Corporate Sector

Model Solutions

Summer Exam-2014

MODEL SOLUTIONS

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Financial Accounting

(Intermediate Level)

Summer Exam-2014

Corporate Sector

Financial Accounting

Ans. 1. (a)

Star Limited

Statement of Comprehensive Income for the year ended 31 December 2013

	2013 Rupees	Marks
Sales	30,500,000	
Less: Cost of sales		
Opening stock	900,000	
Add: Purchases	14,000,000	
Less: Closing Stock	(750,000)	
	14,150,000	
Gross profit	16,350,000	3
Less:		
Administrative expenses (7,523,000-120,000+567,000+270,000+170,000)	8,410,000	4
Selling expenses	6,250,000	0.5
Financial Charges (2,100x10%)/2	105,000	1
Operating expenses	**14,765,000**	
	1,585,000	
Other income	1,280,000	0.5
Profit before tax	**2,865,000**	
Provision for taxation	974,100	1
Profit after tax	**1,890,900**	

Working Notes:

Depreciation & Amortization

Land and Building	(7000-1330)*10% = 567
Motor Vehicle	(1440-360)*25%=270
Software	(850-340)*20%=170

Total Marks 10

Ans. 1. (b)

Star Limited
Statement of Financial Position as at 31 December 2013

	2013 Rupees	Marks
Equity & liabilities		
Equity		
Paid-up share capital	2,500,000	
Advance against shares	500,000	1
Retained earnings (903,000+1,890,900-500,000)	2,293,900	2
	5,293,900	
Non-Current Liabilities		
Long term Loan (2,100,000-(175,000x4))	**1,400,000**	1
Liabilities		
Current portion of Long term loan	700,000	1
Trade creditors	650,000	
Advance from customers	225,000	1
Accrued interest	105,000	1
Provision for taxation	974,100	
	2,654,100	
Total	**9,348,000**	

	2013 Rupees	Marks
Assets		
Non Current Assets		
Land and building (7,000-1,330-567)	5,103,000	0.5
Motor vehicle (1,440-360-270)	810,000	0.5
Computer software (850-340-170)	340,000	0.5
	6,253,000	
Current Assets		
Trade debtors	1,100,000	
Advance to employees	250,000	0.5
Prepayments	120,000	0.5
Stock in trade	750,000	0.5
Cash at bank	875,000	
	3,095,000	
Total	**9,348,000**	

Total Marks 10

Ans. 2.

AK (Private) Limited
Cash Flow Statement
For the year ended 31 December 2013

Cash Flows From Operating Activities

Loss for the year		(100,000)	2.0
Adjustment for:			
Depreciation	20,000		0.5
Loss on sale of equipments	10,000		1.0
Provision for trade debtors	5,000		0.5
		35,000	
Operating loss before working capital changes		(65,000)	
Increase in stock in trade	(100,000)		0.5
Decrease in trade debtors (160,000 - 305,000)	145,000		1.0
Increase in trade and other payables	30,000		0.5
		75,000	
Net cash from operating activities		**10,000**	
Cash flows from investing activities			
Purchase of Property plant and equipments	(100,000)		1.5
Sale proceeds of equipments	20,000		0.5
Net cash flows from investing activities		**(80,000)**	
Cash flows from financing activities			
Increase in Loan from Director		150,000	0.5
Net cash flows from financing activities		**150,000**	
Net cash flows for the year		80,000	
Cash and cash equivalents at the start of year		95,000	0.5
Cash and cash equivalents at end of year		**175,000**	**1.0**
		-	

Working

Calculation of loss before taxation

Accumulated profit-2012	55,000
Add: loss for the year	(100,000)
Accumulated loss - 2013	(45,000)

Calculation of purchase of plant and equipments

Plant and equipments - Year 2012	150,000
Less: Depreciation for the year	(20,000)
Less: Book value of assets disposed off	(30,000)
Assets Without addition	100,000
Addition during the year (200,000 - 100,000)	100,000

Total Marks 10

Ans. 3.			
(a)	i)	**Property, plant and equipment**	
		Property, plant and equipment are tangible items that:	
		(a) are held for use in the production or supply of goods or services, for rental to others, or for administrative purposes; and	1.5
		(b) are expected to be used during more than one period.	1.5
	ii)	**Impairment loss**	
		An impairment loss is the amount by which the carrying amount of an asset exceeds its recoverable amount.	2
(b)		A complete set of F**inancial Statements** comprises:	
	a-	a statement of financial position as at the end of the period;	0.5
	b-	a statement of profit or loss and other comprehensive income for the period;	1
	c-	a statement of changes in equity for the period;	0.5
	d-	a statement of cash flows for the period;	0.5
	e	notes, comprising a summary of significant accounting policies and other explanatory information;	0.5
		comparative information in respect of the preceding period; and	1
	f-	a statement of financial position as at the beginning of the preceding period when an entity applies an accounting policy retrospectively or makes a retrospective restatement of items in its financial statements, or when it reclassifies items in its financial statements.	1
(c)		**A contingent liability is:**	
	a-	a possible obligation that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity; or	2
	b-	a present obligation that arises from past events but is not recognised because: (i) it is not probable that an outflow of resources embodying economic benefits will be required to settle the obligation; or (ii) the amount of the obligation cannot be measured with sufficient reliability.	3
		A contingent asset is a possible asset that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the entity.	2
		Total Marks	**17**

Ans. 4.

Ahmed's Trading Account
For the period from 1st January 2013 to 21 March 2013

		Rs. (000)	
Sales (2035+6710-880)		7,865	3
Cash sales		935	1
		8,800	
Cost of goods sold			
Opening stock	2,585		
Add: Purchases(1540+7590-1265)	7,865		3
	10,450		
Less: Closing stock (balancing figure)	3,850		2
		6,600	1
Gross profit (25% of sales)		2,200	3
Closing stock lost in fire (3,850,000 - 660,000)		3,190	2

Alternatively T accounts can be prepared in working for calculation of sales and purchases figures
For the information of mark-up of 33.33% on cost of goods sold, it is not possible to solve the problem, therefore margin %age will be determined.

Total Marks 15

Ans. 5.	According to IAS2, inventory is to be measured at lower of Cost and Net Realisable Value. The cost of the remaining items are 3 x100 = Rs. 300 NRV 3 x60 = Rs. 180 As NRV is lower than cost so machines are to be valued at Rs. 180
	Total Marks 05

Ans. 6.

2 mark for each ratio and 1 for each comment.

a) Earning per share = 70,000 / 100,000 = 0.7

Comment

EPS:

It's a performance ratio showing how much earning is available to ordinary shareholder as per their holding. Increase in EPS is a positive sign for the company.

b) Dividend cover = 70,000 / 40,000 =1.75

Comment

Dividend Cover:

It shows how much profit is available for the payment of dividend. A good dividend cover enhances the confidence of the investors

c) P/E Ratio = 8 / 7 = 11.43

Comment

P/E Ratio:

It shows growth in share price as compared to earnings. High P/E Ratio indicates the confidence of investors.

d) Dividend yield = (40,000 / 100,000) / 8 = 5%

Comment

Dividend Yield:

It shows how much return an investor is able to earn in terms of dividend

e) Interest cover = 250 / 25 = 10 times

Comment

Interest Cover:

It indicates company's ability to pay interest out of operating profit. High interest cover satisfies the lenders.

Total Marks 15

Ans. 7.	The telephone expenses for the year ended 28 February 2009 are:		
	1 March –31 March 2008 (no telephone)	0	
	1 April –30 June 2008	2,350	1
	1 July –30 September 2008	2,720	1
	1 October- 31 December 2008	3,340	1
	1 January-28 February 2009(two months)	2,400	2
		10810	
		Total Marks	**05**

Ans. 8.	**Project A**	6
	This project meets the criteria in IAS 38 for development expenditure to be recognized as an asset. These are as follows. **a** The product or process is clearly defined and the costs attributable to the product or process can be separately identified and measured reliably. **b** The technical feasibility of the product or process can be demonstrated. **c** The entity intends to produce and market, or, use the product or process and has the ability to do so. **d** The existence of a market for the product or process or, if it is to be used internally rather than sold, its usefulness to the enterprise, can be demonstrated. **e** Adequate resources exist, or their availability can be demonstrated, to complete the project and market or use the product or process. Development cost is to be capitilized because it meets the criteria under IAS 38 and the company is also going concern. It's to be shown as intangible non-current asset and to be amortized & matched against the income they are expected to generate.	
	Project B	4
	Whilst this project meets most of the criteria discussed above which would enable the costs to be carried forward it fails on the requirements that 'adequate resources exist, or their availability can be demonstrated, to complete the project'. Hence it would be prudent to write off these costs. Once funding is obtained the situation can be reassessed and these and future costs may be capitalized.	
	Project C	3
	This is a research project according to IAS 38, ie original and planned investigation undertaken with the prospects of gaining new scientific or technical knowledge or understanding. There is no certainty as to its ultimate success or commercial viability and therefore it cannot be considered to be a development project. IAS 38 therefore requires that costs be written off as inccured.	
	Total Marks	**13**

Performance Measurement

(Intermediate Level)

Summer Exam-2014
Corporate Sector
Performance Measurement

Ans. No. 1.

	Entire Company	Frame Division	Works Division	Marks Allocation
Sales (Note 1)	Rs.1,162500	Rs 742,500	Rs 825,000	
Variable costs (Note 2)	Rs.651,000	Rs 396,000	660,000	
Contribution margin (sales – variable costs)	Rs. 511,500	Rs 346,500	Rs 165,000	3 (1 marks for each)
Fixed costs	Rs.384,000	280,000	Rs 104,000	3 (1 marks for each)
Operating profit (CM – Fixed costs)	Rs.127,500	Rs 66,500	Rs 61,000	3 (1 marks for each)

Note 1:
Frame Division Sales= 5,500 units x Rs 135 = Rs 742,500 **(0.5)**
Works Division Sales= 3,000 units x Rs275= Rs 825,000 **(0.5)**
Entire Company Sales= Rs 825,000 + [Rs 135 x(5,500 – 3,000)] = Rs 1,162,500. **(1)**

Note 2:
Frame Division Variable Costs= 5,500 units x Rs 72 = Rs 396,000. **(0.5)**
Works Division Variable Costs = 3,000 units x (Rs 135+Rs 85)= Rs 660,000. **(0.5)**
Entire Company Variable Costs = (5,500 units x Rs 72) + (3,000 units x Rs 85) = Rs 651,000. **(1)**

Total Marks 13

Ans. No. 2.a

Particulars	Flexible Budget	Marks Allocation
Units Sold	80,000	
Revenue	1,600,000	
Variable Cost:		
Direct Material	480,000	1
Direct Labour	160,000	1
Variable OH	112,000	1
Total Variable Cost	(752,000)	
Contribution Margin	848,000	1
Fixed Costs	850,000	1
Operating Income	(2,000)	1

Ans. No. 2. b

Particulars	Static Budget	Flexible Budget	Actual Result	Volume Variances	Price & Variable Cost Variances	Marks
Units Sold	85,000	80,000	80,000	(5,000) A	-	1
Revenue	1,700,000	1,600,000	1,665,000	(100,000) A	65,000 F	1
Variable Cost:						
Direct Material	510,000	480,000	495,000	(30,000) F	15,000 A	1
Direct Labour	170,000	160,000	189,000	(10,000) F	29,000 A	1
Variable OH	119,000	112,000	144,000	(7,000) F	32,000 A	1
Total Variable Cost	(799,000)	(752,000)	(828,000)	(47,000) F	76,000 A	1
Contribution Margin	901,000	848,000	837,000	(53,000) A	(11,000) A	1.5
Fixed Costs	850,000	850,000	830,000	-	(20,000) F	1.5
Operating Income	51,000	(2,000)	7,000	(53,000) A	9,000 F	1

Total Marks 16

Ans. No. 3

(a)Income Statement (Absorption Costing)

Sales		2,868,750	
Less: Cost of goods Sold			
Opening inventory	-		
Cost of goods Manufactured (125,000 x 17.70)	2,212,500		1
Less: Ending inventory (12,500 x 17.70)	(221,250)		1
		(1,991,250)	
Gross margin		877,500	1
Less:			
Variable Selling (112,500 x 1.50)	168,750		1
Fixed Selling	131,250		1
		(300,000)	
Net operating income		577,500	1

(b)Income Statement (Marginal Costing)

Sales		2,868,750	
Less: Variable expenses			
Beginning inventory	-		
Cost of Goods Manufactured (125,000 x 12.45)	1,556,250		1
Less: Ending inventory (12,500 x 12.45)	(155,625)		1
Variable Cost of Sales	1,400,625		
Variable Selling	168,750		1
		(1,569,375)	
Contribution		1,299,375	1
Less: Fixed OH	656,250		
Fixed Selling	131,250		
		(787,500)	1
Net operating income		511,875	1

(c)Reconciliation Statement

Net operating income as per Absorption Costing	577,500	1
Net operating income as per Marginal C osting	511,875	1
Difference	65,625	
Change in inventory under Absorption Costing	221,250	1
Change in inventory under Marginal Costing	155625	1
Difference	65,625	

Working

Product Cost (Absorption Costing) = DM + DL + VOH + FOH
= (1,125,000 / 125,000) + (431,250 / 125,000) + (656,250 / 125,000)
= 9 + 3.45 + 5.25 = 17.70

Product Cost (Marginal Costing) = DM + DL + VOH
= (1,125,000 / 125,000) + (431,250 / 125,000) = 9 + 3.45 = 12.45

Total Marks 16

Ans. No. 4 a

The Theory of Constraints is a methodology for identifying the most important limiting factor (i.e. constraint) that stands in the way of achieving a goal and then systematically improving that constraint until it is no longer the limiting factor. In manufacturing, the constraint is often referred to as a bottleneck. **(3)**

The Theory of Constraints takes a scientific approach to improvement. It hypothesizes that every complex system, including manufacturing processes, consists of multiple linked activities, one of which acts as a constraint upon the entire system. Focusing on the bottleneck and planning production accordingly improves the overall profitability of the company. **(2)**

Ans. No. 4 b

Particulars	**Per Unit**		**Marks Allocation**
Products	**frozen canned Haleem**	**fresh canned Haleem**	
Sales Price	50	60	
Maximum Sales demand	1,750	3,500	
Marginal costs			
Material	5	7.5	1
Direct wages	7.5	5	1
Direct expenses	2.5	3	1
Variable overhead	7.5	10	1
Total marginal cost	**22.5**	**25.5**	**1**
Contribution	27.5	34.5	1
Material required per unit	1 Kg.	1.5 Kg.	1
Contribution per kg. of material	27.5	23	1
Ranking	1	2	2

Material to be utilized to maximize profitability;

Product	**Qty can be Produced**	**Material Qty consumed per Unit**	**Total Material Qty Consumed**	**Marks Allocation**
frozen canned Haleem	1750	1 per Kg	1750	1
fresh canned Haleem	2167	1.5per Kg	3250	1
			5000	

Total Marks 17

Ans. No. 5.

(i) **Current Ratio = Current Assets/Current Liabilities**
=390/210=1.3 **(2)**

(ii) **Quick Ratio = (Current Assets- Inventory)/Current Liabilities**
=(390-200)/210=0.63 **(2)**

(iii) **Receivable turnover in days= Average Receivable/Net Credit sale*365**
Average Receivable = (110+115)/2=112.5
= 112.5/515*365 = 79.73 days **(2)**

(iv) **Inventory turnover in days = Average Inventory/Cost of goods sold*365**
Average Inventory = (190+200)/2 = 195
=195/260*365=273.75 days **(2)**

(v) **Debt/Equity ratio = Total long term debt/Total Equity**
= 300/400 = 0.75 **(2)**

(vi) **Return on Total Assets = Net Operating income (EBIT)/total Assets*100**
=233/910*100 = 25.6% **(2)**

(vii) **Turnover on Fixed Assets=Net Operating income (EBIT)/Fixed Assets*100**
=233/470*100 = 49.57% **(2)**

(viii) **Gross Profit Margin=Gross profit/Sales*100**
=255/515*100 = 49.51% **(2)**

(ix) **Net Profit Margin = Net profit/sales*100**
= 143/515*100 = 27.77% **(2)**

(x) **Interest Coverage Ratio = EBIT/Interest Expense**
= 233/33 = 7.06 **(2)**

Total Marks 20

Ans. No. 6.a

A **standard**, as the term is usually used in management accounting, is a budgeted amount for a single unit of output. A standard cost is the pre-determined cost of manufacturing a single unit or a number of product units during a specific period in the immediate future. A **standard cost** for one unit of output is the budgeted production cost for that unit. Standard costs are calculated using engineering estimates of standard quantities of inputs, and budgeted prices of those inputs. **(3)**

The major advantages of standard costing are**;** **(1 each for any 3 of the list)**

- Can be used as performance measurement yardstick;
- Can be used to develop budget;
- Can be used to cost product/services for bidding;
- Effective controlling tool

Ans. No. 6.b

(i) Material Price Variance

Material	Actual Qty Consumed	STD Price	Actual Price	Variance	Marks
A	2250	15	16	2250 A	1
B	1950	45	42	-5850 F	1
C	550	85	86	550 A	1
				-3050 F	

(ii) Material Total Quantity Variance

Material	STD Qty allowed	Actual Qty Consumed	STD Price	Variance	Marks
A	2160	2250	15	1350 A	1
B	1920	1950	45	1350 A	1
C	480	550	85	5950 A	1
	4560			8650 A	

(iii) Material Mix Variance

Material	Actual Qty @ STD Mix	Actual Qty @ Actual Mix	STD Price	Variance	Mark
A	2250	2250	15	0	1
B	2000	1950	45	-2250 F	1
C	500	550	85	4250 A	1
	4750	4750		2000 A	

(iv) Material Yield Variance

Material	STD Qty @ STD Mix	Actual Qty @ Actual Mix	STD Price	Variance	Marks
A	2160	2250	15	1350 A	1
B	1920	2000	45	3600 A	1
C	480	500	85	1700 A	1
	4560	4750		6650 A	

Total Marks 18

Bus. Commn. & Beh. Studies

(Intermediate Level)

Summer Exam-2014

Corporate Sector

Bus. Com. & Beh. Studies

Ans. 1 Answers will vary but must contain the principles of Precis writing. **15**

Ans. 2 Communication principles provide guidelines for choice of content and style of presentation, adapted to the purpose and receiver of your message-called the "seven C's," they are completeness, conciseness, consideration, concreteness, clarity, courtesy, and correctness. **08**

COMPLETENESS - Business message is complete when it contains all facts the reader or listener needs for the reaction we desire.

Completeness includes the following:

1. **Providing All Necessary Information**
   - When you initiate a message, check to make sure you have provided all the information the reader needs for thorough, accurate understanding.
   - One way to make your message complete is to answer the five W Questions - who, what, when, where, why - and any other essentials.
2. **Answering All Questions Asked**
   - Whenever you reply to an inquiry, try to answer all questions-stated and implied.
   - If you have no information on a particular question, say so clearly.
   - If you have unfavorable information in answer to certain questions, handle your reply with both tact and honesty.
3. **Giving Something Extra, When Desirable**
   - Sometimes you must do or give more than answer the customers “Specific questions”.

Benefits of Completeness

1. Complete messages are more likely to bring the desired results without the expense of additional messages.
2. They can do a better job of building goodwill. Messages that contain information the receiver needs show concern for others.
3. Complete messages can help avert costly lawsuits that may result if important information is missing.
4. Last, communications that seem inconsequential can be surprisingly important if the information they contain is complete and effective.

Ans. 3 Answers will vary but report must contain the following parts

1. Introduction and Purpose **03**
2. Methods of Investigation **03**
3. Different symptoms of the problem **03**
4. Conclusions **03**
5. Recommendations **03**

(Total Marks 15)

Ans. 4 In Herzberg two-factor theory of motivation, the two factors are called: **08**

- the dissatisfiers-satisfiers or
- the hygiene-motivators or
- the extrinsic-intrinsic factors

Dissatisfiers or Hygiene Factors - the theory concludes that there is a set of extrinsic conditions, the job context, which results in dissatisfaction among employees when the conditions are not present. If these conditions are present, this does not necessarily motivate employees. These conditions are the dissatisflers or hygiene factors, since they are needed to maintain at least a level of "no dissatisfaction."

They include:

1. Salary
2. Job security
3. Status
4. Working conditions
5. Company procedures
6. Quality of technical supervision
7. Quality of interpersonal relations at work place

Satisfiers or Motivators - a set of intrinsic conditions - the job content - when present in the job, builds strong levels of motivation that can result in good job performance. If these conditions are not present, jobs do not prove highly satisfying. The factors in this set are called the satisfiers or motivators and include:

1. Achievement
2. Recognition
3. Responsibility
4. Advancement
5. The work itself
6. The possibility of growth

These motivators are directly related to the nature of the job or task itself. When present, they contribute to satisfaction. This, in turn, can result in intrinsic task motivation.

Ans. 5 Training needs of employees can be determined by any of the following or with the combination of the following methods. **05**

1. **Performance Appraisal**
   Employees' work is measured against the performance standards or objectives established for his or her job.
2. **Analysis of Job requirements**
   The skills or knowledge specified in Job Descriptions are examined and those employees who lack in those areas are identified as suitable candidates for the training.

3. **Organizational analysis**
   The effectiveness of the organization and its success in meeting its goals are analyzed to determine where differences exist. The differences are identified as improvement needed areas and employees are recommended for training to improve overall effectiveness of the organization.
4. **Employee Survey**
   Employees are asked to identify the problems they face in completing tasks and also recommend solutions.

Ans. 6 To compose effective written or oral messages, you must apply certain communication principles, These principles provide guidelines for choice of content and style of presentation, adapted to the purpose and receiver of your message-called the "seven C's," they are completeness, conciseness, consideration, concreteness, clarity, courtesy, and correctness. **07**

CONCISENESS

Conciseness is saying what you have to say in the fewest possible words without sacrificing the other C qualities. A concise message is complete without being wordy. Conciseness, include the following:

1. Eliminating Wordy Expressions. Use single-word substitutes instead of phrases whenever possible without changing meanings.

   Wordy: At this time Concise: Now

2. Omitting unnecessary expressions.

   Wordy: Please be advised that your admission statement was received.

   Concise: Your admission statement has been received.

3. Include Only Relevant Material. The effective, concise message should omit not only unnecessarily wordy expressions but also irrelevant statements.
4. Avoid Unnecessary Repetition. Sometimes repetition is necessary for emphasis. But when the same thing is said two or three times without reason, the message becomes wordy and boring.

Advantages

- A concise message saves time and expense for both sender and receiver. Conciseness contributes to emphasis; by eliminating unnecessary words, you let important ideas stand out.
- When combined with a "you-view", concise messages are inherently more interesting to recipients.
- Finally, concise messages show respect for recipients by not cluttering their professional lives with unnecessary information.

Ans. 7 Answer will vary but besides logical persuasive content it must contain the following. **10**

- Bad news organizational plan.
- Opening Paragraph must begin with a buffer that refers to the firm's appreciation or careful consideration of the reader's request for credit or to his or her interest in the store, or to both.
- Explanations of retail credit refusals should be given.
- Offer for future sales should be maintained.

Ans. 8a Minutes Book is an important and valuable record of a company registered or incorporated bodies. **06**

Functions The functions of Minute book include the following:

1. It is a cumulative record of the business transacted in the various meetings.
2. It can be checked by Government Officials and are open for inspection by the shareholders whenever they like to do so.
3. It helps in building up the history of the company.
4. It reflects the performance and achievements of the company.
5. It is used for future planning and programs.
6. It reflects the interest taken and contribution made by the various shareholders or members of the company.
7. It helps in assessing what progress the company has made during specified period.
8. It helps in finding out the soundness of the policies of the Management.
9. It helps in establishing company's financial position.
10. It helps in tracing the problems faced and how they have been solved.

Ans. 8b **Statutory Meeting (SIM) -** Every company public limited by shares and every company limited by guarantee and having a share capital shall, within a period of not less than three months, not more than six months, from the date at which the company is entitled to commence business, hold a general meeting of the members of the company, which shall be called Statutory Meeting. **04**

Annual General Meeting (AGM) - Every company shall hold its annual general meeting, within eighteen months from the date of its incorporation and thereafter once at least in a year.

(Total Marks 10)

Ans. 9 Organization Development (OD) is the systematic application of behavioral science knowledge at various levels, such as group, inter-group, organization, etc., to bring about planned changes. Its objective is a higher quality of work-life, productivity, adaptability, and effectiveness. It accomplishes this by changing attitudes, behaviors, values, strategies, procedures, and structures so that the organization can adapt to **05**

competitive actions, technological advances, and the fast pace of change within the environment.

Characteristics:

1. Humanistic Values: Positive beliefs about the potential of employees.
2. Systems· Orientation: All parts of the organization, to include structure, technology, and people, must work together.
3. Experiential Learning: The learners' experiences in the training environment should be the kind of human problems they encounter at work. The training should NOT be all theory and lecture.
4. Problem Solving: Problems are identified, data is gathered, corrective action is taken, progress is assessed, and adjustments in the problem solving process are made as needed. This process is known as Action Research.
5. Contingency Orientation: Action are selected and adapted to fit the need.
6. Change Agent: Stimulate, facilitate, and coordinate change.
7. Levels of Interventions: Problems can occur at one or more level in the organization so the strategy will require one or more interventions.

Ans. 10 **On the Job methods** 06

- Coaching - The training of an employee by his or her immediate boss or supervisor is by far the most effective management development technique.
- Job rotation - It involves shifting managers from position to position so they can broaden their experience and familiarize themselves with various aspects of the firm's operations.
- Training positions - Trainees are third method of developing managers. Trainees are given staff positions immediately under a manager. Such assignments give trainees a chance to work with and model themselves after outstanding managers.
- Planned work activities - It involve giving trainees important work assignments to develop their experience and ability.
- Participation - Trainees may be asked to head taskforce or participate in an important committee meeting. It helps them gain insight into how organizations operate and also improve their human relations skills.

Off the Job methods 01

Employees are sent to different training programs. It enables them to focus on training and development only. It also improves their professional socialization.

(Total Marks 07)

Ans. 11 Answer will vary but besides content following characteristics must be checked.

The theme of the essay with a definite purpose is present	**2.5**
The thoughts are in order with a definite conclusion	**2.5**
Slangs and free and easy construction is not used	**2.5**
The writing shows personal thoughts of writer and is simple in structure	**2.5**

(Total Marks 10)

Business Laws

(Intermediate Level)

Summer Exam-2014

Corporate Sector

Business Laws

Ans. 1	**Precedent:** In Pakistan the courts have to follow the following rules of precedent:	
	▪ The decisions of the Privy Council are not of the highest authority. Now, under the new constitution, the Supreme Court is the highest authority in the country. ▪ The decisions of one High Court are not authoritative with regard to another High Court. ▪ In the same High Court the decision of a single judge is binding on another single judge but not on a court of Appeal. ▪ A judge of the lower court is bound to follow the ruling of the High Court of his own presidency when there is a conflict amongst the High Courts. ▪ Unreported judgments have as much binding authority as reported ones.	**01** **01** **1.5** **1.5** **01**
		Total Marks 06
Ans. 2 (a)	To the above general rule there are, two exceptions which are stated as under:- a) Where the partnership agreement gives a right to a partner to introduce a new partner. b) When a minor admitted to the benefits of partnership elects to become a partner on attaining majority.	 **2.5** **2.5**
Ans. 2 (b)	**Registration of Subsequent Alterations.** The following changes in the firm are to be registered. a. Change of firm's name. b. Change of principal place of business. c. Closing down of old place of business d. Opening a new place of business. e. Change in the names or addresses of partners, f. Change in the constitution of firm g. Dissolution of firm, h. Minor elects to become a partner or not on attaining majority. **(one mark each for any five correct answers)**	**05**
		Total Marks 10
Ans. 3	In an unconditional contract for the sale of specific goods in a deliverable state, the property in the goods passes to the buyer when the contract is made, and it is immaterial whether the time of payment of the price or the time of the delivery of the goods, or both, is postponed. The property in goods had passed onto the buyer and Seema is liable to pay for it whether delivery is taken or not or paid or not.	**03** **01**
		Total Marks 04

Ans. 4 (a)	**i) Prospectus.** "Prospectus" means any document described or issued as prospectus, and includes any notice, circular, advertisement, or other communication, inviting offers from the public for the subscription or purchase of any shares or debentures of, a body corporate, or inviting deposits from the public, other than deposits invited by a banking company or a financial institution approved by the Federal Government, whether described as prospectus or otherwise;	**03**
	ii) Subsidiary Company. It means a company or a body corporate whose more than fifty percent (50%) voting securities are held or controlled (directly or indirectly), by some other company or such other company has a power to elect and appoint more than fifty percent (50%) of the directors of such company.	**01** **01**
Ans. 4 (b)	i) The first Annual General Meeting (AGM) of the company is required to be held within 18 months from the date of incorporation.	**02**
	ii) Statutory meeting is required to be held within a period of not less than three months but not more than 6 months from the date at which a company is entitled to commence business.	**02**
	iii) A seven days notice is required for holding Board of Directors Meeting however, in emergency meeting may be called at a shorter period notice.	**01**
	iv) The notice of Annual General Meeting (AGM) shall be sent to the shareholders at least twenty one days before the date fixed for the meeting.	**01**
		Total Marks 11
Ans. 5 (a)	**Change in status of a Single Member Company** A change in the status of a single member company may come under the following circumstances:- i) By transfer / further allotment of shares to any other person; ii) By the death of single member; and iii) By the operation of a law affecting the status of single member company.	 **01** **01** **01**
Ans. 5 (b)	A Single Member Company can be converted into a private company on increase of the number of its members to more than one. The company shall pass a special resolution for change of status and alter its articles accordingly within thirty days and transfer the shares within seven days. The company shall appoint and elect one or more additional directors within fifteen days of passing the special resolution and notify the appointment on Form 29 under the Companies (General Provisions and Forms) Rules, 1985 within fourteen days of appointment. Further, the company is required to file a notice of the fact in writing the form as set out in Form S2, with the registrar within sixty days from the date of passing of special resolution.	**01** **01** **01** **01**
		Total Marks 07

Ans. 6	Legislation is either supreme or subordinate. The supreme law is that which proceeds directly from the sovereign power in the State and is therefore free from any external control. Subordinate legislation is that which proceeds from any authority other than the sovereign power, and it is therefore, dependent for its continued existence and validity on some supreme or superior authority.	**02** **02**
	Total Marks 04	
Ans. 7	The following agreements are declare void under the Act:- i) Where both the parties to an agreement are under a mistake of fact essential to the agreement. ii) Agreement in restraint of the marriage of any person other than a minor. iii) Agreement in restraint of trade. iv) Agreement in absolute restraint of judicial proceedings. v) An agreement the meaning of which is uncertain and in-capable of being made certain. vi) Agreement by way of wager. vii) Agreement to do an act which is impossible in it or which subsequently becomes impossible without any default of a party. viii) Agreement made without consideration. **(01 mark for each correct answer)**	 **06**
	Total Marks 06	
Ans. 8 (a)	Where Kamal elects not be become a partner: a) His rights and liabilities shall continue to be those of a minor up to the date on which he gives public notice. b) His share shall not be liable for any acts of the firm done after the date of the notice, and c) He shall be entitled to sue the partners for his share of the property and profits.	 **02** **01** **01**
Ans. 8 (b)	A retiring partner may (i) carry on similar business with that of the firm, (ii) compete in such business, and (iii) advertise such business, but unless the contract otherwise provides, he cannot; (a) use the old firm name, (b) represent himself as carrying on the business of the old firm, or (c) solicit customers of the old firm.	 **01** **01** **01** **01** **01** **01**
	Total Marks 10	

Ans. 9	(a)	In case of shares allotted otherwise than in cash, along with filing of Form 3, produce for inspection and examination of registrar a written contract constituting the title of the allottee to the allotment together with the contract of sale or for service or other consideration for the allotment.	**03**
	(b)	In the case of bonus shares file with the registrar return of allotment together with the copy of the resolution authorizing the bonus issue.	**02**
		Total Marks 05	
Ans. 10		Annual General Meetings are required to be held once at least in every calendar year, within a period of 04 months following the close of its financial year and not more than fifteen months after holding of its last preceding AGM.	**04**
		In view of the above AB Limited can hold its 20th AGM latest by 30th April, 2014.	**03**
		Total Marks 07	

Taxation

(Intermediate Level)

Summer Exam-2014

Corporate Sector

Taxation

Ans. 1

OUTPUT TAX		RUPEES
Sales (2,000,000 + 3,000,000) x 17%		850,000
Less: Input tax		
Purchases from registered person (1,500,000 x 17%)	255,000	
Import (1,000,000 x 17%)	170,000	(425,000)
TAX LIABILITY FOR JULY		**425,000**

Total Marks 06

Ans. 2 (a)

INPUT TAX

In relation to a registered person, input tax means;

1- The tax levied under Sales Tax Act, 1990 on supply or import of goods.
2- In relation to goods or service acquired by the person excise duty on sales tax mode on the manufacture or production of goods or rendering or providing of services.
3- The provincial sales tax levied on services rendered and
4- The tax levied under Sales Tax Act 1990 as adopted in the state of Azad Jammu & Kashmir on the supply of goods received by that person.

Total Marks 02

Ans. 2 (b)

TAX FRAUD:

Tax fraud means any of the following actions taken by a person knowingly, dishonestly or fraudulently and without any lawful excuse in contravention of the duties or obligations imposed under the Sales Tax Act, 1990 or rules or instructions under the Act; or

1- Doing of any Act or causing to do any act,
2- Omitting to take any action or causing the omission to take any action;
3- Making of taxable supplies without getting registration under the Sales Tax Act; or
4- Falsifying or causing falsification of the sales tax invoices. The person should be doing or omitting any act with the intention of;
    a. Understating the tax liability.
    b. Underpaying the tax liability for two consecutive tax periods
    c. Overstating the entitlement of tax credit or tax refund to cause loss of Tax.

In this case burden of Proof shall be upon the accused.

Total Marks 02

Ans. 3	**OUTPUT TAX**	**RUPEES**
	Taxable Supplies (Rs. 2,500,000 x 17%)	425,000
	Exempt Supplies	NIL
	TOTAL OUTPUT TAX	**425,000**
	INPUT TAX	
	Input tax attributable to taxable supplies	
	(2,000,000 x 17%) x 2,500,000/4,000,000	212,500
	NET TAX LIABILITY	**212,500**
		Total Marks 06

Ans. 4 (a)

EMPLOYMENT:

Employment includes;

a- a directorship or any other office involved in the management of a company;

b- a position entitling the holder to a fixed or ascertainable remuneration or

c- a the holding or acting in any public office

Total Marks 02

Ans. 4 (b)

INDUSTRIAL UNDERTAKING:

Industrial undertaking means;

a- an undertaking which is setup in Pakistan and which employs;

1. ten (10) or more persons in Pakistan and involves the use of electrical energy or any other form of energy which is mechanically transmitted and is not generated by human or animal energy or
2. twenty (20) or more persons in Pakistan and does not involve the use of electrical energy or any other form of energy which is mechanically transmitted and is not generated by human or animal energy and which is engaged in:
   - i- The manufacture of goods or materials or the subjection of goods or materials to any process which substantially changes their original condition
   - ii- Ship Building
   - iii- Generation, conversion, transmission or distribution of electrical energy or the supply of hydraulic power or
   - iv- The working of any mine, oil well or any other source of mineral deposits and

b- Any other industrial undertaking which the Board may notify in the official Gazette by notification.

Total Marks 02

Ans. 4 (c)	**Tax payer** Tax payer means any person who drives an amount chargeable to tax under the ordinance and includes; a- Any representative of a person who drives an amount chargeable to tax. b- Any person who is required to deduct or collect tax under this ordinance. c- Any person required to furnish a return of income or pay tax under this ordinance.
	Total Marks 02

Ans. 5

ABC LIMITED

		RUPEES
Accounting Profit for the year		1,200,000
Add:		
Donation to un recognized Institution	130,000	
Brokerage paid without deduction of tax	125,000	
Reserve for bad debt	145,000	
Accounting Depreciation	80,000	480,000
		1,680,000
Less: Dividend (Separate block of income)		(200,000)
Tax depreciation (400,000 x 15%)		(60,000)
TAXABALE INCOME		**1,420,000**
TAX LIABILITY	1,420,000 x 34%	482,800

Total Marks 08

Financial Reporting

(Final Level)

Summer Exam-2014

Corporate Sector

Financial Reporting

Ans. 1.	**a)** **Cost of asset**		
		Rs.	07
	Purchase price (150,000-2,000)	148,000	
	Import duties	12,000	
	Site preparation	15,000	
	Trial run cost	15,000	
	Dismantling cost at PV	12,400	
	Total	202,400	
	b) **Depreciation for the year ended December 31, 2013**	**Rs.**	
	Cost of asset 202,400		03
	Useful life 5		
	Months used in current year 6		
	(202,400/5)x6/12	20,240	
		Total Marks 10	
Ans. 2.	a) The tax rates announced after the yearend are not applicable and do not effects the tax calculation, whether current or deferred, therefore it is non-adjusting event.		04
	b) Although the goods are sold before the yearend but chances of occurrence considered were remote, further the explosion also occurred after the yearend. Therefore, there is no need to recognize the provision.		04
	c) The provision should be revised and updated in the financial statements, a further expense of Rs. 0.3 million should be recognized.		04
	d) The amount of provision should be revised and updated according to new information and reduction in provision should be incorporated in the current year financial statements. It is assumed that there is objective evidence of existence of the technology.		03
		Total Marks 15	
Ans. 3.	**a)** **Classification of lease** The lease can only be classified as finance lease if any of the five conditions is satisfied: - a) Ownership of asset transferred to lessee at the end of lease term; b) The lessee has the bargain purchase option at the end of lease term and it is reasonably certain that the lessee will avail the bargain purchase option; c) The lease term is for major part of economic life of asset; d) The present value of minimum lease payments substantially equal to the fair value of asset; or		02

	e) The asset is of specialized nature and persons other than lessee have to materially modify the asset before use. PV of MLP's = 9.76 x 10,000 = 97,600 % of fair value = 97,600/160,000 = 61% According to the conditions discussed above this is an operating lease because none of the above conditions is satisfied. **b) Expense of the year** Rs. Initial direct cost 5,000 Rentals paid (10,000x4) 40,000 45,000	05
		Total Marks 07

Ans. 4.

Name of related party	Nature of transaction	Amount of transaction Rs.	Balance outstanding Rs.	Remarks
Subsidiary company LAL Limited	Goods purchased	10 million	NIL	The transaction was at arm's length
Associated concerns KAMA Limited	Goods sold	2.5 million	2.5 million	The related party relationship is due to common directorship; however the transaction is at arm's length.
Others				
Wife of Director	Donation given	0.25 million	N/A	The donation paid to charitable organization in which wife of director is trustee

Note: - The relationship in b) is not related party as the executives of subsidiary company cannot effect the decisions of parent company.
The joint venturers are not related parties unless some other relationship exists.

Total Marks 12

Ans. 5.

Borrowing cost eligible for capitalization:

	Rs. (000)
Borrowing cost eligible	310
Interest income (1,000x7.5%)	(75)
Net borrowing cost eligible	235

Total Marks 07

Ans. 6.

a) **05**

	Rs.
Opening deferred tax liability	19,425
Deferred tax charged to revaluation surplus (20,000x.35)	7,000
Deferred tax charge to profit or loss account (40,200-20,000)x0.35	7,070
Closing deferred tax closing liability	33,495

Taxable income for the year	125,400
Un-used tax losses brought forward	(20,000)
Taxable profit for the year	105,400
Current tax (105,400x0.35)	36,890

b) **05**

	Rs. (000)
Interest cost **(100,000x13%8/12)**	8,667
Borrowing cost of suspended period	(1,084)
	7,583
Interest income (500x7/8)	(438)
Net borrowing cost eligible	7,145

c) **05**

	Rs. (000)
Cost of investment (200x25)	5,000
Share of net assets (26,400x0.25)	(6,600)
Bargain purchase gain	(1,600)
Restated cost of investment	6,600
Share of post acquisition profit net of dividend (5,400-1,200)x0.25	1,050
	7,650

Total Marks 15

Ans. 7.

Rahim Limited
Statement of comprehensive income
For the year ended December 31, 2013

	2013 (Rs. 000)	2012 (Rs. 000) Restated
Sales	72,200	52,400
Cost of goods sold	(60,800)	(39,570)
Gross profit	11,400	12,830
Operating expenses	(5,000)	(3,830)
Operating profit	6,400	9,000
Interest expense	(605)	(540)
Profit before tax	5,795	8,460
Tax expense	(2,348)	(1,731)
Profit after tax	3,447	6,729

Rahim Limited
Statement of changes in equity
For the year ended December 31, 2013

	Share capital Rs. (000)	Retained earnings Rs. (000)	Total Rs. (000)
Balance b /f	50,000	7,920	57,920
Profit for the year 2012		6,729	6,729
Balance c /d	50,000	14,649	64,649
Bonus issue	5,000	(5,000)	--
Profit for the year 2013	--	3,447	3,447
Balance c /d	55,000	13,096	68,096

Total Marks 14

Ans. 8. a) **05**

Goodwill	Rs. (million)	Rs. (million)
Cost of investment		
Shares (27x18)		486
Fair value of NCI (3x12)		36
		522
Fair value of net assets		
Share capital	300	
Pre-acquisition reserves		
Retained earnings	25	
Fair value gain	50	375
Goodwill		147

b) 15

	HL RS. (m)	SL RS. (m)	Adj. RS. (m)	Consolidated RS. (m)
Sales	18,750	13,500	(200)	32,050
Cost of sales	(5,670)	(5,060)	138	(10,592)
Gross profit	13,080	8,440	(62)	21,458
Selling expenses	(2,030)	(2,010)	--	(4,040)
Administrative expenses	(1,630)	(1,140)	--	(2,770)
Interest expenses	(310)	(202)	--	(512)
Other income	75	-	(54)	21
Profit before tax	9,185	5,088	(116)	14,157
Income tax	(1,170)	(1,235)	--	(2,405)
Profit for the period	8,015	3,853	(116)	11,752
NCI (3,853-5-3-25-29)x.10	**--**	**(379)**	**--**	**(379)**
Profit attributable to group	**8,015**	**3,474**	**(116)**	**11,373**

Cost of sales	5	
Pre-acquisition reserves		5
Cost of sales	3	
Accumulated depreciation		3
Sales	200	
Cost of sales		200
Cost of sales	25	
Closing stock		25
Other income	54	
Dividend		54
Cost of sales	29	
Goodwill		29

Total Marks 20

Management Accounting

(Final Level)

Summer Exam-2014

Corporate Sector

Management Accounting

Ans 1 a)

(i) Accounting rate of return: (ARR)

Project A

Average annual profit = Rs.200, 000 - Rs.100, 000 depreciation
= Rs.100, 000.

Average capital employed = (Rs.556, 000 + Rs.56, 000) / 2
= Rs.306, 000

ARR = $\frac{\text{Rs.100, 000}}{\text{Rs.306, 000}} \times 100\%$
= 32.7% (2)

Project B

Average annual profit = Rs.500, 000 - Rs.263, 000 depreciation
= Rs.237, 000.

Average capital employed = (Rs.1, 616,000 + Rs.301, 000)/2
= Rs.958, 500.

ARR = $\frac{\text{Rs.237, 000}}{\text{Rs.958, 500}} \times 100\%$
= 24.7% (2)

(ii) Payback

Project A

Payback period = $\frac{\text{Rs.556, 000}}{\text{Rs.200.000}}$
= 2.8 years, or 2 years 9 months (1.5)

Project B

Payback period = $\frac{\text{Rs.1, 616,000}}{\text{Rs.500.000}}$
= 3.2 years, or 3 years 2 months (1.5)

(iii) Net present value (NPV)

Year	**Discount Factor at 15%**	**Project 1 Cash flow Rs.**	**PV Rs.**	**Project 2 Cash flow Rs.**	**PV Rs.**
0	1.000	(556,000)	(556,000)	(1,616,000)	(1,616,000)
1 – 5	3.352	200,000	670,400	500,000	1,676,000
5	0.497	56,000	27,832	301,000	149,597
NPV			142,232		209,597

(5)

Ans 1	**(iv) Internal rate of return (IRR)** Both projects have a positive NPV at 15%. Try a higher discount rate: ***Try 20%*** NPV of Project 1 = - 556,000 + (200,000 × 2.991) + (56,000 × 0.402) = - 556,000 + 598,200 +22,512 = + Rs.64, 712 NPV of Project 2 = -1,616,000 + (500,000 × 2.991) + (301,000 × 0.402) = - 1,616,000 + 1,495,500 + 121,002 = + Rs.502 ***Try 25%*** NPV of Project 1 = - 556,000 + (200,000 × 2.689) + (56,000 × 0.328) = - 556,000 + 537,800 + 18,368 = + Rs.168 NPV of Project 2 = -1,616,000 + (500,000 × 2.689) + (301,000 × 0.328) = -1,616,000 + 1,495,500 + 121,002 = - Rs.172, 772 IRR of Project 1 = 25%+ $\frac{168}{(64{,}712 - 168)}$ × (25−20) % = 25.01%, = 25% to the nearest 1%. IRR of Project 2 =25%+ $\frac{502}{(502+172772)}$ × (25−20) % = 20.01%, = 20% to the nearest 1%.	 (2) (2)
Ans 1 b)	Project 2 should be recommended because it has a higher NPV. When there are mutually exclusive projects, ignoring risk and uncertainty, the NPV method should be used to make the project selection. It does not matter that project 1 seems better on the basis of ARR, payback and IRR.	 (4)

Total Marks 20

Ans 2 a)	EOQ = $\sqrt{\frac{2 \times ordering\ cost \times Annual\ Demand}{Holding\ Cost}}$ Ordering cost = 10 per order Holding Cost = 2 per unit Annual demand = 1000 unit = $\sqrt{\frac{2 \times 10 \times 1000}{2}}$ =100 units	(1.5) (1.5)
Ans 2 b)	**The total cost at EOQ** Purchase Cost = Purchase Price x Annual Demand = Rs.20 x 1000 = Rs20, 000 Ordering Cost = *No. of orders x Ordering Cost / Order = 10 x Rs.10 = Rs.100 Holding Cost = (EOQ / 2) x Holding Cost = (100 / 2) x Rs. 2 = Rs.100 *No of Orders = Annual Demand / EOQ = 1000 / 100 = 10 orders Total Cost = Purchase Cost + Ordering Cost + Holding Cost = Rs.20000 + Rs.100 + Rs. 100 = Rs. 20,200	(0.75) (0.75) (0.75) (0.75)
Ans 2 c)	**i . At 2% Discount offer** Purchase Cost = Rs.20 x 0.98 x 1000 = Rs.19, 600 Ordering Cost = (1000 / *200) x Rs.10 = Rs.50 Holding Cost = (*200 / 2) x Rs.2 = Rs.200 Total Cost = Rs.19, 600 + Rs.50 + Rs.200 = Rs.19850 *Order Size = 200	 (0.5) (0.5) (0.5) (0.5) (0.5)

ii. At 2.5% Discount

	Purchase Cost	=	Rs.20 x 0.975 x 1000	
		=	Rs.19, 500	(0.5)
	Ordering Cost	=	(1000 / *250) x Rs.10	
		=	Rs.40	(0.5)
	Holding Cost	=	(*250 / 2) x Rs.2	
		=	Rs.250	(0.5)
	Total Cost	=	Rs.19, 500 + Rs.40 + Rs.300	
		=	Rs.19, 790	(0.5)
	*Order Size = 250			(0.5)
	The optimum level would be 250 units at which cost is minimum i.e. Rs. 19,790.So company would accept supplier offer at 2.5% Discount			(1)

Total Marks 12

Ans 3	**Dividend Growth model**	$= \frac{Dividend\ (1+g)}{Ke - g}$	(3)
		$= \frac{113.1\ (1+0.07)}{0.15 - 0.07}$	
		= Rs.1515	
	Value per share	= Rs.1515/640 **=2.37 per Share**	(2)
	Growth Rate	$= \left(\frac{Latest\ Dividend}{Dividend\ n\ years\ ago}\right)^{1/n} - 1$ $= (113.1/85)^{1/4} - 1$ = 7%	(3)

Total Marks 8

Ans 4 a)	**Share Repurchase** Some time, companies have the right to buy back their shares as in the case of Salik Co. This can be beneficial to the company. **i. Benefits of Share repurchase** **1.** Suitable use of surplus cash which may be classified as dead asset. **2.** Increase in EPS by the reduction in no. of shares. **3.** It helps to avoid the possibility of take over. There are some drawbacks of share repurchase as well	(2-3)

	ii. Draw Back of Share Repurchase **1.** It will increase the Co. gearing. **2.** Repurchase may portray that the company might not be effectively using their funds. **3.** Difficult to determine the price at which the shares could be repurchased	(2-3)
Ans 4 b)	**Factors need to be considered by the Salik co. before adopting any policy regarding dividends are:** **1.** The need to retain and re-invest in order to remain profitable. **2.** Any restrictions imposed by Govt. on Salik Co. Regarding profit distribution. **3.** Any convents imposed by the Banks of the Company **4.** Salik Co. liquidity Position **5.** The Signaling effect to the shareholders.	(3-4)

Max Marks 10

<table>
<tr><td>Ans 5 a)</td><td>
<table>
<tr><td></td><td></td><td>Rs.000</td><td>Rs.000</td></tr>
<tr><td>Sales</td><td></td><td></td><td>288</td></tr>
<tr><td>Variable cost:</td><td>Direct material</td><td>54</td><td></td></tr>
<tr><td></td><td>Direct wages</td><td>72</td><td></td></tr>
<tr><td></td><td>Production O/H</td><td>18</td><td></td></tr>
<tr><td></td><td>Variable Admin Costs.etc</td><td>27</td><td>(171)</td></tr>
<tr><td>Contribution</td><td></td><td></td><td>117</td></tr>
</table>
Contribution per Unit =Rs.117000/9000 = Rs.13
Break Even Point = Fixed Cost / Contribution per unit
= (Rs.42000+Rs.36000)/Rs.13
= 6000 units
Break Even Sales Revenue = Breakeven units x Selling Price per Unit
= 6000 units x Rs.32/Unit
=Rs.192, 000
</td><td>(3)
(2.5)
(1.5)</td></tr>
<tr><td>Ans 5 b)</td><td>
If activity behavior increased to 100% Capacity.
<table>
<tr><td>No. Of Units</td><td>=</td><td>12000</td></tr>
<tr><td>Contribution (12000 x Rs.13)</td><td>=</td><td>Rs.156000</td></tr>
<tr><td>Less: Fixed Production O/H</td><td>=</td><td>Rs.42000</td></tr>
<tr><td>Less: Fixed Admin Costs</td><td>=</td><td>Rs.36000</td></tr>
<tr><td>Profit</td><td></td><td>Rs.78000</td></tr>
</table>
</td><td>(3)</td></tr>
<tr><td>Ans 5 c)</td><td>
If Selling Price reduced to Rs.28/Unit
<table>
<tr><td></td><td>Rs.000</td></tr>
<tr><td>Sales(Rs.28 x 10800)</td><td>302.4</td></tr>
<tr><td>V.cost Rs.171000 x (90%/75%)</td><td>205.4</td></tr>
<tr><td>Contribution</td><td>97.2</td></tr>
<tr><td>F.Cost</td><td>78</td></tr>
<tr><td>Profits</td><td>19.2</td></tr>
</table>
</td><td>(3)</td></tr>
</table>

Ans 5 d)	**If Selling Price Reduced by 15%**	
		Rs.000
	Sales(Rs.27.20 x 10800)	326.4
	V.cost Rs.171000 x (100%/75%)	(228)
	Contribution	**98.4**
	F.Cost **:Budgeted**	(78)
	:Special Advertising	(5)
	Profits	**15.4**
		(3)

Ans 5 e)	A unit price of Rs.32 as suggested in original budget should be adopted as it would generate the Profits of Rs39,000 maximum in all proposals	(2)

Total Marks 18

Ans 6 a)	**Financial ratios**				
			2013	***2014***	
	Net profit margin	Profi before interest and tax / Sales revenue	18/180 = 10%	16.5/185=8.9%	(2)
	Asset turnover	Sales / Capital employed	180/105.6 = 1.7 times	185/ 123.2 = 1.5 times	(2)
	Current ratio	Current assets / Current liabilties	13.6/ 8.4 =1.6:1	11.9/9.2 = 1.3:1	(2)

Ans 6 b)

The fall in operating profit may have been caused by an increase in costs, whilst the new investment will have caused an increase in capital employed. (2)

Asset turnover has fallen. Sales have only increased by 2.8% between 2013 and 2014 so the new investment may not yet have had a significant effect upon sales.

In the short term, the investment has increased assets and costs but has not yet influenced sales. (2)

The current ratio has deteriorated so the firm's ability to meet its short-term obligations from its short-term resources has been reduced. The expenditure on the investment may have decreased the cash balance between 2013 and 2014, causing the deterioration in liquidity. (2)

Total Marks 12

Ans 7

Step-1: Statement of Physical Flows

Work in Process at start	0
Units Started	50000
To be accounted for	50000
Units Completed	41000
Normal Loss (50000 x 5%)	2500
Closing WIP	5000
Abnormal Loss	1500
Units accounted for	50000

(1)

Statement of Equivalent Units

	Total	**Materials**	**Conversion Cost**
Unites completed	41000	41000	41000
Normal Loss	2500	0	0
Closing Work in Process			
100% completed for Material& 50 % for conversion cost	**5000**	**5000**	**2500**
Abnormal Loss	1500	1500	1500
Units Accounted For	**50000**	**47500**	**45000**

(4)

Step -2: Statement of Cost per Equivalent Unit

Costs to be Accounted for	**Total Rs.**	**Materials Rs.**	**Conversion Cost Rs.**
Opening WIP	0	0	0
Direct Material	49875	49875	
Direct labour(500 x 5)	2500		2500
Over Heads (2500 x 44%)	1100		1100
	53475	49875	3600
Cost Per Equivalent		1.05	0.08

(4)

Step-3: Process Account

	Material	**Conversion Cost**	**Total**
Out Put	41000 x 1.05 = 43050	41000 x 0.08 = 3280	46330
Normal Loss	0 x1.05 = 0	0 x 0.08 =0	0
Closing WIP	5000 x 1.05 = 5250	2500 x 0.08 = 200	5450
Abnormal Loss	1500 x 1.05 = 1575	1500 x 0.08 = 120	1695
Total Cost(Agreed With Step-2)	49875	3600	53475

(5)

Process 2 A/C

	Unit	Rs.		Unit	Rs.
DM	50000	49875	Out Put	41000	46330
DL		2500	Normal Loss	2500	0
O/H		1100	Closing WIP	5000	5450
			Abn. Loss	1500	1695
	50000	53475		50000	53475

(1)

Total Marks 15

Ans 8

FIFO Method:

	Receipt/(Issues)			Balance/(Quantity)		
Date	**Quantity**	**Price(Rs.)**	**Value(Rs.)**	**Rs.50**	**Rs.60**	**Rs.70**
March 9	800	50	40000	800		
March 10	(300)	50	(15000)	(300)		
March16	500	60	30000		500	
March 19	(300)	50	(15000)	(300)		
March 25	(200)	50	(10000)	(200)		
	(100)	60	(6000)		(100)	
March 28	700	70	49000			700
March 29	(300)	60	(18000)		(300)	
March 31(Bal)	**800**		**55000**	**0**	**100**	**700**

(4)

Value of Issues (Rs.15000+Rs.15000+Rs.10000+Rs.6000+Rs.18000) =Rs64000

Value of Closing Stock =Rs.55000

Rs.119, 000

(1)

Total Marks 5

Auditing

(Final Level)

Summer Exam-2014

Corporate Sector

Auditing

Ans. 1. (a)	• Ensure suitably qualified to act as auditor. • Ensure relevant resources exist within the firm. • Ensure timelines can be met within current work commitments. • Perform background check over the client – ensure clean track record, Professional management, significant issues expected and whether audit risk is manageable. • Obtain professional clearance from predecessor auditor. **Up to 1 mark for a valid description**	**05**
Ans. 1. (b)	• Disclosure is permitted by law and is authorized by the client. • Disclosure is required by law (e.g. production of documents in course of legal proceedings). • There is a professional duty or right to disclose **One (1) mark for each situation if properly described, vague description not to be given a full mark**	**05**
	Total Marks 10	
Ans. 2. (a)	• Banks and Financial institutions. • Prospective investors and shareholders. • Employees. • Tax Authorities. • Regulatory Authorities. • Suppliers. • Competitors. **Half (1/2) mark for each user (explanations are not required)**	**04**
Ans. 2. (b)	• Auditor's work is permeated by judgement. • Audit is of a TEST NATURE. • Materiality is applied. • Audit report is issued a long time after the balance sheet date. • Audit evidence is PERSUASIVE & not CONCLUSIVE. • Limitations in accounting and control systems. **One (1) mark for each valid limitation**	**05**
	Total Marks 09	

<table>
<tr><td>Ans. 3</td><td>(a) PERFORMANCE MATERIALITY:
Performance materiality means the amount or amounts set by the auditor at less than materiality for the financial statements as a whole to reduce to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatements exceeds materiality for the financial statements as a whole. If applicable, performance materiality also refers to the amount or amounts set by the auditor at less than the materiality level or levels for particular classes of transactions, accounts balances or disclosures.</td><td>02</td></tr>
<tr><td></td><td>(b) QUALITATIVE MATERIALITY:
Other than financial numbers, information in the financial statement may also be relevant and significant based on its nature. Such information is likely to be given importance by the reader of the financial statements irrespective of the monetary amount associated with it. For example, information in the financial statements about remuneration of the Chief Executive Officer and other Directors would be considered material based on qualitative characteristics. Similarly significant transactions with related parties would also be considered material.</td><td>02</td></tr>
<tr><td></td><td>(c) ADVOCACY THREAT:
Advocacy threats arise in those situations where the audit firm promotes a position or opinion to the point that subsequently objectivity is compromised. Examples would include commenting publicly on future events in particular circumstances, having made assertions without detailing the assumptions, or acting as an advocate on behalf of audit clients in litigation or disputes with third parties. Advocacy threats also arise if the firm promotes shares in a listed audit client.</td><td>02</td></tr>
<tr><td></td><td>(d) LOWBALLING:
When an auditor quotes a significantly lower fee for an audit service that charged by the predecessor firm, there is a significant self-interest threat to independence of the auditor. This is because in the future, the auditor may compromise on objectivity in order not to displease the client so as to continue the client relationship which had started with a possibly loss-making fee arrangement.</td><td>02</td></tr>
<tr><td></td><td>(e) STATISTICAL SAMPLING:
An approach to sampling that has the following characteristics:
(i) Random Selection of the sample items; and
(ii) The use of probability theory to evaluate sample results, including measurement of sampling risk.

One (1) mark for a basic definition and an additional one (1) mark for adequate description or example, as applicable</td><td>02</td></tr>
<tr><td></td><td colspan="2">Total Marks 10</td></tr>
</table>

Ans. 4	• Conduct a cash count at the end of business on the last day or prior to commencement on the first day of the next year and ensure the cash in hand shown by ABC limited matches the physical cash held. • Obtain documentation from the custodian of cash as audit evidence; obtain last documents of cash receipts and cash payments to ensure cut-off has been applied appropriately. • If the date of the count is different from the year end date, ensure appropriate work-back procedures are performed. • Obtain a certificate or statement of cash in hand from the management of the company. • Obtain standard bank confirmations from each bank with which ABC limited has conducted banking operations and transactions. • Re-perform an arithmetic check on the bank reconciliation statements. • Trace cheques shown as outstanding on the bank reconciliation to the cash book prior to the year end and to the subsequent bank statements and obtain explanations from any large or unusual items not cleared at the time of the audit. • Compare cash book and bank statements in detail for the last month of the year. • Review other bank reconciliations on a sample basis to ensure regular clearance of outstanding items • Verify any contra items in the bank statements or cash books maintained by ABC limited. • Inspect the cash book and bank statements for any large, unusual, one-off or unique transactions and inquire from management about the purpose of the same. • Inquire from management if any of the savings, current or term deposit accounts are secured against any loan facility availed by ABC Limited, in which case a disclosure of the same may be suggested in the financial statements. • Determine whether the bank accounts are subject to any restrictions. **One (1) mark for each procedure appropriately related to ABC limited's disclosure in the financial statement, deduct marks for vague explanations or generic cash and bank audit procedures**	
	Total Marks 15	

<table>
<tr><td>Ans. 5.
(a)</td><td>

All insurance officers in all branches may not be accounted for in the accumulation and calculation of payroll.
One insurance officer may be paid twice.
An insurance officer may overstate the amount of commission earned by him by misstating premium numbers.
Appropriate approvals may not be in place for the working of commission.
Timely communication of commission may not be made.
HR Department may not ensure the existence of an insurance agent prior to payment of salary.
List of employees, days worked and similar information may not be the same with the Finance, HR and Insurance sub-departments.
Increments may not be calculated correctly.
Deductions of items such as tax and loan deductions, and perks / benefits / privileges may not be appropriately accounted for.
Increments may not be applied at the correct rate.
Increments may not be applied on time.
Double promotion or increment may be accounted.
Payment to employees may not correspond to the amount they are entitled / eligible to get.
Departmental bonus may be overstated by the insurance agents' incorrect working or collusion within the sub-departments of insurance.
Tax workings may not take into account the departmental bonus and commissions, resulting in less deduction of tax from employee salaries.
Effect of leavers and joiners may not be accounted for on a timely basis i.e. an employee who has left may still be paid a salary.

One mark for each valid control risk if properly explained
</td><td>08</td></tr>
<tr><td>Ans. 5.
(b)</td><td>

Obtain consolidated salary sheets for a sample from 12 months to ensure the total amount as per salary sheet matches the amount recorded in the general ledger.
Perform an analytical review on the salaries expense by preparing a trend analysis of total salary per month; identify if the movements in the trend correspond to the increment, promotions, leavers and joiners.
Prepare another monthly trend analysis of commission expense and correlate with insurance premium earned by the company to ensure that any excess commission paid to insurance officers corresponds to increase in insurance premium earned by Connect.

</td><td>08</td></tr>
</table>

	• Select a sample of insurance officers from each branch and ensure their commission calculations are correct by inspecting the insurance premium record and recalculating the commission. • Obtain a sample from the quarterly departmental bonus calculations and ensure accuracy of calculation. • Match the information in the departmental bonus calculation with the underlying record of insurance premium. • On a sample basis, ensure that any insurance premiums shown in the commission and bonus workings were actually realized in cash as well by tracing the premium amounts to Connect's bank statement. • Select a sample of joiner / new recruits and ensure their payroll was commenced from the date they joined. • Match a sample of new recruit's payroll with their appointment letters. • Select a sample of leavers and ensure they were stopped payment of salary from the date of leaving by performing a review of subsequent salary sheets. • Select a sample or promotions and match the amount paid with the promotion letters issued to and acknowledged by the relevant employees. • Select a sample of increments and apply recalculation procedures to ensure accurate calculation of increment and tax effect thereon.	
	Total Marks 16	
Ans. 6	Answer should be based around the following points (Difference in candidates' expression to be judged)	
	(a) Manufacturing client - inventory likely to be material, physical verification is an important audit procedure to obtain assurance over the existence and valuation assertions. Quality of evidence is of highest level since it is auditor-derived evidence. Amount being material would result in modification of the audit opinion. Assuming other items such as fixed assets, receivable and liabilities are also of similar or larger amount, a pervasive effect is unlikely, therefore a qualified opinion would suffice.	**04**
	(b) As per IAS-37, definition of provision appears to have been met by the company's act of installation of power plant. Substantial time and effort point towards materiality of the provision. Despite being material, the effect is likely to be confined to a single area of the financial statements and would therefore not be pervasive. Qualified opinion should be expressed.	**04**
	(c) Such as significant amount being unaudited due to inability to obtain sufficient appropriate audit evidence. Further, absence of lawyer, tax and bank	

	confirmations means the impact is not confined to a single area of the financial statements. Qualification would not seem suitable since too many items in the financial are impacted. Disclaimer of opinion should be given.	**04**
	(d) Although company formation was 2 year ago and therefore there can be an argument that fixed assets are new, the nature of business is such that technological changes can quickly render the entire plant and machinery obsolete in limited time. The item is likely to be material to the financial statements based on qualitative factors as well. However, the fact that similar companies have carried out the test but no impairment was identified indicates that there may not be a possible adjustment to the financial right now (although such an adjustment could occur in the future). On a conservative note and to avoid any risk, consideration should be given to include an emphasis of matter paragraph in the financial statements, but the opinion should not be qualified.	**04**
	(e) Non- disclosure as a going concern can misled to the users of the financial statements. It would therefore be inappropriate on the part of the auditor not to raise this matter in the audit report. The overall impact of the non-disclosure must be considered and if pervasive, an adverse opinion should be expressed. Otherwise, at least a qualified opinion should be given. **Up to 2 marks for providing a basis and one mark for stating the opinion in response to that basis**	**04**
		Total Marks 20
Ans. 7	'Expert' a person or firm possessing special skill, knowledge and experience in a particular field other than accounting or audit. As per ISA 620, an auditor can either make use of the management expert or use his own expert (Known as the 'auditor expert'). When determining need for an expert, consider i) engagement teams knowledge and previous experience ii) risk of material misstatement based on nature, complexity and materiality of the matter iii) quantity and quality of other audit evidence to be obtained. Auditor should evaluate professional competence, capability and objectivity of the expert. In situations where the auditor finds that the expert possesses adequate amount of competence and objectivity, the auditor can use the expert's work to reduce the nature, timing and extent of his procedures. For example, if an entity follows the revaluation model Under IAS 16, management may engage a professional valuer as an expert to determine with certain degree of judgment, the value of its land and buildings. The auditor can then either make use of the management expert or utilize the services of his expert to assess whether the value appearing in the balance sheet of the said company seems to be a reasonable approximation of the revalued amount as per IAS 16 criteria.	

	An auditor would usually have to review the significant assumptions used by the expert to challenge those assumptions. To take another example, many companies hire subject matter specialist lawyers to advocate on their behalf in cases of litigation involving complex matters. In such situations too, the auditor with all his financial expertise would not be in a position to decide about the possible outcome of a matter or the 'strength' in a particular case. A lawyer engaged as an expert would therefore be able to provide insights as regards the above. An auditor is also required to evaluate appropriateness of the expert's work in relation to the assertion being addressed and to ensure whether assumptions used by the expert appear to be reasonable. Auditor's report should not refer to the work of an expert. **Up to 1 mark for each point provided adequately explained**	
		Total Marks 10
Ans. 8	The auditor should comply with the ethical requirements relevant to the audit of the annual financial statements of the entity. These ethical requirements govern the auditor's professional responsibilities in the following areas: independence, integrity, objectivity, professional competence and due care, confidentiality and professional behavior. The objective of an engagement to review interim financial information is to enable the auditor to express a conclusion whether, on the basis of the review, anything has come to the auditor's attention that causes the auditor to believe that the interim financial information is not prepared, in all material respects, in accordance with an applicable financial reporting framework. The auditor makes inquiries, and performs analytical and other review procedures in order to reduce to a moderate level the risk of expressing an inappropriate conclusion when the interim financial information is materially misstated. The auditor and the client should agree on the terms of the engagement. The auditor should have an understanding of the entity and its environment, including its internal control, as it relates to the preparation of both annual and interim financial information, sufficient to plan and conduct the engagement so as to be able to: a) Identify the types of potential material misstatement and consider the likelihood of their occurrence; and b) Select the inquiries, analytical and other review procedures that will provide the auditor with a basis for reporting whether anything has come to the	

auditor's attention that causes the auditor to believe that the interim financial information is not prepared, in all material respects, in accordance with the applicable financial reporting framework.

The auditor uses the understanding of the entity and its environment, including its internal control, to determine the inquiries to be made and the analytical and other review procedures to be applied and to identify the particular events, transactions or assertions to which inquiries may be directed or analytical or other review procedures applied.

The auditor should make inquiries, primarily of persons responsible for financial and accounting matters, and perform analytical and other review procedures to enable the auditor to conclude whether, on the basis of the procedures performed, anything has come to the auditor's attention that causes the auditor to believe that the interim financial information is not prepared, in all material respects, in accordance with the applicable financial reporting frame work.

The auditor ordinarily performs the following procedures:

- Reading the minutes of the meetings of shareholders, those charged with governance, and other appropriate committees to identify matters that may affect the interim financial information, and inquiring about matters dealt with at meetings for which minutes are not available that may affect the interim financial information .
- Considering the effect, if any, of matters giving rise to a modification of the audit or review report, accounting adjustments or unadjusted misstatements, at the time of the previous audit or reviews.
- Communicating, where appropriate, with other auditors who are performing a review of the interim financial information of the reporting entity's significant components.
- Inquiring of members of management responsible for financial and accounting matters, and others as appropriate about the following:
  - Whether the interim financial information has been prepared and presented in accordance with the applicable financial reporting framework.
  - Whether there have been any changes in accounting principles or in the methods of applying them.
  - Whether any new transactions have necessitated the application of a new accounting principle.
  - Whether the interim financial information contains any known uncorrected misstatements.
  - Unusual or complex situations that may have affected the interim financial

information, such as a business combination or disposal of a segment of the business.

- Significant assumptions that are relevant to the fair value measurement or disclosures and management's intention and ability to carry out specific courses of action on behalf of the entity.
- Whether related party transactions have been appropriately accounted for and disclosed in the interim financial information.
- Significant changes in commitments and contractual obligations.
- Significant changes in contingent liabilities including litigation or claims.
- Compliance with debt covenants.
- Matters about which questions have arisen in the course of applying the review procedures.
- Significant transactions occurring in the last several days of the interim period or the first several days of the next interim period.
- Knowledge of any fraud or suspected fraud affecting the entity involving:
  a) Management;
  b) Employees who have significant roles in internal control; or
  c) Others where the fraud could have a material effect on the interim financial information.
- Knowledge of any allegations of fraud, or suspected fraud, affecting the entity's interim financial information communicated by employees, former employees, analysts, regulators, or others.
- Knowledge of any actual or possible noncompliance with laws and regulations that could have a material effect on the interim financial information.

- Applying analytical procedures to the interim financial information designed to identify relationships and individual items that appear to be unusual and that may reflect a material misstatement in the interim financial information. Analytical procedures may include ratio analysis and statistical techniques such as trend analysis or regression analysis and may be performed manually or with the use of computer-assisted techniques.
- Reading the interim financial information, and considering whether anything has come to the auditor's attention that causes the auditor to believe that the interim financial information is not prepared, in all material respects, in accordance with the applicable financial reporting framework.
- The auditor should obtain evidence that the interim financial information agrees or reconciles with the underlying accounting records. The auditor may obtain evidence that the interim financial information agrees or reconciles with the underlying accounting records by tracing the interim financial

information to:

a) The accounting records, such as the general ledger, or a consolidating schedule that agrees or reconciles with the accounting records; and

b) Other supporting data in the entity's records as necessary.

The auditor should obtain written representation from management that:

a) It acknowledges its responsibility for the design and implementation of internal control to prevent and detect fraud and error;

b) The interim financial information is prepared and presented in accordance with the applicable financial reporting framework;

c) It believes the effect of those uncorrected misstatements aggregated by the auditor during the review are immaterial, both individually and in the aggregate, to the interim financial information taken as a whole. A summary of such items is included in or attached to the written representations;

d) It has disclosed to the auditor all significant facts relating to any frauds or suspected frauds known to management that may have affected the entity;

e) It has disclosed to the auditor the results of its assessment of the risks that the interim financial information may be materially misstated as a result of fraud;

f) It has disclosed to the auditor all known actual or possible noncompliance with laws and regulations whose effects are to be considered when preparing the interim financial information; and

g) It has disclosed to the auditor all significant events that have occurred subsequent to the balance sheet date and through to the date of the review report that may require adjustment to or disclosure in the interim financial information.

One (1) mark for each valid point

Total Marks 10