

(Rupees)

| | P | Q | R | |
|---|---|---|---|---|
| Direct Material | 10,000 | 5,000 | 1,000 | **(01)** |
| Direct Labour | 5,000 | 250 | 5,000 | **(01)** |
| F.O.H @ Rs. 13 | 13,000 | 1,300 | 6,500 | **(01)** |
| per hour | **28,000** | **6,550** | **12,500** | **(01)** |

**(ii) Separate Rates of Direct Labour Hours**

| | P | Q | R | |
|---|---|---|---|---|
| Direct Material | 10,000 | 5,000 | 1,000 | **(01)** |
| Direct Labour | 5,000 | 250 | 5,000 | **(01)** |
| F.O.H | (5 × 1,000) | (15 × 100) | (20 × 500) | **(01)** |
| | 5,000 | 1,500 | 10,000 | |
| | **20,000** | **6,750** | **16,000** | **(01)** |

**Total Marks 20**

**Q.2. (a)**

| Days | Actual Production Units | Actual Time Hour | Standard Time Hour | Time Saved Hour | Regular Wages Rs. | Bonus Rs. | Total Wages Rs. | |
|---|---|---|---|---|---|---|---|---|
| Monday | 3,800 | 80 | 76 | --- | 6,400 | --- | 6,400 | **(1.2)** |
| Tuesday | 4,500 | // | 90 | 10 | 6,400 | 800 | 7,200 | **(1.2)** |
| Wednesday | 4,600 | // | 92 | 12 | 6,400 | 960 | 7,360 | **(1.2)** |
| Thursday | 4,500 | // | 90 | 10 | 6,400 | 800 | 7,200 | **(1.2)** |
| Friday | 4,400 | // | 88 | 8 | 6,400 | 640 | 7,040 | **(1.2)** |

| FOH Applied Rs. | Unit Labour cost Rs. | Unit FOH Cost Rs. | Unit Conversion cost Rs. | |
|---|---|---|---|---|
| 4,000 | 1.684 | 1.053 | 2.737 | **(1.2)** |
| 4,000 | 1.600 | 0.889 | 2.489 | **(1.2)** |
| 4,000 | 1.600 | 0.870 | 2.470 | **(1.2)** |
| 4,000 | 1.600 | 0.889 | 2.489 | **(1.2)** |
| 4,000 | 1.600 | 0.909 | 2.509 | **(1.2)** |

**(b) (i)** Time worked = 48 hours
Rate per hour = Rs. 100 / hour

| | | |
|---|---|---|
| Regular wage = 48 × 100 | = Rs. 4,800 | |
| Bonus = 8 × 50% × 100 | = Rs. 400 | |
| Total | = Rs. 5,200 | **(05)** |

**(b) (ii) If charged to the production:** **(1.5)**

| | |
|---|---|
| Work in progress | 4,800 |
| FOH – Control | 400 |
| Payroll | 5,200 |

**(b) (iii) If charged to a specific job: (1.5)**

| | |
|---|---|
| Work in progress | 5,200 |
| Payroll | 5,200 |

**Total Marks 20**

**Q.3.**

**Farhan Manufacturing Co.**
**Cost of Production Report Department – 3**
**For the month of October, 2014**

**Quantity Schedule**

| | | | |
|---|---|---|---|
| Units in process-opening (½ Complete) | 6,000 | | |
| Units received from proceeding dept. | 45,000 | 51,000 | **(02)** |
| Units completed &transferred to next dept. | 41,500 | | |
| Units still in process (2/3rd Complete) | 9,000 | | |
| Units lost at the end of process | 500 | 51,000 | **(02)** |

**Cost Charged to Department**

| | | Rs. | Total Rs. | Per Unit Rs. | |
|---|---|---|---|---|---|
| Work-in-process opening inventory | Lab | 10,000 | | | |
| | FOH | 18,000 | 28,000 | | **(01)** |
| Cost from proceeding department | | | 180,000 | 4.0 | **(01)** |
| Cost added by department | | | | | |
| Labour | | | 144,000 | 3.2 | **(01)** |
| Factory Overhead | | | 126,000 | 2.8 | **(01)** |
| Total Cost added by department | | | 270,000 | 6.0 | **(01)** |
| Total cost accounted for | | | 478,000 | 10.0 | **(01)** |

**Cost Accounted for as follow**

| | Rs. | Rs. | |
|---|---|---|---|
| Cost transfer to next dept. of WIP opening inv. | | | |
| Inventory cost | 28,000 | | |
| Labour (6,000 × ½ × 3.2) | 9,600 | | |
| Factory overhead (6,000 × ½ × 2.8) | 8,400 | 46,000 | **(02)** |
| Cost transfer of current product units, 35,500 units × Rs. 10 | | 355,000 | **(01)** |
| Cost of units lost at end | | 5,000 | **(01)** |
| Cost of WIP closing inventory from Proceeding dept. (9,000 × Rs. 4) | 36,000 | | |
| Labour (9,000 × 2/3× 3.2) | 19,200 | | |
| Factory Overhead (9,000 × 2/3× 2.8) | 16,800 | 72,000 | **(02)** |
| Total cost accounted for | | 478,000 | **(02)** |

**Computation Explained**

| | | |
|---|---|---|
| Equivalent production | | |
| Units transfer to next dept. | 41,500 | **(01)** |
| Less opening WIP inventory | 6,000 | **(01)** |
| | 35,500 | **(01)** |
| Add opening WIP inventory (6,000 × ½) | 3,000 | **(01)** |
| Add closing WIP inventory (9,000 × 2/3) | 6,000 | **(01)** |
| Add units lost at end | 500 | **(01)** |
| | 45,000 | **(02)** |

**List Cost**

| | | |
|---|---|---|
| Labour | = Rs. 144,000 ÷ 45,000 units = Rs. 3.2 | **(01)** |
| Factory Overhead | = Rs. 126,000 ÷ 45,000 units = Rs. 2.8 | **(01)** |

**Cost of lost units**

| | | Rs. | |
|---|---|---|---|
| Cost from proceeding dept. | (500 × 4.0) | 2,000 | |
| Labour | (500 × 3.2) | 1,600 | |
| Factory overhead | (500 × 2.8) | 1,400 | |
| | | 5,000 | **(02)** |

**Total Marks 30**

**Q.4.** **Standard Cost Per Unit** **(05)**

| | Rs. |
|---|---|
| Direct Materials 0.06kg at Rs. 42*kg* | 2.52 |
| Direct Labour 1.3 hours at Rs. 8 Hours | 10.40 |
| Prime Cost | **12.92** |
| Add Variable overhead 1.3 hour @ Rs. 7.00 | 9.10 |
| Total Variable Cost | **22.02** |

**Standard Cost** **(05)**

| | Rs. |
|---|---|
| Direct Materials (Rs. 16,900 + Rs. 740) | 17,640 |
| Direct Labour (Rs.70,560 + Rs. 2,240) | 72,800 |
| Variable Overhead (Rs. 68,400 - Rs 4,700) | 63,700 |
| Total Variable Cost | **154,140** |
| Fixed Cost (Rs. 57,000 – 1,000) | 56,000 |
| Total Cost | **210,140** |

**Total Marks 10**

**Q.5.**

**Irfan Corporation**
**Comparative Income Statement**
**For the month ending June 30, 2011**

| | Rs. (million) | | |
|---|---|---|---|
| | **FIFO** | **LIFO** | |
| Sales (16,000 units @ Rs. 7,000) | 112.00 | 112.00 | **(01)** |
| Opening inventory | 6.00 | 6.00 | **(01)** |
| Purchases | 62.90 | 62.90 | **(01)** |
| Available for sale | 68.90 | 68.90 | **(01)** |
| Closing inventory | **17.40** | **15.80** | **(01)** |
| Cost of goods sold | 51.50 | 53.10 | **(01)** |
| Gross profit(Sales – Cost of goods sold) | 60.50 | 58.90 | **(01)** |
| Marketing and administrative expenses | 21.00 | 21.00 | **(01)** |
| Income before income tax | 39.50 | 37.90 | **(01)** |
| Income tax (35%) | 13.83 | 13.27 | **(01)** |
| Net Income | **25.67** | **24.63** | **(02)** |

**FIFO**

| Units | Rs. / Unit | Rs. (m) | |
|---|---|---|---|
| 4,000 | 3,500 | 14.00 | |
| 1,000 | 3,400 | 3.40 | |
| 5,000 | | **17.40** | **(02)** |

**LIFO**

| Units | Rs. / Unit | Rs. (m) | |
|---|---|---|---|
| 2,000 | 3,000 | 6.00 | |
| 2,000 | 3,200 | 6.40 | |
| 1,000 | 3,400 | 3.40 | |
| 5,000 | | **15.80** | **(02)** |

**Cash position at end of the June**

| | | Rs. (m) | |
|---|---|---|---|
| | **FIFO** | **LIFO** | |
| Sales (receipts) | 112.00 | 112.00 | **(01)** |
| Purchases | 62.90 | 62.90 | |
| Marketing and administrative expenses | 21.00 | 21.00 | |
| Income tax (35%) | 13.83 | 13.27 | |
| Total disbursements | 97.73 | 97.17 | **(02)** |
| Cash balance | 14.27 | 14.83 | **(01)** |

**Total Marks 20**

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# Financial Accounting

## (Level-3)

# Winter Exam-2017
# Solutions – Financial Accounting

**Q.1.**

| | | | Cost | NRV | Valuation (lower of cost /NEV) | |
|---|---|---|---|---|---|---|
| Engine | 7.00 + 0.80 + 10/2 | = | 12.80 | 18 | 12.8 | **(2)** |
| Carriage | 5.00 + 0.50 + 10/5 | = | 7.50 | 11 | 7.5 | **(2)** |
| Track | 2.00 + 0.25 + 10/10 | = | 3.25 | 04 | 3.25 | **(2)** |

**Total Marks 06**

**Q.2.**

ABC
Statement of Cash Flow
For the year ended 31st may, X2

| | Rs. | Rs. | |
|---|---|---|---|
| **Cash Flow from operating activities:** | | | |
| Profit before Tax | 880,000 | | **(0.5)** |
| **Adjustment from Non-Cash Item** | | | |
| Depreciation | 62,000 | | **(1)** |
| Profit on disposal Assets | (17,000) | | **(0.5)** |
| Cash Flows before working capital charges | 925,000 | | |
| **Working Capital Charges** | | | |
| Increase in Working Capital | (16,000) | | **(2)** |
| Cash generated from Operating Activities | | 909,000 | |

**Total Marks 04**

**Q.3.**

| **Branch Current Account** | | | | | |
|---|---|---|---|---|---|
| **1988** | | **Rs.** | **1988** | | **Rs.** |
| Jan 31 | Fixtures and fittings sent to branch **(1.5)** | 20,000 | Jan 31 | Returns from branch **(1.5)** | 3,300 |
| | Stock sent to branch **(1.5)** | 4,400 | | Remittances from branch **(1.5)** | 25,000 |
| | Bank account **(1)** | 1,000 | | | |
| Dec 31 | Goods to branch **(1.5)** | 33,000 | Jan 31 | Balance c/d **(1.5)** | 30,100 |
| | | 58,400 | | | 58,400 |

**Total Marks 10**

**Q.4.**

| | | |
|---|---|---|
| **i)** | Dr. Cash a/c XX | |
| | Cr. Branch current a/c XX | **(2)** |
| **ii)** | Dr. Goods from head office XX | |
| | Cr. Head office current a/c XX | **(2)** |
| **iii)** | Dr. Branch debtors a/c XX | |
| | Cr. Branch stock a/c XX | **(2)** |
| **iv)** | Dr. Branch P/L a/c XX | |
| | Cr. General P/L a/c XX | **(2)** |
| **v)** | Dr. Branch P/L a/c XX | |
| | Cr. Branch debtors a/c XX | **(2)** |

**Total Marks 10**

**Q.5. (a)**

| | Rs. | |
|---|---|---|
| Cost (1.1.1994) | 45,000 | |
| Accumulated Depreciation (45,000 x 2% x 15years) | (13,500) | (2) |
| Carrying Value 1.1.2009 | **31,500** | (1) |
| Valuation | 150,000 | (2) |
| Carrying Value at 1.1.2009 | (31,500) | |
| Revaluation Gain | **118,500** | (1) |

**06**

**Q.5. (b)** Depreciation charge for year ended 31.12.2009 = Rs. 150,000/35 = Rs. 4,286 **08**

Total Life $= \frac{1}{2} = 50$ years

Depreciation $= \frac{\text{FMV}}{\text{R. Life}} = \frac{150{,}000}{(50-15)} = 4{,}286$

**Total Marks 08**

**Q.6. (a)**

| | Rs. | Rs. | |
|---|---|---|---|
| Cost of Sales | | | |
| Opening Inventory | 45,678 | | |
| Purchases | 98,000 | | |
| Closing Inventory (W-1) | (42,130) | | |
| | | 101,548 | (2) |
| Closing Valuation | | 42,800 | (1) |
| Less Damaged Inventory: | | | |
| Table | 500 | | (1) |
| Chairs (100 x 4) | 400 | 900 | (1) |
| Add NRV: | | | |
| Table (200 – 50 ) | 150 | | (2) |
| Chairs (20 x 4) | 80 | 230 | (1) |
| | | 42,130 | |

**08**

**Q.7.**

**Extract to Statement of Financial Position**

| | School | Club |
|---|---|---|
| Due from Customer (4) | Rs.(000) | Rs.(000) |
| Cost to Date | 90 | 150 |
| Profit / (Loss) to date | 30 | (75) |
| Contract work in progress | 120 | 75 |
| Progress billings to date | (116) | (11) |
| | 4 | 64 |
| Receivables (2) | | |
| Progress Billings to date | 116 | 11 |
| Receipts to date | (116) | (11) |
| | 0 | 0 |

| Extract to Statement of Comprehensive Income (4) | | |
|---|---|---|
| Revenue (300 x 4%) (300 x 4%) | 120 | 120 |
| Cost of Revenue | (90) | (150) |
| Profit / (Loss) | 30 | (30) |
| Provision for onerous contract [180-225] | - | (45) |
| Net Profit / (Loss) | 30 | (75) |

**Total Marks 10**

**Q.8. a** **05**

| Income Statement and appropriation account for the year ended 31st December | | |
|---|---|---|
| | School | Club |
| | Rs.(000) | Rs.(000) |
| Profit from Operations | | 117,200 |
| Bank Interest | 700 (1) | |
| Interest on Loan from Saleem [40,000@ 5% x 6/12] | 1,000 (2) | (1,700) |
| Interest on Capital | Nil (0.5) | |
| Salaries | Nil (0.5) | |
| | | |
| Shares of profit | | |
| Hameed | 38,500 | |
| Saleem | 38,500 | |
| Qureshi | 38,500 (1) | |
| | | 115,500 |

**b** **04**

| | | | |
|---|---|---|---|
| **Hameed** | **(38500 + 22500)** | **61,000** | (1) |
| **Saleem** | **32,000 + 500 =** | **32,500** [38,500 + 1,000 - 7,000] | (2) |
| **Qureshi** | | **40,000** [38,500 + 1,500] | (1) |

**c** **05**

| | Hameed | Saleem | Qureshi | |
|---|---|---|---|---|
| | Rs. | Rs. | Rs. | |
| Original Balance | 3,500 | (6,250) | (14,250) | |
| Interest on capital | (5,000) | (5,000) | (5,000) | (1) |
| Salary | (18,000) | Nil | Nil | (1) |
| Original Profit | (41,500) | (20,750) | (20,750) | (1) |
| Revised Profit | 38,500 | 38,500 | 38,500 | (1) |
| Original Interest | | (500) | | |
| Revised Interest | | 1000 | | (1) |
| Revised Balance | (22,500) | 7,000 | (1,500) | |

**Total Marks 14**

**Q.9. a** **14**

| MIRA Limited<br>Statement of Comprehensive Income Year ended 31st December 2009 | |
|---|---|
| Revenue (1) | 193,500 |
| Cost of Sales (33,000 + 115,869 – 31, 869) (3) | (117,000) |
| **Gross Profit (1)** | 76,500 |
| Distribution Costs (1) | (12,597) |
| Administration Expenses (19,125 + 4,500 + 22,500 + 1,676) (4) | (47,801) |
| **Profit from Operation (1)** | 16,102 |
| Finance Costs (1) | 0 |
| **Profit before tax** | 16,102 |
| Income Tax (1) | (4,832) |
| **Profit for the Period** | 11,270 |
| Other Comprehensive Income: | |
| Gain on Investment (1) | 150,000 |
| **Total Comprehensive Income for the year** | 161,270 |

**b** **06**

| MIRA Limited<br>Statement of Changes in Equity year ended 31st December 2009 | | | | | |
|---|---|---|---|---|---|
| | **Ordinary Shares** | **Share Premium** | **Revaluation Reserve** | **Retained Earning** | **Total** |
| | Rs. | Rs. | Rs. | Rs. | Rs. |
| **Balance @ 01-01-2009** | 52,500 | 18,000 | 0 | 731,955 | 802,455 |
| Profit for the year | - | - | - | 11,270 | 11,270 |
| Dividends | - | - | - | (5,250) | (5,250) |
| **Shares issued** | 0 | 0 | - | - | - |
| Revaluation | - | - | 150,000 | - | 150,000 |
| **Balance @ 31-12-2009** | 52,500 (1) | 18,000 (1) | 150,000 (1) | 737,975 (2) | 958,475 (1) |

**c** **10**

| MIRA Limited<br>Statement of Financial Position as at 31st December 2009 | | |
|---|---|---|
| | **Ordinary Shares** | **Share Premium** |
| | Rs. | Rs. |
| **Non-Current Assets** | | |
| Tangible Assets (600,000 + 225,000 – 36,000 – 4,500 + 112,500 – 22,500 – 22,500 ) (3) | - | 852,000 |
| **Current Assets** | | |
| Inventory (0.5) | 31,869 | - |
| Trade Receivables (130,867 – 3,926) (1) | 126,941 | - |
| Bank (0.5) | 19,427 | |
| | | 178,237 |
| **Total Assets** | | 1,030,237 |

| | | |
|---|---|---|
| **Equity and Liabilities** | | |
| Ordinary Share Capital (0.5) | 52,500 | - |
| Share premium (0.5) | 18,000 | - |
| Retain Earnings (731,955 + 11,270 – 5,250) (2) | 737,975 | - |
| Revaluation Reserve (0.5) | 150,000 | - |
| Bank (0.5) | | 958,475 |
| **Non-Current Liabilities** | | 0 |
| **Current Liabilities** | | |
| Trade Payables (0.5) | 61,680 | |
| Taxation (0.5) | 4,832 | |
| Dividend payable (0.5) | 5,250 | |
| | | 71,762 |
| | | 1,030,237 |

**Total Marks 30**

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# Business Commn. & Report Writing

## (Level-3)

**Q.1.** **Wheel Network**: In this network, the leader is very important and powerful. He holds the central position and plays the key role to disseminate information. The primary communication occurs between the members and the group leader and then group leader shares the information with all. In wheel network, decisions can be made fast but group morale is low since subordinates do not take part in decision making. It is an example of centralized communication.

**Circle Network**: The circle network assumes no leader. There is complete equality. The members can communicate with persons to their right and left. Each member of the circle has the same authority or power to impact the group. The information moves rather slowly, and might get distorted; however, members' morale is high because everyone participates in the decision making process. It is an example of horizontal and decentralized communication.

**Total Marks 05**

**Q.2.** **Levels of information**

1. **Strategic**: Long-term decision making, e.g. 3-5 year plan including opening a new factory in 3 years' time.
2. **Tactical**: Short-term issues and opportunities, e.g. 1 year plan including switching a key supplier in 6 months' time.
3. **Operational**: Day to day activities, e.g. weekly ordering of new supplies.

**Total Marks 03**

**Q.3.** **Benefits of using emails include:**

- An audit trail of messages is automatically retained and can be consulted in future, if required.
- The sending and receiving of emails is virtually instantaneous anywhere in the world.
- Recipients can access emails anywhere and anytime at their convenience.
- Traditional and expensive mailshots to multiple recipients can be replaced by quicker and cheaper multi-recipient email communications.
- Easy to use and organize daily correspondence.
- Low cost.
- Environment friendly – doesn't use paper (unless the email is printed out).

**Total Marks 06**

**Q.4.** **The key points to consider in communicating a negative messages:**

i. **Use a buffer**: A buffer is a neutral or positive statement designed to soften the impact of the negative message. A good buffer makes the reader more receptive to the negative message.

ii. **Offer an explanation:** Offering of a sound reason prepares the ground for the reader to accept the refusal. Explanation includes giving convincing reasons why the matter must be handled differently from the expectations of the reader.

iii. **Avoid emphasizing the refusal**: The refusal message should not be over emphasized, although it should be clearly stated in the message.

iv. **Present an alternative or compromise**: Offering an alternative option would give the reader a different perspective and create an impression that the sender has a positive and helpful attitude.

v. **End with a positive statement:** The ending of an unfavorable message should be on an assuring and positive note with a reader-friendly closing.

**Total Marks 05**

**Q.5. The 'You' approach**

While communicating messages, the sender's focus on the recipient's benefits, needs, or interest is termed as 'you' approach. This approach suggests empathizing with the audience. This may stimulate a positive response from the audience.

**Consideration** in communication suggests adopting the 'you' approach.

**When to avoid using 'you' approach**

Using the 'you' approach is not always appropriate. The sender should avoid YOU in sensitive cases, for example, instead of saying: "While travelling on company's expense, you can't travel business class on short haul flights."

One could say: "While travelling on company's expense, you can travel business class on long haul flights".

The sender should avoid this approach when the receiver is at fault, for example, instead of saying: "You have not sent the report".

One could say: "The report was not received".

**Total Marks 06**

**Q.6. Factors affecting perception**

1. **Perceiver**: The characteristics of the perceiver, like attitudes, motives, interests, experience, expectations and beliefs affect the perception. For example, if one expects teachers to be mentors, old people to be forgetful, then he perceives them as such, irrespective of their actual traits. Similarly if one needs something, he/she will be attracted to that particular object, ignoring all other objects which, at the same time, may attract someone else.

2. **Target**: The characteristics of the object under focus may also affect the perception of the perceiver, e.g. individuals who are talkative are more likely to be noticed than those who are quiet; the objects that are moving will arrest attention as compared to the static ones; the bright colors are easily seen than the lighter ones.

- **Context:** The context in which we see the target also affects our perception, e.g. a person perfectly dressed up for a corporate meeting is normal but the same person attired for a cricket match with the same group of people would appear weird. Though the perceivers and target both are the same but the situation is different. Such situational factors might include; time, place, light, temperature, seasons, etc.

**Total Marks 09**

**Q.7. Purposes of interpersonal communication**

1. To learn: Interpersonal communication enables us to learn about others and ourselves—our strengths and our weaknesses.

2. To connect: Interpersonal communication helps to form significant connections which help overcome loneliness, depression and hopelessness.

3. To inspire: We inspire others, and others may inspire us; for example, Inspiring a friend to choose a career.

4. To support: We interact to help and support others, for example, consoling, comforting, and counseling others.

5. To play and enjoy: We often interact to seek pleasure or to enjoy. Such fun activities break monotony of a daily routine.

**Total Marks 05**

**Q.8.** The diagram depicts five basic conflict management Styles/Techniques, along with the degree of cooperation and assertiveness in each style.

i. **Avoiding:** It is also known as withdrawing where one party neither pursues its own concerns nor those of the opponent party. A party may recognise that the conflict exists but wants to either withdraw from it or suppress it. At this stage the cooperativeness as well as assertiveness of both parties is very low.

ii. **Competing:** In this strategy one party wins and the other loses. One party firmly pursues its concerns despite the resistance of the other party. Here the winner is very obvious and clear and ends up making gains out of the situation. At this stage the cooperativeness is low but assertiveness of dominating part is very high.

iii. **Accommodating:** It is also known as smoothing, it is about accommodating the concerns of the other party. Here one party loses or gives in to accommodate the other party. This practice encourages the other party and conflict situation is defused. It is self-sacrificing in nature. At this stage the cooperativeness of losing party is high while assertiveness of the winning party is high.

iv. **Compromising:** This strategy leads to a mutually acceptable solution that partially satisfies both the parties. This improves the relationship between both the parties. However none of the parties get what it actually wants, both sacrifice. There is no clear winner or loser. At this stage the cooperativeness and assertiveness of both parties are moderate.

v. **Collaboration:** Here both the parties enjoy win-win situation. It sees conflict as an opportunity to arrive at a mutually beneficial result. It identifies the principal concerns of the opponents and arrives at a solution that meets each party's concerns. At this stage the cooperativeness and assertiveness of both parties are high.

**Total Marks 10**

**Q.9.** **Informational meetings**: These meetings clarify the topic under discussion and provide information. In such meetings participants learn, ask questions and try to understand the information being provided. Here problems are not solved, no recommendations are made. Participants attend these meetings with the sole objective of being informed and assimilate the information, e.g. announcement of new mission statement.

**Suggested solution meetings**: Here the core purpose is to find suggested solution to some core issue. Recommendations are sought for and comments are made on the options recommended. Often no decision is made, and meeting tends to remain explanatory and informational. A final suggested solution is worked out and forwarded for approval either from higher authorities or is kept for overall group's consensus.

**Problem-solving meetings:** The purpose of these meetings is to work out some solution. The problem is presented, then suggested solutions are gathered; these recommendations are evaluated and then final decision is made for further action.

**Total Marks 06**

**Q.10.**

**a) Analytical Reports**

Analytical report analyses the facts, draws conclusions and makes recommendations. These reports are generally organized around logical arguments and conclusions. These reports contain analytical information in narrative form.

**b) Informational reports**

Informational report focuses on facts but do not offer any type of recommendations. These reports are organized around subtopics. These reports present information without any personal biases of the person creating them.

**c) Periodic reports:**

Periodic reports are prepared and submitted at regular, prescribed intervals. They may be submitted annually, semi-annually, quarterly, monthly, fortnightly, weekly or even daily. They are organized in a standard predefined way. Periodic/ routine reports discuss the performance of a department or division during a particular time period.

**d) Statutory reports**

These reports are prepared and presented according to the form and procedure laid down by law, e.g. Audit report. The structure and contents of these reports are determined by the related authorities. These reports are required by law and being unable to submit them with respected authorities would end up in legal consequences

**Total Marks 08**

**Q.11. (a)** 04

- Improved lower-cost technology with greater bandwidth.
- Wider variety of video conferencing tools available associated with increasingly more powerful PC's.
- Environment friendly IT initiatives such as reduced air travel.
- High travel costs combined with austerity related cost saving initiatives.

**(b)** **Social Networking:** 08
It refers to establishing communities of people through social network sites such as Facebook, Twitter, LinkedIn, Google+, etc.

**Practical use of Social Networking:**
**At Personal level**
The most general use of social networking sites, and the key reason for them existing in the first place, is for personal interests. For example, it is used for updating status, viewing friends' statuses, looking at photos, to connect to people who met lately, or being in touch with someone who shares the same interests, or to keep in touch with people thousands of miles away.

**At Business level**
There are social networking sites that are developed exclusively for the networking purposes within a business environment. For example, companies have a small team who run the Twitter feed as part of their overall Public Relations role. It provides efficient customer service. With the rise of internet marketing, social media is being used by businesses for updates, advertisements, recruitment process, etc.

**Total Marks 12**

**Q.12.** The report is an objective, planned presentation of facts. The Human Resource Manager should give a critical analysis of the situation which may get worse if not addressed promptly and prudently. The report should follow a proper format.

The report may follow a memo format. It may consist of the details discussed under the following headings:

- Term of Reference/Introduction
- Background
- Analysis of the current situation
- Findings
- Conclusion
- Recommendations

**Total Marks 13**

**Q.13.** It is a complaint letter which should state precisely the problem and request for the adjustment. The tone should reflect the urgency and seriousness of the matter. The language should be courteous.

The given complaint letter should follow the format of a formal letter. It may be written in the following order:
- Address of the sender (assumed)
- Date
- Address of the receiver (assumed)
- Salutation
- Subject line (optional)
- Paragraph 1: Thank the prompt delivery OR stating the business relation of both Organizations. Explaining briefly the problem.
- Paragraph 2: Details of the defects and the problem faced.
- Paragraph 3: requesting a prompt action and delivery of books. Courteous ending
- Complimentary close
- Enclosure (optional)

**Total Marks 12**

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# Taxation

## (Level-3)

**Q.1.** Federal taxes in Pakistan like most of the taxation systems in the world are classified into two broad categories, viz., direct and indirect taxes. A broad description regarding the nature of administration of these taxes is explained below:

**DIRECT TAXES**

**Income Tax**
Direct taxes primarily comprise of Income Tax. In the Income Tax Ordinance, 2001, tax is levied generally on the net income of a taxpayer earned during a tax year computed by applying the specified tax rates as applicable to respective taxpayer.

For the purpose of the charge of tax and the computation of total income, all income is classified under the following heads:

- Salary
- Income from property
- Income from business
- Capital gains; and
- Income from other sources

**Capital Value Tax**
Capital value tax on different transaction such as transfer of immoveable property, transfer of rights etc.

**INDIRECT TAXES**
Following are the indirect taxes under the Pakistani Taxation System.

**Custom Duty**
Goods imported and exported from Pakistan are liable to rates of customs duties as prescribed in Pakistan Customs Tariff. Customs duties in the form of import duties and export duties constitute a major part of the total tax receipts. The rate structure of customs duty is determined by a large number of socio-economic factors. However, the general scheme envisages higher rates on luxury items as well as on less essential goods. The import tariff has been given an industrial bias by keeping the duties on industrial plants and machinery and raw material lower than those on consumer goods.

**Federal Excise Duty**
Federal Excise duties are levied on a limited number of goods produced or manufactured, and services provided or rendered in Pakistan. On most of the items Federal Excise duty is charged on the basis of value or retail price. Some items are, however, chargeable to duty on the basis of weight or quantity. Classification of goods is done in accordance with the Harmonized Commodity Description and Coding system which is being used all over the world. All exports are liable to Zero per cent Federal Excise Duty.

**Sales Tax**
Sales tax is levied at various stages of economic activity @17 per cent on:

All goods imported into Pakistan, payable by the importers

All supplies made in Pakistan by a registered person in the course of furtherance of any business carried on by him.

There is an in-built system of input tax adjustment and a registered person can make adjustment of tax paid at earlier stages against the tax payable by him on his supplies. Thus, the tax paid at any stage does not exceed 17% of the total sales price of the supplies

**Total Marks 09**

**Q.2. (a)** **(i) Public Company** 04

Public company means:

a) A company in which not less than fifty per cent of the shares are held by the Federal Government or Provincial Government;

b) A company in which not less than fifty per cent of the shares are held by a foreign Government, or a foreign company owned by a foreign Government;

c) A company whose shares were traded on a registered stock exchange in Pakistan at any time in the tax year and which remained listed on that exchange at the end of that year; or

d) A unit trust whose units are widely available to the public and any other trust as defined in the Trusts Act, 1882 (II of 1882

**(ii) Profit on Debt** 02

Profit on a debt whether payable or receivable, means:

a) any profit, yield, interest, discount, premium or other amount owing under a debt, other than a return of capital; or

b) any service fee or other charge in respect of a debt, including any fee or charge incurred in respect of a credit facility which has not been utilized

**(iii) Non-Profit Organization** 03

Non-profit organization‖ means any person other than an individual, which is:

a) established for religious, educational, charitable, welfare or development purposes, or for the promotion of an amateur sport;

b) formed and registered under any law as a non-profit organization;

c) approved by the Commissioner for specified period, on an application made by such person in the prescribed form and manner, accompanied by the prescribed documents and, on requisition, such other documents as may be required by the Commissioner;

And none of the assets of such person confers, or may confer, a private benefit to any other person;

**(iv) Filer** 02

Filer means a taxpayer whose name appears in the active taxpayers' list issued by the Board from time to time or is holder of a taxpayer's card.

**Total Marks 11**

**Q.3.** **(i) Distributor** 02

Distributor means a person appointed by a manufacturer, importer or any other person for a specified area to purchase goods from him for further supply and includes a person who in addition to being a distributor is also engaged in supply of goods as a wholesaler or a retailer.

**(ii) Person** 03

Means:

a) an individual;
b) a company or association of persons incorporated, formed, organized or established in Pakistan or elsewhere;
c) the Federal Government;
d) a Provincial Government;
e) a local authority in Pakistan; or
f) a foreign government, a political subdivision of a foreign government, or public international organization

**(iii) Time of Supply** 04

In relation to:

a) a supply of goods, other than under hire purchase agreement, means the time at which the goods are delivered or made available to the recipient of the supply‖ 1[—or the time when any payment is received by the supplier in respect of that supply, whichever is earlier];
b) a supply of goods under a hire purchase agreement, means the time at which the agreement is entered into; and
c) services, means the time at which the services are rendered or provided;

Provided that in respect of sub clause ( a) ,(b) or (c), where any part payment is received, –

a) for the supply in a tax period, it shall be accounted for in the return for that tax period; and
b) in respect of exempt supply, it shall be accounted for in the return for the tax period during which the exemption is withdrawn from such supply.

**(iv) Similar Supply** 02

Similar supply, in relation to the open market price of goods, means any other supply of goods which closely or substantially resembles the characteristics, quantity, components and materials of the aforementioned goods.

**Total Marks 11**

**Q.4.** Any expenditure that provides an advantage or benefit for a period of more than one year is included in the definition of intangibles and is required to be amortized over the period of expected benefit or 10 years whichever is less.

As such ML would be allowed to charge only $1/10^{th}$ of the expense i.e. Rs.90,000 in tax year 2017.

**Bad debts**

Only those bad debts are allowed as admissible deductions which have previously been included in the taxpayer's business income chargeable to tax and on fulfillment of some more conditions.
Since the staff loan was not previously offered to tax as business income, it would not be admissible.

**Initial Allowance**

Initial allowance is only admissible on such plant and machinery which was not previously used in Pakistan.
Since in this case, the equipment was previously used in Pakistan, the initial allowance is not admissible.

**Vehicle on Finance Lease**

Entire lease rentals paid during the year, on leased assets, i.e. Rs.800,000 shall be allowed as admissible deduction.

Following expenditures however, would not be admissible:

| | |
|---|---|
| Finance charges | Rs.200,000 |
| Depreciation | Rs.400,000 |

**Total Marks 09**

**Q.5. Minimum tax on the income of certain persons.**

(1) This section shall apply to a resident company, an individual (having turnover of ten million rupees or above in the tax year 2017 or in any subsequent tax year and an association of persons (having turnover of ten million rupees or above in the tax year 2017 or in any subsequent tax year where, for any reason whatsoever allowed under this Ordinance, including any other law for the time being in force:

a) loss for the year;
b) the setting off of a loss of an earlier year;
c) exemption from tax;
d) the application of credits or rebates; or
e) the claiming of allowances or deductions (including depreciation and amortization deductions) no tax is payable or paid by the person for a tax year or the tax payable or paid by the person for a tax year is less than the percentage as specified in column (3) of the Table in Division IX of Part-I of the First Schedule of the amount representing the person‘s turnover from all sources for that year:

**Explanation**: For the purpose of this sub-section, the expression tax payable or paid does not include-

a) Tax already paid or payable in respect of deemed income which is assessed as final discharge of the tax liability under section 169 or under any other provision of this Ordinance; and
b) Tax payable or paid under section 4B.

(3) Where this section applies:

a) the aggregate of the person‘s turnover as defined in sub-section (3) for the tax year shall be treated as the income of the person for the year chargeable to tax;
b) the person shall pay as income tax for the tax year (instead of the actual tax payable under this Ordinance), minimum tax computed on the basis of rates as specified in Division IX of Part I of First Schedule;
c) where tax paid under sub-section (1) exceeds the actual tax payable under Part I, clause (1) of Division I, or Division II of the First Schedule, the excess amount of tax paid shall be carried forward for adjustment against tax liability under the aforesaid Part of the subsequent tax year:

Provided that the amount under this clause shall be carried forward and adjusted against tax liability for five tax years immediately succeeding the tax year for which the amount was paid.

**(4) Turnover means:**

a) the gross sales or gross receipts, exclusive of Sales Tax and Federal Excise duty or any trade discounts shown on invoices, or bills, derived from the sale of goods, and also excluding any amount taken as deemed income and is assessed as final discharge of the tax liability for which tax is already paid or payable;
b) the gross fees for the rendering of services for giving benefits including commissions; except covered by final discharge of tax liability for which tax is separately paid or payable;
c) the gross receipts from the execution of contracts; except covered by final discharge of tax liability for which tax is separately paid or payable; and
d) the company's share of the amounts stated above of any association of persons of which the company is a member.

**Total Marks 15**

**Q.6. (a) Association of Persons** 02

Association of Persons includes:

- a firm;
- a Hindu undivided family;
- any artificial juridical person and anybody of persons formed under a foreign law, but does not include a company. Define the term "Association of Persons' under Income Tax Ordinance, 2001.

**(b)Rules relating to residential status of AOP:** 02

An association of person is treated as tax resident for a tax year if the control and management of its affairs is situated wholly or partly in Pakistan at any time during that tax year.

**(c) Taxability of income of AOP, in the hands of its member** 03

a) The amount received by a member of the association in the capacity as member out of the income of the association shall be exempt from tax. However, such share of member is included in income of the member for determination of tax rate i.e. for rate purpose only.

b) If member(s) of an AOP is a company, the share of such company/ies shall be excluded for the purpose of computing the total income of the AOP and the company/ies shall be taxed separately at the rates applicable to the companies, according to their share.

**(d) Rules relating to set off and carry forward of losses of an AOP** 03

An AOP is entitled to set off and carry forward its losses against its income only. However, share of loss from AOP is neither adjustable against the income of its members nor it is considered for rate purpose.

**Total Marks 10**

**Q.7.** **(i) Conveyance** 02

"Conveyance" means any means of transport used for carrying goods or passengers such as vessel, aircraft, vehicle or animal etc.

**(ii) Franchise** 02

"Franchise" means an authority given by a franchiser under which the franchisee is contractually or otherwise granted any right to produce, manufacture, sell or trade in or do any other business activity in respect of goods or to provide service or to undertake any process identified with franchiser against a fee or consideration including royalty or technical fee, whether or not a trade mark, service mark ,trade name, logo, brand name or any such representation or symbol, as the case may be, is involved.

**(iii) Establishment** 02

"Establishment" includes an undertaking, firm or company, whether incorporated or not, an association of persons and an individual.

**Total Marks 06**

**Q.8.** **Sales tax payable for January 2017**

**Input tax**

| | |
|---|---|
| ➢ On purchases of Rs.2,000,000 from unregistered persons | 0 |
| ➢ On purchases of raw materials from registered persons: | |
| Purchases inclusive of sales tax Rs.8,190,000 | |
| Input tax (Rs. 8,190,000 x 100/117 = 7,000,000 x 17%) | 1,190,000 |
| Sales tax credit brought forward from December 2013 | 300,000 |
| **Input Tax** | **1,490,000** |

**Output tax**

**On taxable supplies**

| | |
|---|---|
| ➢ In local market to registered persons (Rs.4, 000,000 x 17%) [s.3(1)] | 680,000 |
| ➢ In local market to unregistered persons (Rs.6,000,000 x 17 %) [s.3(1A)] | 1,020,000 |
| ➢ Exported to Hong Kong (Rs.2,000,000 x 0%) | 0 |
| ➢ Given to an executive director (Rs.600,000 x 17%) | 102,000 |
| | 1,802,000 |
| Less sales tax on sales return from registered person (500,000 x 17%) | (85,000) |
| **Output Tax** | **1,717,000** |
| **Admissible input tax credit 90% of output tax** | |
| [Rs. 1,717,000 x 90% = 1,545,000) or input tax | |
| [Rs. 1,490,000] whichever lower [s.8B(1)] | (1,490,000) |
| Sales Tax Payable | 227,000 |
| Add: 2% Further Tax on Supplies to Un-Registered Person [6,000,000x2%] | 120,000 |
| **Sales Tax Payable for the month** | **347,000** |

**Total Marks 13**

**Q.9.** **Sarfraz Akram**

**Taxable income and tax payable for the tax year 2017**

| | |
|---|---|
| Basic salary ((360,000 – 36,000) x 12) [s. 12(2)(a)] | 3,888,000 |
| Medical allowance ((36,000 x 12)) | |
| [Fully taxable if Re-imbursement is Exempt] | 432,000 |
| Bonus payment [s. 12(2) (a)] | 720,000 |
| House rent allowance (120,000 x 12) [s. 12(2) (a)] | 1,440,000 |
| Perquisite representing the use of a car (Working 1) | 100,000 |
| Payment of medical expenses to a clinic on behalf of | |
| Sarfraz Akram [150,000-150,000] Exempt | -- |
| Perquisite of annual membership of Executive Club | |
| [s. 13(10) and (13)] | 400,000 |
| Encashment of earned leave | 280,000 |
| Perquisite on account of services of security guard | |
| ((40,000 x 12)/2) [s. 13(5)] | 240,000 |
| Income under the head 'salary'/assessable under the normal tax regime | 7,500,000 |
| *Less* deductible allowance | |
| Deductible allowance on account of profit paid on loan for the acquisition | |
| of the house [s.64A] (Working 2) | (500,000) |
| Taxable Income | 7,000,000 |
| Tax on taxable income (Up to Rs.7,000,000) | |
| [Para (1A) of Div. I of Pt. I of 1st Sch.] | 1,422,000 |
| *Less:* | |
| Tax credit on donation given to a school (Working 3) | (10,157) |
| Tax on taxable income under the normal law[NTR] | 1,411,843 |
| Tax on income assessable under the final tax regime (FTR): | |
| Tax on winning first prize in quiz competition (Working 4) | 400,000 |
| Total tax payable | 1,811,843 |
| Tax already paid: | |
| Tax deducted by employer (ISL) at source [s.149] | 600,000 |
| Tax deducted from prize money [s.156] | 400,000 |
| | (1,000,000) |
| Tax payable with return/statement of FTR | 811,843 |

**Explanation of items not included in the computation of taxable income/tax credit**

**Agricultural income of Rs.800,000.**

Agricultural income is not taxable under the Income Tax Ordinance, 2001 (the 'Ordinance'). Similarly, provincial agricultural tax paid is not to be deducted from the tax liability under the Ordinance.

**Workings**

**Working 1**

Where a car is provided for personal as well as business use, 5% of the cost of the car accrued to ISL is treated as salary income on account of this perquisite. The value of the car on 30 June 2017 is irrelevant.

| | |
|---|---|
| Purchase Cost | 2,000,000 |

5% to be treated as the value of the perquisite (2,000,000 x 5%) 100,000 [s.13(3) read with rule 5 of the Income Tax Rules, 2002]

**Working 2**

| | |
|---|---|
| Taxable income | 7,000,000 |
| Maximum ceiling in terms of 50% of taxable income | 3,500,000 |
| Maximum ceiling in absolute terms | 2,000,000 |

Since the amount of profit paid by Sarfraz at Rs.500,000 does not exceed either of the limits at (a) or (b) above, the full amount is allowable as a deductible allowance. [s.60C]

**Working 3**

| | |
|---|---|
| Taxable income | 7,000,000 |
| Tax on taxable income | 1,422,000 |
| Donation paid | 50,000 |

Since the tax donation paid at Rs.50,000 is less than the ceiling of 30% of taxable income, a tax credit is allowable on the full amount of Rs.50,000 at the average rate of tax, i.e. (1,422,000/7,000,000) x 50,000=10,157

**Working 4**

The prize money won from the quiz competition is taxable under the final tax regime (FTR).

| | |
|---|---|
| The prize money including tax (1,600,000 + 400,000) | 2,000,000 |
| No expense is allowable against this income, hence the gross amount is chargeable to tax at 20% [s.156] | 400,000 |

**Total Marks 16**

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# Financial Reporting

## (Level-4)

**Q.1.** **Journal entries**

| | Debit | Credit |
|---|---|---|
| At start of first year | Rs. (000) | Rs. (000) |
| Right to use asset account (4,095+150) | 4,245 | |
| Lease liability account | | 4,095 |
| Bank account | | 150 |
| Recognition of lease in the books of lessee | | |
| At the end of first year | | |
| Depreciation account (4,245/5) | 849 | |
| Accumulated depreciation account | | 849 |
| Recognition of depreciation on right to use asset | | |
| Interest expense | 512 | |
| Lease liability | | 512 |
| Recognition of interest expense on lease | | |
| Lease liability account | 1,150 | |
| Maintenance cost account | 100 | |
| Bank account | | 1,250 |
| Payment of lease rental and maintenance cost | | |

**Workings**

**W – 1 Allocation of transaction price**

| | Leasing Rs. (000) | Services Rs. (000) |
|---|---|---|
| Fair value of asset/services [100 x 5] | 5,500 | 500 |
| [5,500/6,000]x100=92%, [500/6,000] x 100=8% | | |
| Rental allocated as: - [1,250 x 92%], [1,250 x 8%] | 1,150 | 100 |

**W – 2 Lease repayment schedule**

| Date Year | Opening Rs. (000) | Interest Rs. (000) | Receipt Rs. (000) | Closing Rs. (000) |
|---|---|---|---|---|
| 1 | 4,095 | 512 | (1,150) | 3,457 |
| 2 | 3,457 | 432 | (1,150) | 2,739 |
| 3 | 2,739 | 342 | (1,150) | 1,931 |
| 4 | 1,931 | 241 | (1,150) | 1,022 |
| 5 | 1,022 | 128 | (1,150) | -- |

**W – 3 Present value of lease payments**

PV = Annuity factor x rental + discount factor x guaranteed residual value

PV = 3.56 x 1,150 = 4,095

**Total Marks 15**

**Q.2.** **Tax expense**

| | Rs. (000) |
|---|---|
| Current tax (1,081.65+2.5) | 1,084.15 |
| Deferred tax | 425.20 |
| | 1,509.35 |

**Workings: -**

| **Working – 1** | Rs. (000) |
|---|---|
| Profit before tax | 5,360 |

| | |
|---|---|
| Add: - accounting depreciation | 2,000 |
| Provision for doubtful debts | 325 |
| Gratuity expense | 571 |
| | 8,256 |
| Less: -tax depreciation | (1,500) |
| Bad debts written off | (125) |
| Dividend income | (20) |
| Gratuity paid | (365) |
| Capital gain | (340) |
| Taxable profit for the year | 5,906 |
| Un-used tax losses brought forward | (2,300) |
| Net taxable profit for the year | 3,606 |
| Current tax @ 30% | 1,081.80 |
| Minimum Tax | 0.15 |
| | 1,081.65 |

**Working – 2 Calculation of Deferred Tax**

| Particulars | Taxable temporary differences | Deductible temporary differences | Deferred tax |
|---|---|---|---|
| **2016** | **Rs. (000)** | **Rs. (000)** | **Rs. (000)** |
| Depreciation | 2,500 | | 775.0 |
| Provision of doubtful debts | | 250 | (77.5) |
| Gratuity payable | | 650 | (201.5) |
| Un-used tax losses | | 2,300 | (713.0) |
| Net deferred tax liability | 2,500 | 3,200 | (217) |
| Deferred tax asset | | | (217.0) |
| Un-used tax credit | | | (150.0) |
| | | | (367.0) |
| **2017** | | | |
| Depreciation | 2,000 | | 600.0 |
| Provision of doubtful debts | | 450 | (135) |
| Gratuity payable | | 856 | (256.8) |
| Net deferred tax liability | 2,000 | 1,306 | 208.2 |

**Reconciliation**

| | |
|---|---|
| Tax on accounting profit | Rs. 1,608.0 |
| Tax expense | Rs. 1,509.5 |
| Effect of capital gain | Rs. 102.0 |
| Effect of dividend income (20x17.5%) | Rs. 3.5 |
| Effect of change in tax rate (700x1%) | Rs. (7.0) |
| Tax on accounting profit | Rs. 1,608.0 |

**Total Marks 14**

# Winter Exam-2017
# Solutions – Financial Reporting

**Q.3. Parent Consolidated Statement of Financial Position**
**As at June 20, 2017**

| | Rs. (000) | Rs. (000) |
|---|---|---|
| Assets - Non-current assets | | |
| Property, plant and equipment (7,200+4,635) | 11,835 | |
| Development | 450 | |
| Goodwill | 3,650 | 15,935 |
| Current asset | | |
| Inventory (4,035+2,035+465-100) | 6,435 | |
| Receivables (1,440+3,545) | 4,985 | |
| Cash and bank balances | 75 | 11,495 |
| | | 27,430 |
| Equity and liabilities | | |
| Equity –ordinary share capital | 10,000 | |
| Consolidated retained earnings [-400+5,689+1,913) | 7,202 | 17,202 |
| Non-controlling interest [-60+1,157+591) | | 1,688 |
| | | 18,890 |
| Current liabilities | | |
| Trade payables [3,440+3,100) | 6,540 | |
| Tax payable [935+1,065] | 2,000 | 8,540 |
| | | 27,430 |



**Parent Consolidated Statement of Comprehensive Income**
For the year ended June 30, 2017

| | Parent Rs. (000) | Subsidiary Rs. (000) | Adjustments Rs. (000) | Consolidated Rs. (000) |
|---|---|---|---|---|
| Operating profit | 3,688 | 2,632 | 365 | 6,685 |
| Dividend from subsidiary | 240 | -- | (240) | -- |
| Profit before tax | 3,928 | 2,632 | 125 | 6,685 |
| Tax expense | (263) | (142) | -- | (405) |
| Profit after tax | 3,665 | 2,490 | 125 | 6,280 |
| Attributable to NCI(2,490+465)X20% | | | | 591 |
| Attributable to group | | | | 5,689 |

**Workings**

**W – 1 Goodwill**

| | Rs. (000) | Rs.(000) |
|---|---|---|
| Investment | | 6,000 |
| Fair value of NCI | | 950 |
| | | 6,950 |
| Subsidiary net assets | | |
| Share capital | 4,000 | |
| Retained earnings [250+1,000] | (1,250) | 2,750 |
| Goodwill | | 4,200 |
| Impairment loss | | (550) |
| Net goodwill | | 3,650 |

**W –2 Consolidated retained earnings –opening**

| | |
|---|---|
| Parent [4,350+400-3,665] | 1,085 |
| Subsidiary share of post-acquisition profit | 828 |
| | 1,913 |

| **W – 3 Subsidiary retained earnings – opening** | **Pre** | **Post** |
|---|---|---|
| Balance [2,525+300-2,490] | (250) | 585 |
| Fair value loss | (1,000) | 1,000 |
| Impairment loss | | (550) |
| | (1,250) | 1,035 |

**W –4 Non-controlling interest**

| | |
|---|---|
| Fair value | 950 |
| Share of post-acquisition profits [1,035 x 20%] | 207 |
| | 1,157 |

**W –5 Journal entries**

| | | |
|---|---|---|
| Profit or loss account | 240 | |
| NCI | 60 | |
| Dividend of subsidiary | | 300 |
| Closing stock | 465 | |
| Cost of sales | | 465 |
| Sales | 1,500 | |
| Cost of sale s | | 1,500 |
| Cost of sales | 100 | |
| Closing stock | | 100 |

**Total Marks 27**

**Q.4.** **Statement of financial position**

| | **Year 2 Rs. (000)** | **Year 1 Rs. (000)** |
|---|---|---|
| Assets | | |
| Contract asset [720+90+86] | -- | 896 |
| Retained earnings | 394 | 246 |

| **Statement of comprehensive income** | **Year 2 Rs. (000)** | **Year 1 Rs. (000)** |
|---|---|---|
| Sales | -- | 1,620 |
| Services income (180/2) | 90 | 90 |
| Less: - cost of sales [1,500+50] | (50) | (1,550) |
| | 40 | 160 |
| Interest income [1,620 – 900]x12%, [720+90+86]x12% | 108 | 86 |
| Profit for the year | 148 | 246 |

**Journal entries**

| | | |
|---|---|---|
| **Year – 1 –start** | | |
| Contract asset/receivable account | 1,620 | |
| Sales | | 1,620 |
| Recognition of sales | | |
| Bank account | 900 | |
| Contract asset/receivable account | | 900 |
| **Year – 1 –end** | | |
| Contract asset/receivable account | 90 | |
| Services income account | | 90 |
| Recognition of services income | | |
| Contract asset/receivable account | 86 | |
| Interest income account | | 86 |
| **Year – 2 end** | | |
| Contract asset/receivable account | 90 | |
| Services income account | | 90 |
| Recognition of services income | | |
| Recognition of services income | 108 | |
| Interest income account | | 108 |
| Bank account [896+90+108] | 1,094 | |
| Recognition of services income | | 1,094 |
| Recognition of receipt from customer | | |

Workings

| | |
|---|---|
| **W – 1 Allocation of transaction price** | |
| Computers [1,800x1,800]/2,000 | 1,620 |
| Maintenance services [200x1,800]/2,000 | 180 |

**Total Marks 14**

**Q.5.** **a)** Under IAS – 2 Inventory, stock should be measured at lower of cost or net realizable value. The cost of inventory is measured under absorption costing method and production overheads are part and parcel of cost of inventory. Therefore, firs the overheads will be added to determine the cost of inventory and then compared with the cost of inventory. As after adding the overheads cost of inventory is higher than the net realizable value, it should be written down by Rs. 1.5 million to get the value of inventory.

**b)** IAS – 37 Provisions, contingent liabilities and contingent assets, requires provision will be recognized if there is present obligation as result of past obligating event, probable outflow of the entity and amount is reliably measure then the provision will be recognized. As there is a possible chance that the entity will be held responsible therefore, provision cannot be recognize only a disclosure will be made in the financial statements.

**c)** The opening retained earnings of the current year will be reduced by Rs. 4.5 million as well as the cash balance. There will be no effect on taxation as it is not an allowable expense. However, the previous year will not be restated and the disclosure regarding impracticable situation will be given under IAS – 8 Accounting policy, change and accounting estimates and errors.

**Total Marks 15**

**Q.6.** **a)** Identification of reportable segment under IFRS – 08 Operating segment

| Criteria 10% | Calculation | Result |
|---|---|---|
| **Revenue** | | |
| Cement | [15,780/(17,015+63,741)]x100 | |
| | (15,780/80,756)x100=20% | Reportable |
| Pharmaceutical | (18,516/80,756)x100=23% | Reportable |
| Paint | (19,900/80,756)x100=25% | Reportable |
| Fertilizer | (20,655/80,756)x100=26% | Reportable |
| Chemical | (5,905/80,756)x100=7% | Not Reportable |
| **Asset** | | |
| Cement | (17,256/33,023)x100=52% | Reportable |
| Pharmaceutical | (4,685/33,023)x100=14% | Reportable |
| Paint | (5,256/33,023)x100= 16% | Reportable |
| Fertilizer | (4,568/33,023)x100=14% | Reportable |
| Chemical | (1,258)/33,023)x100=4% | Not Reportable |
| **Profit / (loss)** | | |
| Cement | (2,581/10,035)x100=26% | Reportable |
| Pharmaceutical | (3,457/10,035)x100=34% | Reportable |
| Paint | (2,820/10,035)x100=28% | Reportable |
| Fertilizer | (6,578/10,035)x100=66% | Reportable |
| Chemical | (635/10,035)x100=6% | Not Reportable |

**Criteria 75%**

| | | |
|---|---|---|
| External revenue of reportable segments | 10,525+13,256+15,650+20,655=60,086 | |
| Total external revenue | 63,741+1,520=65,265 | |
| % | (60,086/65,265)x100=92% | Satisfied |

So, chemical segment is not Reportable segments

**b)** Disclosure in the financial statements for reportable segments

| **Particulars** | **Reportable segments** | | | | **Un-allocated** | **Others** | **Adjustments** | **Total** |
|---|---|---|---|---|---|---|---|---|
| | **Cement** | **Pharmaceutical** | **Paint** | **Fertilizer** | -- | -- | | |
| Revenue | 15,780 | 18,516 | 19,900 | 20,655 | 1,520 | 5,905 | (17,015) | 65,261 |
| Operation profit | 2,581 | (3,457) | 2,820 | (6,578) | 1,560 | 635 | -- | (2,439) |
| Asset | 17,256 | 4,685 | 5,256 | 4,568 | 10,550 | 1,258 | -- | 43,573 |
| Liabilities | 15,652 | 2,568 | 4,659 | 2,652 | 5,350 | 5,656 | -- | 36,537 |

**Total Marks** **15**

# Management Accounting

(Level-4)

**Q.1. Following are the limitations of management accounting:**

1. It is concerned with Financial and Cost Accounting. If these records are not reliable, it will affect the effectiveness of Management Accounting.
2. Decisions taken by the Management Accountant may or may not be executed by the Management.
3. It is very expensive. Only big concerns can adopt this method of accounting.
4. New rules and regulations are to be framed; hence there is a possibility of opposition from the employees.
5. It is only in the developing stage.
6. It provides only data and not decisions.
7. It is a tool to the management and not an alternative of management.
8. Management Accounting System has to be implemented in full otherwise will not give meaningful results.
9. Need a full time management Accountant along with staff members to implement and analyze results which could be beneficial for the organization.

**Total Marks 05**

**Q.2.**

| | | (Rs.) |
|---|---|---|
| **a)** | Sales | 612,500 |
| | Less allowance for doubtful account | (6,125) |
| | Less increase in trade account receivable during month | (17,500) |
| | Increase in Creditors | 5,000 |
| | Estimated September Cash Receipt from operations | **593,875** |
| **b)** | Marketing, general, and administrative expenses: | |
| | Fixed (62,125 - 35,000 ) | 27,125 |
| | Variable [ (612,500 x 15% )- (6,125)] | 85,750 |
| | Cost of goods sold (612,500 x 70%) | 428,750 |
| | Increase in inventory during month | 8,750 |
| | Estimated September Cash Disbursement | **550,375** |

**Total Marks 15**

**Q.3. (a)** The relevant cost of Keowhite to be utilized in producing the special order is Rs. 220,000 plus 7,500 x 24 = Rs. 400,000. This is the opportunity cost foregone in using the chemical. **05**

**(b)** Comments on each number: **05**

**(i)** For material in stock (12,500kg) Only Rs. 220,000 is relevant as it is sales value that company will forego if it uses the chemical.

**(ii)** The book value comes to Rs. 250,000 (12,500 kgs x Rs. 20/kg). This is irrelevant in the decision making being Sunk Cost.

**(iii)** The current purchase cost of material in stock is Rs. 300,000 (12,500 kgs x Rs. 24 per kg). This is also irrelevant since company will not purchase Keowhite of 12,500 kgs.

**(iv)** The company has to purchase 7,500 kgs of Keowhite so has to pay the current purchases cost, which is (7,500 kgs x Rs.24) Rs. 180,000.

**Total Marks 10**

**Q.4. (a) (i)** Contribution-margin ratio $= \dfrac{\text{Unit Contribution Margin}}{\text{Unit Sales Price}}$ **04**

$= \dfrac{\text{Rs. } 120 - \text{Rs. } 60}{\text{Rs. } 120} = 0.5$

**(ii)** Contribution margin per unit = Rs. 120 – Rs. 60 = Rs. 60 **04**

**(iii)** Break-even point (in sales rupees) $= \dfrac{\text{Fixed Expenses}}{\text{Contribution Margin Ratio}}$ **04**

$= \dfrac{\text{Rs. } 160{,}000}{0.5} = \text{Rs. } 320{,}000$

Break-even point (in units) $= \dfrac{\text{Fixed Expenses}}{\text{Unit contribution margin}}$

$= \dfrac{\text{Rs. } 160{,}000}{\text{Rs. } 120 - \text{Rs. } 60} = 2{,}667$ Milk Power Packs

**(iv)** Safety Margin (%) $= \dfrac{3{,}600 - 2{,}667}{3{,}600} \times 100 = 26\%$ **04**

**(b)** Let X denote the sales volume of Milk Power Packs required to earn a target net profit of Rs. 4,000,000. **04**

Rs. 120X – Rs. 60X – Rs. 160,000 = Rs. 400,000

Rs. 60X = Rs. 560,000

X = 9,333 Milk Power Packs

**Total Marks 20**

**Q.5.** **04**

| | Company – A | Company – B | Company – C | Company – D |
|---|---|---|---|---|
| **Sales Revenue** | **480,000,000** | 240,000,000 | **120,000,000** | 110,000,000 |
| **Variable Expenses** | 240,000,000 | **225,000,000** | 40,000,000 | 20,000,000 |
| **Total Contribution Margin** | **240,000,000** | 15,000,000 | 80,000,000 | **90,000,000** |
| **Fixed Expenses** | 20,000,000 | **15,000,000** | **30,000,000** | **40,000,000** |
| **Net Income** | **220,000,000** | **0** | 50,000,000 | 50,000,000 |
| **Break-Even Sales Revenue** | 40,000,000 | 240,000,000 | **45,000,000** | **48,888,889** |
| **Capital Employed** | 880,000,000 | 100,000,000 | 300,000,000 | **250,000,000** |
| **ROCE** | 25% | 0% | 17% | 20% |

**Explanatory notes for selected items:**

| | (Rs.) |
|---|---|
| Break-even sales revenue | 40,000,000 |
| Fixed expenses | 20,000,000 |
| Variable expenses | 20,000,000 |

Therefore, variable expenses are 50 percent of sales revenue.

When variable expenses amount to Rs. 240,000,000, sales revenue is Rs. 480,000,000.

Rs. 240,000,000 is the break even sales revenue as well as actual sales revenue, so fixed expenses must be equal to the contribution margin of Rs. 15,000,000 and profit must be zero.

Rs. 45,000,000 = Rs. 30,000,000 / 0.6667 , where 2/3 is the contribution-margin ratio.

Rs. 48,888,889 = Rs. 40,000,000/0.81818, where 0.82 is the contribution-margin ratio.

**Comments on performance:**

Company A has a net profit of Rs. 220 million which is highest among all the four companies. It also has an ROCE of 25% which is also the highest.

Company B has nil net profit and 0% ROCE.

Company C has 50 million Net Profit and an ROCE is 17%

Company D has 50 million Net Profit and an ROCE is 20%
Based on the above results company A from textile sector is performing the best.

**Total Marks 15**

**Q.6.** The analysis by Beenish is wrongly prepared. The correct statement would be as below:

| | | (Rs.) | (Rs.) |
|---|---|---|---|
| Sales Revenue | | | 50,000,000 |
| Less: Cost of food (corrected) | | | 25.000,000 |
| Gross profit | | | 25,000,000 |
| Less: | Operating expenses | | |
| | Wages office | 5,000,000 | |
| | Electricity | 2,000,000 | |
| | Depreciation of equipment and furnishings | 2,000,000 | |
| | Selling Expenses | 2,500,000 | |
| | Total | | 11,500,000 |
| Profit | | | 13,500,000 |
| Add Depreciation | | | 2,000,000 |
| Cash Profit | | | **15,500,000** |

Notes:

**(1)** The income statement not correctly prepared by Beenish. She has shown a loss of Rs. 4 million, whereas actually there is cash profit of Rs. 15.5 million.

**(2)** Cost of food was not correct. The Beenish's Mother used Rs. 5 million worth purchases, these should be excluded.

**(3)** The allocated costs should also be excluded like depreciation of building Rs. 3 million because it will be incurred regardless of whether business is operated or not.

**(4)** Wages of Rs. 1.0 million (mother's servant) is not a business expense, hence should be excluded. Similarly home electricity expense of Rs. 0.5 million is a personal expense and should not be charged to business.

**(5)** The Drawings of Beenish Rs. 3.0 million also needs to be excluded and debited to her drawings account.

**(6)** Similarly Rs. 2.0 million relating to depreciation of Beenish house should be excluded.

**(7)** Beenish wrongly charged depreciation Rs. 3.0 million on Land which is conceptually wrong, hence should be excluded.

After above adjustments the cash profit comes to Rs. 15.5 million and there is no loss. Therefore, no need to outsource it at price of Rs. 10.0 million since present profit of Rs. 15.5 million is greater than that.

**Total Marks 20**

# Winter Exam-2017

## Solution - Management Accounting

| Type of Cash Flow | 2017 | 2018 | 2019 | 2020 | 2021 | 2022 | 2023 | 2024 | 2025 | 2026 |
|---|---|---|---|---|---|---|---|---|---|---|
| **(1) Construction of clinic** | (8,000,000) | (5,000,000) | | | | | | | | |
| **(2) Equipment purchased** | | (1,000,000) | | | | | | | | |
| **(3) Staffing** | | | (1,600,000) | (1,600,000) | (1,600,000) | (1,600,000) | (1,600,000) | (1,600,000) | (1,600,000) | (1,600,000) |
| **(4) Other operating costs** | | | (500,000) | (500,000) | (500,000) | (500,000) | (500,000) | (500,000) | (500,000) | (500,000) |
| **(5) Donations** | | | 1,000,000 | 1,000,000 | 1,000,000 | 1,000,000 | 1,000,000 | 1,000,000 | 1,000,000 | 1,000,000 |
| **(6) Patient Fee** | | | 4,500,000 | 4,500,000 | 4,500,000 | 4,500,000 | 4,500,000 | 4,500,000 | 4,500,000 | 4,500,000 |
| **(7) Equipment Purchased** | | | | | | (2,000,000) | | | | |
| **(9) Salvage value - Equipment** | | | | | | 400,000 | | | | |
| | | | | | | | | | | |
| **Incremental cash flow** | (8,000,000) | (6,000,000) | 3,400,000 | 3,400,000 | 3,400,000 | 1,800,000 | 3,400,000 | 3,400,000 | 3,400,000 | 3,400,000 |
| | x | x | x | x | x | x | x | x | x | x |
| **Discount factor*** | 1.000 | 0.909 | 0.826 | 0.751 | 0.683 | 0.621 | 0.564 | 0.513 | 0.467 | 0.424 |
| **Present value** | (8,000,000) | | | 2,553,400 | | | | | | |
| **Net present value** | | (5,454,000) | 2,808,400 | **2,039,000** | 2,322,200 | 1,117,800 | 1,917,600 | 1,744,200 | 1,587,800 | 1,441,600 |

**The proposal of establishing hospital / clinic is viable as it is giving positive NPV of Rs. 2,041,752. Therefore, the project should be taken up.**

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# Audit, Assurance & Ethics

(Level-4)

**Q.1 (a)** 1 mark for identifying that scope limitation exists. 03

1 mark for justifying that the matter is material but not pervasive.

1 mark for identifying that qualified opinion should be expressed in this case.

In this scenario, the auditors are unable to physically inspect the inventory. As the controls over inventory are considered to be weak, the auditors cannot rely on entity's controls. If the auditor is unable to obtain sufficient and appropriate audit evidence from alternate sources, this will constitute a scope limitation.

The amount of Rs. 1.5 million is material as it represents 27% of profit before tax and 8.3% of net assets.

Therefore, a qualified opinion will be appropriate in these circumstances.

**(b)** 1 marks for identifying that the modification has been drafted for material misstatement and not for scope limitation which exists in the given scenario. 04

2 marks for identifying that the draft audit opinion is not in accordance with the form recommended by ISA, as the basis of modification paragraph has been merged with the opinion paragraph.

1 mark for identifying wrong headings used.

**(c)** 1 marks for using correct headings for Basis for Qualified Opinion and Qualified Opinion paragraph. 04

2 mark for explaining why auditors were unable to obtain sufficient and appropriate evidence.

1 mark for expressing the correct opinion: "In our opinion, except for the possible effects of the matter described in the Basis for Qualified Opinion paragraph, the financial statements present fairly, in all material respects …. in accordance with International Financial Reporting Standards.

**Total Marks 11**

**Q.2** 2 marks for identifying the assurance services provided – "audit" and "review"

6 marks for comparison between audit and review.

| Audit | Review |
|---|---|
| An audit provides a high, but not absolute, level of assurance | Provide a moderate level of assurance |
| An external audit provides positive assurance that, in the opinion of the auditors, the financial statements do present fairly the financial position and performance of the company. | Negative assurance is an opinion that 'nothing has come to our attention to suggest that the information is misstated'. |
| more time-consuming than a review | Less time-consuming. |
| More costly than a review. | Less costly. |
| Requires extensive procedures to be performed | Procedures performed mainly consists of use of inquiry, observation and analytical procedures. |

**Total Marks 08**

**Q.3** **(a)** 1 mark for each factor 04

When deciding whether he needs to use an expert to assist him in obtaining sufficient appropriate evidence, the auditor should consider such factors as:

- The nature, significance and complexity of the matter
- The risk of material misstatement
- The availability of alternative sources of audit evidence.
- Whether management has used a management's expert

**(b)** 2 marks for identifying the need for further work to be performed by the expert and the auditor. 04

2 marks for identifying the impact on auditor's report

**(c)** If the auditor determines that the work performed by the auditor's expert is not adequate, the auditor shall: 03

- Agree with that expert on the nature, timing and extent of further work to be performed by the expert
- Perform additional audit procedures appropriate in the circumstances

If the auditor concludes that the work of the auditor's expert is not adequate for the auditor's purposes and the auditor cannot resolve the matter through the additional audit procedures it will be considered as a scope limitation and the auditor shall express modified opinion if the impact is material, or disclaim the opinion if the impact is both material and pervasive.

The examples of Financial Statement areas where the work of an input might be necessity are:

i. Valuation of property
ii. Valuation of property Liabilities
iii. Valuation of property for Taxation
iv. Valuation of property for Litigation

**Total Marks 11**

**Q.4** **(a)** 2 marks for discussion of rights of retiring auditor 03
1 mark for discussion of duties of retiring auditor

**<u>Rights of the Retiring Auditor</u>**

- Retiring auditor may make a representation in writing to the company not exceeding a reasonable length and requests its communication to the members of the company.
- If a copy of the representation is not sent as aforesaid because it was received too late or because of the company's default, the auditor may, without prejudice to his right to be heard in person, require that the representation shall be read out at the meeting

**<u>Duties of Retiring Auditor</u>**

- The retiring auditor shall file with the Institute a copy of the statement which he may have sent to the proprietors/Board of Directors of the Company for circulation among the shareholders

**(b)** 1 mark for each procedure identified 04
**The retiring auditor should:**

- Ensure that the current auditor (if any) has resigned from the audit in a proper manner, or has been removed from office in accordance with any appropriate local legislation.

- Ensure that its appointment is valid in law and is properly documented
- Prepare and submit an engagement letter to the board of the new client
- Obtain clearance from the institute before accepting the engagement

**(c)** Engagement documentation is the property of the firm. The firm may, at its discretion, make portions of, or extracts from, engagement documentation available to clients, provided such disclosure does not undermine the validity of the work performed, or, in the case of assurance engagements, the independence of the firm or its personnel. 02

**Total Marks 09**

**Q.5. (a)** 1 mark for explaining the term 03
2 marks for giving examples (up to 1 mark for each)

The term 'expectation gap' refers to the fact that the public perception of the role and responsibilities of the external auditor is different from his statutory role and responsibilities. Some examples of the misunderstandings inherent in the public's expectations are as follows:

- The public believes that the audit opinion in the audit report amounts to a 'certificate' that the financial statements are correct and can be relied upon for all decision-making purposes, including decisions about takeovers.
- The public also believes that the auditor has a duty to prevent and detect fraud and that this is one reason for an audit.
- The public assumes that, in carrying out his audit work, the auditor tests 100% of the transactions undertaken during the accounting period.

**(b)** 1 mark for explaining that auditor tests transactions on sample basis 03

1 mark for identifying that auditor is not responsible for the prevention or detection of fraud and that it is primarily the responsibility of management to establish systems and controls to prevent or detect fraud (and errors).

1 mark for explaining that the Auditor is responsible for obtaining reasonable assurance that the financial statements taken as a whole are free from material misstatement, whether caused by fraud or error.

**(c)** 1 mark for each factor identified: 05

- Its cost. The cost of an audit can be very high
- Some items might be estimates whose truth and fairness will not be known with certainty until some point in the future.
- Most fraud will include an attempt to deliberately conceal the truth or misrepresent information.
- In order to balance cost and efficiency the auditor routinely uses sampling rather than tests every item.
- Irrespective of how robust a client's systems are they will always incorporate some degree of inherent limitation.
- Audit evidence is persuasive rather than conclusive, i.e, they persuade the auditor to believe that a particular assertion has been justified instead of providing a conclusion

**Total Marks 11**

**Q.6.** 2 marks each for positive and negative confirmation 04

**(a)** Positive confirmation: A request that the confirming party respond directly to the auditor indicating whether the confirming party agrees or disagrees with the information in the request, or providing the requested information.

Negative confirmation request – A request that the confirming party respond directly to the auditor only if the confirming party disagrees with the information provided in the request.

**(b)** 1 mark for each reason 03

Negative confirmation provides less persuasive evidence than positive confirmation.

- The failure to receive a response to a negative confirmation request does not explicitly indicate receipt by the intended confirming party of the confirmation request or verification of the accuracy of the information contained in the request - Debtor may have ignored the confirmation request or the debtor might have not received the confirmation request.
- Confirming parties also may be more likely to respond indicating their disagreement with a confirmation request when the information in the request is not in their favor, and less likely to respond otherwise.
- If no reply is received, there is no explicit audit evidence.

**(c)** 1 mark for each step. 05

In the case of each non-response, the auditor shall:

- Send second requests and follow up
- Reconfirm the addresses
- perform alternative audit procedures to obtain relevant and reliable audit evidence, e.g:
  - Check subsequent clearances (for debtor and creditors)
  - For each invoice outstanding at the confirmation date, the auditor should verify the audit trail.
- If the auditor has determined that a response to a positive confirmation request is necessary to obtain sufficient appropriate audit evidence, alternative audit procedures will not provide the audit evidence the auditor requires. The auditor shall determine the implications for the audit and the auditor's opinion

**Total Marks 12**

**Q.7.** 0.5 mark for each audit procedure identified
0.5 for each correct assertion identified

| | | |
|---|---|---|
| Analytical | Existence & Completeness | ▪ Comparison of GP ratio, Receivable Turnover Ratio & Debtors' Age with Past and Industry averages<br>▪ Comparison of bad debts expense as a %age of sales with Past and Industry averages |
| Tests of Details | Existence | ▪ Send confirmation requests to a sample of debtors and perform follow up procedures.<br>▪ Vouch selected amounts from the list of balances with supporting documentation e.g. Sale invoices, tracing receipts<br>▪ Review accounts receivable ledger for any unusual debits/credits to identify any misclassification |
| | Completeness | ▪ Review reconciliation between balance of General Ledger (Debtors' Control Account) and Subsidiary Ledger (Sales Ledger). Select debtors with small or zero balances for confirmation. |
| | Valuation and Allocation | ▪ Obtain invoice wise breakup of individual suppliers and recalculate the total outstanding amount.<br>▪ Confirmation replies<br>▪ Perform following procedures to determine adequacy of provision for bad debts:<br>o Obtain and review aging of receivables.<br>o Ensure that policy of provision for bad debts is consistent with past practice, industry practice and current economic conditions.<br>o Calculate estimate for provision using prior relations of bad debts and sales (Analytical procedure)<br>o Review any correspondence of the client company with customers, lawyers and collection agencies<br>o Examine Cash Receipts and Credit Notes subsequent to year end. |
| | Rights and Obligation | ▪ Inquire management whether any receivables have been sold, discounted, or hypothecated.<br>▪ Review bank confirmations, loan agreements, and minutes of the BOD meetings for indications of whether debtors have been sold, factored, discounted, or pledged as collateral.<br>▪ Examine receipts subsequent to year end. |
| | Cl/Pr | ▪ the list of receivables ledger agrees to the Financial Statements<br>▪ Receivables are correctly classified and presented in the financial statements. |

**Total Marks** **09**

**Q.8.** **(a)** 2 marks for identifying which services can be offered 06

4 marks for identifying the safeguards

A firm can provide bookkeeping and accounting services if services are of a routine nature e.g.:

1. Recording transactions approved by client.
2. Posting transactions to general ledger and to trial balance.
3. Preparing financial statements based on information in the trail balance.
4. Providing payroll services based on client-originated data

**Safeguards for assurance service:**

1. Individual performing non-assurance engagement should not be part of audit engagement team.
2. Firm should involve an independent chartered accountant to review the work.

**Safeguards for non-assurance service:**

1. Managerial functions/decisions should not be taken by firm/individuals (e.g. approval of transactions, preparing or changing source data for transactions, determining or changing journal entries).

**(i)** 2. Obtaining the client's acknowledgement of responsibility for the results of the work performed by the firm/individual.

**(b)** 2 marks for discussing if lease is under normal lending procedures 04
2 marks for discussing if lease is not under normal lending procedures

If lease is not under normal lending procedures and terms and conditions, Self-interest threat would be so significant that no safeguard could reduce the threat to acceptable level and hence the engagement should not be accepted.

If lease is made under normal lending procedures and terms and conditions, it does not create threat to independence and the engagement can be accepted.

**Total Marks 10**

**Q.9.** 1 mark for each risk identified

0.5 mark for separate identification of risk of fraud

- There is a risk that previous finance director may have undertaken other fraudulent transactions; these would need to be written off in the statement of profit or loss.
- There is a risk that the deficiencies in controls (e.g; bonus being based on profit's figure) have not been correctly addressed by the management since the incident, hence increasing the control risk.
- The company recognizes its revenue on a basis of estimation basis which can easily be manipulated by management to achieve its target. This is indicative of risk of fraud and this creates opportunity for the management.
- Lack of segregation of duties increase the control risk and creates opportunity for fraud.
- There is a risk that some or all of the research cost is capitalized and not expensed out.
- The management may manipulate the financial statements to comply with the debt covenants of bank (Pressure to commit fraud).
- In case of breach of debt covenants, the classification of the loan in the balance sheet will have to be changed.

**Total Marks 07**

**Q.10.** 2 marks for explaining use at each stage:

- At **planning** stage:
  - Gain understanding of client entity and business
  - Help identify areas of high audit risk
- At **substantive** phase as source of audit evidence
  - To look for possible material misstatements during the audit rather than later, in the end-of-audit review

- At **conclusion** stage
  - To assist the auditor when forming an overall conclusion as to whether the financial statements are consistent with his understanding of the entity.
  - Corroborate the conclusions formed through other procedures performed during the audit
  - Identify previously unrecognized risk of material misstatement

**Total Marks** **06**

**Q.11.**

**(a)** 1 mark – identification of Material Misstatement 03

1 mark for calculating Impact – material (27% of profit before tax and 7% of net assets)

1 mark for Opinion – Qualified

**(b)** 3 marks for discussing that this will have no impact as this constitutes a change in accounting estimate. 03

**Total Marks** **06**

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