Corporate Sector

Model Solutions

Winter Exam-2014

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Pakistan Institute of
Public Finance Accountants

Financial Accounting

(Intermediate Level)

Ans. 1(a). **Potential User Groups are:**

01). Shareholders
02). Management
03). Creditors
04). Employees
05). Pressure Group
06). Tax Authority
07). Investors
08). Government

Ans. 1(b). **(i) According to IAS-01-A Liability should be classified as a current liability when it:**

- **(i)** Is expected to be settled in the normal course of the enterprise's operating cycle; or
- **(ii)** Is due to be settled within Twelve months of the balance sheet date.

(ii) According to IAS-01-An Asset should be classified as a current assets when it:

- **(i)** Is expected to be realized in, or is held for sale or consumption, in the normal course of the enterprises operating cycle; or
- **(ii)** Is held for trading purposes or for the short-term and expected to be realized within twelve months of the balance sheet date; or
- **(iii)** Is cash or cash equivalent asset which is not restricted in its use.

Total Marks 11

Ans. 2.

Mr. X
Statement of Cash Flows
For the year ended December 31, 2013

05

CASH FLOW FROM OPERATING ACTIVITIES			
Profit before Taxes	**W-01**		220,200
Adjustments for :			
Depreciation	**W-02**	23,200	
Loss on Disposal of Equipments	**W-03**	7,300	
Profit on Disposal of Furniture	**W-03**	(11,000)	
Profit on Sale of Investments		(7,500)	12,000
OPERATING PROFIT BEFORE WORKING CAPITAL CHANGES			232,200
Increase in Debtors (31,700-21,500)		(13,400)	
Increase in Inventory (25,000-19,400)		(5,600)	
Increase in Creditors (10,800-6,500)		4,300	
Decrease in Accrued Expenses (10,800-4,300)		(6,500)	
Decrease in Bills Payable (8,600-6,500)		(2,100)	(23,300)
Cash Flow from Operating Activities			208,900

CASH FLOW FROM INVESTING ACTIVITIES				04
Sale Proceeds of Equipment		6,500		
Purchase of Equipment	**W-04**	(66,000)		
Insurance Claim		60,000		
Purchase of Furniture	**W-04**	(80,000)		
Sale of Investments (16,900+7500)		24,400	(55,100)	
Cash used in Investing Activities			153,800	
CASH FLOW FROM FINANCING ACTIVITIES				02
Additional Capital		12,000		
Repayment of Loan		(22,000)		
Drawings (15,000x12)		(180,000)	(190,000)	
Net Increase in Cash and Cash Equivalents			(36,200)	01
Opening Balance of Cash and Cash Equivalents			41,400	
CLOSING BALANCE OF CASH AND CASH EQUIVALENTS			**5,200**	

WORKING NOTES

W-01 - CAPITAL ACCOUNT

Balance Brought Forward	83,800
Balance Carried Forward	136,000
Increase in Captial Account	52,200
Additional Capital	(12,000)
Drawings (15,000x12)	180,000
Profit for the year	220,200

W-02 - DEPRECIATION

	Furniture	Equipment	
Balance Brought Forward	15,000	18,000	
Balance Carried Forward	8,000	24,000	
Increase in Depreciation	(7,000)	6,000	
Depreciation on Disposal	15,000	9,200	
Depreciation for the year	8,000	15,200	
Total Depreciation			**23,200**

W-03 - GAIN ON SALE OF ASSETS

	Furniture	Equipment
Cost	64,000	23,000
Less Accumulated Depreciation	15,000	9,200
Net Book Value of Equipmet	49,000	13,800
Sold	60,000	6,500
Gain on Sale of Equipment	(11,000)	7,300

W-04 - FIXED ASSETS

	Furniture	Equipment
Balance Brought Forward	64,000	43,000
Balance Carried Forward	80,000	86,000
Increase in Fixed Assets	16,000	43,000
Disposal of Equipmet	64,000	23,000
Total Increase in Fixed Assets	80,000	66,000

Total Marks 12

Ans. 3.

	Modern	Style365
1 Net Profit as % of Sales		
Net Profit / Sales x 100	100,000/555,000	150,000/750,000
	18.02%	20.00%

Comments:
Net profit of Style365 is better than Modern in spite of the fact the gross profit margin is lower. Possible reason is the effective management of expenses by Style365.

	Modern	Style365
2 Inventory Turnover		
Cost of Goods Sold / Average Inventory	240,000/(100,000+60,000)/2	330,000/(800,000+70,000)/2
	3.00 Times	4.40 Times

Comments:
Style365 inventory turnover is better than Modern this might be because of bulk purchase discount offered to customers.

	Modern	Style365
3 Accounts Receivable / Sales Ratio		
Accounts Receivable / Sales x 12	125,000/555,000	100,000/750,000
	2.73 Months	1.60 Months

Comments:
On average Modern's debtors take more time than Style365. This is because of inefficiency on the part of credit control department or deliberate policy to boost sales.

	Modern	Style365
4 Accounts Payable / Purchase Ratio		
Accounts Payable / Purchase x 12	104,000/200,000	100,500/320,000
	6.24 Months	3.77 Months

Comments:
Modern takes almost double time to pay its creditors. Because of working capital problem Company is delaying creditor's payment to avoid bank overdraft.

	Modern	Style365
5 Return on Capital employed on average capital basis.		
Net Profit / Average Capital x 100	100,000/(76,000+116,000)/2	150,000/(72,000+152,000)/2
	104.17%	133.93%

Comments:
ROCE of Style365 is clearly better than Modern. Good profitability is the sign of good return.

Based on the reasons mentioned above and put all these factors together it appears that Style365 business is being run more efficiently, and is more profitable as consequence.

Total Marks 15

Ans. 4.

Cost of Equipment	
Cost Paid	3,000,000
Add Import Duty	1,000,000
Other Non-refundable Taxes	60,000
Transportation Cost	10,000
Insurance in Transit	4,000
Cost of Equipment	**4,074,000**
Useful Life	05 Years
Salvage Value	350,000
Depreciation for June 30, 2012 = (4,074,000-350,000) / 5	744,800
During 2012-13 the useful life revised to	5 Years
During 2012-13 the salvage value is estimated	400,000

Revised Depreciation on the basis of Remaining Life and Salvage Value

Depreciation for June 30, 2013 and 2014	(4,074,000-744,800-400,000) / 5	585,840

(a) Depreciation Expenses for the years ending

30-Jun-12	744,800
30-Jun-13	585,840
30-Jun-14	585,840
Depreciation for year June 30, 2012, 13 and 14.	**1,916,480**

(b) Exchange Gain / Loss on Disposal

Equipment Cost	4,074,000
Accumulated Depreciation	1,916,840
Book Value	2,157,160
Less Cash Value	2,800,000
Exchange Gain on Disposal	**642,840**

Income Tax & Fire Insurance are not to be capitalized.

Total Marks 08

Ans. 5.

SHIFA DISTRIBUTORS
Trading Profit and Loss Account
For the Period ended June 24, 2014

Sales	W-01		9,000,000
Less Cost of Sales			
Opening Stocks		1,250,000	
Add Purchases	W-02	9,125,000	

Pakistan Institute of Public Finance Accountants

Available for Sales	10,375,000	
Closing Stock	**2,875,000**	
Cost of Sales		7,500,000
Gross Profit = 20% on Cost i.e., 9,000,000 x 20/120		**1,500,000**

The Stock Lost in Flood Rs. 2,875,000/=.

W-01 - SALES

Gross Sales	9,625,000
Add Un-recorded Sales	625,000
Less Sales Return	(1,250,000)
Total Sales during the period	**9,000,000**

W-02 - PURCHASES

Gross Purchases	8,250,000
Less Purchase Return	(375,000)
Add Frieght on Purchases	1,250,000
Total Purchase during the period	**9,125,000**

Total Marks 06

Ans. 6.

CASH ACCOUNT

RECEIPTS		**PAYMNETS**	
Particulars		**Particulars**	
Opening Balance	14,000	Drawings (3,500 x 52)	182,000
Sale of Investments	30,000	Salaries (13,000 x 12)	156,000
Profit on Investments	5,200	Wages	5,200
Accounts Receivables	2,873,000	Miscellaneous Expenses	7,800
		Purchases (2,000 x 52)	104,000
		Cash Deposited	2,450,200
		Closing Balance	17,000
	49,200		2,922,200

BANK ACCOUNT

RECEIPTS		**PAYMNETS**	
Particulars		**Particulars**	
Opening Balance	275,200	Accounts Payable	2,158,000
Cash Deposited	2,450,200	Rent	75,000
		Rates	14,400
		Electricity	9,200
		Repair	8,400
		Insurance	4,000
		Miscellaneous Expenses	5,200
		Drawings	90,000
		Closing Balance	361,200
	2,725,400		2,725,400

ACCOUNTS PAYABLE

RECEIPTS		PAYMNETS	
Particulars		**Particulars**	
Bank	2,158,000	Opening Balance	94,000
Cash	104,000	Purchases	2,270,000
Ending Balance	102,000		
	2,364,000		2,364,000

TRADE DEBTORS

Particulars		**Particulars**	
Balance B/d	19,000	Cash	2,873,000
Sales	2,881,000	**Bad Debts**	5,000
		Ending Balance	22,000
	2,900,000		2,900,000

Mr. ASLAM
Trading Profit and Loss Account
For the Period ended June 30, 2014

Sales		2,881,000
Less Cost of Sales		
Opening Stocks	115,000	
Add Purchases	2,270,000	
Available for Sales	2,385,000	
Closing Stock	80,200	
Cost of Sales		2,304,800
		576,200

Total Marks 18

Ans. 7.

ABC TEXTILES LIMITED
Profit and Loss Account
For the Year ended June 30, 2014

			Rupees in '000s
Sales			17,628,000
Less Cost of Goods Sold	**W-01**		7,476,000
Gross Profit			10,152,000
Less : Administrative Expenses	**W-02**	(3,624,000)	
Less : Selling & Distribution Expenses	**W-03**	(875,000)	
			(4,499,000)
Profit from Operations			5,653,000
Financial Charges			(609,000)

Profit before Tax		5,044,000
Provision for Taxation		
Current	500,000	
Prior	175,000	
		(675,000)
Net Profit for the period		4,369,000

ABC TEXTILES LIMITED
Balance Sheet
as on June 30, 2014

			Rs. in '000s
EQUITY AND LIABILITIES			
EQUITY			
Paid-up Capital		3,000,000	
Share Premium		1,500,000	
Un-appropriated Profit		4,609,000	
Total Equity			9,109,000
Current Liabilities			
Sundry Creditors		1,575,000	
Accrued Expenses (Sales Tax Payable)		2,085,000	
Short Term Bank Loan		500,000	
			4,160,000
TOTAL EQUITY AND LIABILITIES			**13,269,000**
ASSETS			
Non-current assets	**W-04**		9,579,000
Current Assets			
Closing Stocks		2,400,000	
Debtors (1,314,000-114,000-60,000)		1,140,000	
Cash at Bank		150,000	
			3,690,000
Total Assets			**13,269,000**

ABC TEXTILES LIMITED
Statement of Changes in Equity
For the year ended June 30, 2014

	Capital	Share Premium	Retain Earning	Total
Opening Balance July 01, 2013	1,500,000	750,000	840,000	3,090,000
Prior Year's Adjustment - Inventory			(300,000)	(300,000)
	1,500,000	750,000	540,000	2,790,000
Issue of Shares during the Year	1,500,000	750,000		2,250,000
Profit for the Year			4,369,000	4,369,000

Dividend Paid			(300,000)	(300,000)
	3,000,000	1,500,000	4,609,000	9,109,000

ABC TEXTILES LIMITED
Notes to the Accounts
For the year ended June 30, 2014

W-01 COST OF GOODS SOLD

Opening Stock	3,300,000
Purchases	6,300,000
	9,600,000
Less Closing Stocks	2,400,000
	7,200,000
Depreciation	276,000
Cost of Goods Sold	**7,476,000**

W-02 ADMINISTRATIVE EXPENSES

Salaries	500,000
Miscellaneous Admin Expenses	2,000,000
Audit Fees	200,000
Depreciation	750,000
Bad Debts Expenses	114,000
Provision for Bad Debts (1,314,000-114,000)*5%	60,000
Total Administrative Expenses	**3,624,000**

W-03 SELLING EXPENSES

Sales Staff Salaries	200,000
Miscellaneous Admin Expenses	250,000
Distribution Expenses	250,000
Depreciation	75,000
Advertisement Expenses	100,000
	875,000

W-04 NON-CURRENT ASSETS

	Building	Plant	Motor Vehicle	Total
Opening Balance as on July 01, 2013	15,000,000	2,100,000	480,000	17,580,000
Accumulated Depreciation	6,000,000	720,000	180,000	6,900,000
Written Down Value	9,000,000	1,380,000	300,000	10,680,000
Depreciation Rate	5%	20%	25%	10%
Depreciation for the Year	750,000	276,000	75,000	1,101,000
Accumulated Depreciation June 30, 2014	6,750,000	996,000	255,000	8,001,000
Written Down Value as on June 30, 2014	**8,250,000**	**1,104,000**	**225,000**	**9,579,000**

Total Marks 24

Ans. 8.

Cost

An amount that has to be paid or given up in order to get something in the business. In business, cost is usually monetary valuation of 1). Effort and 2). Material

OR

In business and accounting cost is the monetary value spent by a company to produce a product. It does not include Profit and Mark-up.

OR

In accounting cost is defined as the cash amount (or the cash equivalent) given up for an asset. Cost includes all costs necessary to get an asset in place and ready for use.

Cost comprises of

- Cost of purchase (including Taxes, Transport & Handling) net of trade discount received.
- Conversion Cost (including fixed & variable manufacturing overheads)
- Other Costs (incurred in brining inventories to their present location and condition)

Net Realizable Value

It is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.

Total Marks 06

Performance Measurement

(Intermediate Level)

Ans. 1.

(a) The flexed budget will be based on the actual activity level of 90,000 units. **05**

	Rs.	Rs.
Sales Rs.950,000 × 90/95 =		900,000
Cost of sales		
Raw materials 133,000 × 90/95 =	126,000	
Direct labour:152,000 × 90/95 =	144,000	
Variable production overheads:	95,400	
Fixed production overhead:	125,400	490,800
		409,200

(b)

(i) Raw materials cost total variance = 126,000 – 130,500 = Rs.4,500 (Adverse). **03**

(ii) Direct labour cost total variance = 144,000 – 153,000 = Rs.9,000 (Adverse) **03**

(iii) Fixed overhead absorption rate = 125,400 / 28,500 = Rs.4.40 per machine hour **04**
Standard machine hours for actual production = 28,500 × 90/95 = 27,000 hours
Standard fixed overhead (actual production) = 27,000 × 4.4 = Rs.118,800
Fixed overhead absorbed on actual hours = 27,200 × 4.4 = Rs.119,680
Fixed overhead efficiency variance = 118,800 – 119,680 = 880 (Adverse)

(iv) Fixed overhead absorbed on actual hours = 27,200 × 4.4 = Rs.119,680 **04**
Fixed overhead absorbed on budgeted hours = 28,500 × 4.4 = Rs.125,400
Fixed overhead capacity variance = 119,680 – 125,400 = Rs.5,720 (Adverse)

(v) Budgeted overhead expenditure = Rs.125,400 **04**
Actual overhead expenditure = Rs.115,300
Fixed overhead expenditure variance = 125,400 – 115,300 = Rs.10,100 (Favourable)

(c)

(i) **02**
- Different suppliers were used and these charged a lower price (favourable price variance) than the usual supplier.
- Materials were purchased in sufficient quantities to obtain a bulk purchases discount (a quantity discount, resulting in a favourable price variance.

(ii) **02**
- Using employees who are less experienced than 'standard', resulting in adverse efficiency variances.
- An event causing poor morale

(iii) **02**
- Efficient working by direct labour: a favourable labour efficiency variance results in a favourable fixed overhead efficiency variance.
- Working more hours or less hours than budgeted (capacity variance).

Total Marks 29

Ans. 2.

	X (Rs.)	Y (Rs.)	Marks
Material cost	1.50	4.00	02
Labour cost	7.00	3.50	02
	8.50	7.50	
Overhead cost:			06
Set-up			
$\frac{Rs.20{,}000}{40} = Rs.500\ per\ set-up$			
$X: \frac{Rs.500 \times 30}{45{,}000}$	0.33		
$Y: \frac{Rs.500 \times 10}{5{,}000}$		1.00	
Purchasing			
$\frac{Rs.16{,}000}{80} = Rs.200\ per\ order$			
$X: \frac{70 \times Rs.200}{45{,}000}$	0.31		
$Y: \frac{10 \times Rs.200}{5{,}000}$		0.40	
Labour supervision			
$X, Y: \frac{Rs.23{,}750}{47{,}500} = Rs.0.50\ per\ labour\ hour$	0.50	0.25	
Total unit cost	Rs.9.64	Rs.9.15	

Total Marks 10

Ans. 3.

(a) <u>Break-even analysis</u> 05

Break-even point = $\frac{Total\ fixed\ cost}{Contribution\ per\ pair}$

Contribution per pair = Selling price – Variable cost = Rs.40 – Rs.25 = Rs.15

Break-even point = $\frac{Rs.100{,}000 + Rs.40{,}000 + Rs.100{,}000}{Rs.15} = \frac{Rs.240{,}000}{Rs.15}$

= 16,000 units

Margin of safety = Current levels of sales – Break-even sales
= 25,000 – 16,000 = 9,000 units

(b) <u>Net income from sale of 20,000 units</u> 05

	Rs.
Contribution: (20,000 × Rs.15)	300,000
Less: Fixed costs	(240,000)
Net profit	60,000

Total Marks 10

Ans. 4.

Physical flows 02

	Units
Work in process, 1 December	15,000
Units started	30,000
To account for	45,000
Units completed:	
From opening work in process	15,000
From units started in period*	25,000
Work in process as 31 December	5,000
Units account for	45,000

Equivalent units of work in the period: 02

	Materials Rs.	Conversion Rs.
Units completed:		
From opening work in process (3/5)	-	9,000
From current production	25,000	25,000
Work in process at December (1/2)	5,000	2,500
	30,000	36,500

Cost to be accounted for:

	Rs.	Rs.	Rs.
Work in process at 1 December			10,250
Costs added in the period	Rs.24,750	Rs.20,000	44,750
			Rs.55,000

Costs per equivalent unit: 02

$$\frac{Rs.24{,}750}{30{,}000} = Rs.0.825 + \frac{Rs.20{,}000}{36{,}500} = Rs.0.548 \quad = \quad \text{Rs.}1.373$$

Cost of finished production: 06

		Rs.	Cost Rs.
From opening work in process			
Value at 1 December		10,250	
Add: Conversion, 9,000 × Rs.0.548		4,930	
			15,180
Started and completed in period:			
Materials	25,000 × Rs.0.825	20,625	
Conversion	25,000 × Rs.0.548	13,700	
Total	25,000 × Rs.1.373		34,325
Total value of work completed			49,505
Value of work in process:			
Materials, 5,000 × Rs.0.825		4,125	
Conversion, 2,500 × Rs.0.548		1,370	
Total value of work in process			5,495
Total costs for period			Rs.55,000

Process Account — 03

	Units	Rs.		Units	Rs.
Opening WIP	15,000	10,250	Output	40,000	49,505
Materials	30,000	24,750	Closing WIP	5,000	5,495
Conversion cost	-	20,000			
	45,000	Rs.55,000		45,000	55,000

Total Marks 15

Ans. 5.

(a) Component A should always be bought out regardless of any limiting factors, as its variable cost of production is higher than the outside purchase price. — 04

(b) If machine hours are limited to 4,000 hours: — 04

	Component B	Component C
Excess cost	Rs.2	Rs.6
Machine hours per unit	0.5	2
Excess cost per machine hour	Rs.4	Rs.3

Component C has the lowest excess cost per limiting factor and should, therefore, be bought out.

(c) If labour hours are limited to 4,000 hours: — 04

	Component B	Component C
Excess cost	Rs.2	Rs.6
Labour hours	2	4
Excess cost per labour hour	Rs.1	Rs.1.50

Therefore, component B has the lowest excess cost per limiting factor and should be bought out.

Total Marks 12

Ans. 6.

	2013	2012	Marks
Current ratio	$\frac{626.8}{599.1}$ = 1.05	$\frac{654.4}{642.2}$ = 1.02	03
Quick ratio	$\frac{584.1}{599.1}$ = 0.97	$\frac{576.4}{642.2}$ = 0.90	03
Accounts receivables collection Period	$\frac{295.2}{2,176.2}$ x 365 = 49.5 days	$\frac{335.5}{2,344.8}$ x 365 = 52.2 days	03
Inventory turnover period	$\frac{42.7}{1,659.0}$ x 365 = 9.4 days	$\frac{78.0}{1,731.5}$ x 365 = 16.4 days	03
Accounts payable payment period	$\frac{190.8}{1,659.0}$ x 365 = 42.0 days	$\frac{188.1}{1,731.5}$ x 365 = 40.0 days	03

Total Marks 15

Ans. 7.	**(a) Flexible Budget:** Flexible budget is a budget which by recognizing the difference in behavior between fixed and variable costs in relation to fluctuations in output, turnover, or other variable factors, etc. It is designed to change in relation to the level of activity actually attained.	**03**
	(b) Normal Loss: The loss expected during the normal course of operation, for unavoidable reasons is called normal loss and this is due to inherent result of the particular process and thus uncontrollable in the short run. Management, over time, are usually able to identify an average percentage of normal loses expected to arise from the production process. For example, 100 kg, introduced into the production process and on an average 95 kg. comes out after the process, we can say that the normal process loss is 5%	**03**
	(c) Abnormal Gain: If the loss is less than the normal expected loss, the difference is considered as abnormal gain. Abnormal gain is accounted similar to that abnormal loss. Abnormal gains will be debited to the process account and credited to an abnormal gain accounts. The abnormal gain account is debited with the figure of reduced normal loss in quantity and value. At the end of the accounting year the balance in the abnormal gains account will be carried to Profit and Loss Account.	**03**
		Total Marks 09

Bus. Commn. & Beh. Studies

(Intermediate Level)

Ans. 1	**There is not a single correct answer, but for guideline following paraphrase could be used.** Michelangelo had a tremendous memory. He could remember the details of works of art after having seen them just once. He copied these works, but changed them dramatically. He created copies in his own, unique style. As a result, few people ever realized some of his works were actually copies.	
		(Total Marks 08)
Ans. 2	The answers will vary but it must contain the following.	
	1. Direct request to grab the attention of the reader.	**3**
	2. Background of the situation.	**3**
	3. Persuasive details should be given to create interest and desire.	**3**
	4. Easy action to be taken by the reader should be mentioned.	**3**
		(Total Marks 12)
Ans. 3	Answers will vary but report must contain the following	
	1. Letter head	**1.5**
	2. Details of meeting date, time and venue.	**2.5**
	3. Signature of the Secretary	**1**
	4. Items proposed by following departments: a. Finance b. Sales c. Information Technology d. Human Resource	**10**
		(Total Marks 15)
Ans. 4	The answers will vary but must contain the following:	
	1. Introduction	**3**
	2. Problem details	**3**
	3. Reasons	**3**
	4. Impact on organization	**3**
	5. Suggestions	**3**
		(Total Marks 15)

Ans. 5	Following points must be kept in mind: 1. The précis should be all in your own words. 2. The précis must be a connected whole. It may be divided into sections or paragraphs, according to changes in the subject matter, but these must not appear as separate notes rather must be joined together in such a way as to be read continuously. 3. The précis must be complete and self-contained. In other words it must convey its message fully and clearly without requiring any reference to the original to complete its meaning. 4. It is only the main purpose or general meaning of the passage which you have to express. There is no room in a précis for colloquial expressions. All redundancies of expression must be avoided. 5. The précis must be in simple English.	
		(Total Marks 06)
Ans. 6	Answer will vary but besides content following characteristics must be checked.	
	1. The theme of the essay with a definite purpose is present	**3**
	2. The thoughts are in order with a definite conclusion	**3**
	3. Slangs and free and easy construction is not used	**3**
	4. The writing shows personal thoughts and is simple in structure	**3**
		(Total Marks 12)
Ans. 7	1. **Commitment to the program.** At every organizational level, manager's commitment to achieving personal and organizational objectives and to the MBO process is required for an affective program. Managers must meet with those they supervise, first to set objectives and then to review progress toward these objectives. 2. **Top-level goal setting.** Effective MBO programs usually start with the top managers. Because they determine the organization's strategy and set preliminary goals that resemble annual objectives in their content and terms.	

3. **Individual Goals**. In an effective MBO program, each manager and staff member has clearly defined job responsibilities and objectives. The purpose of setting objectives in specific terms at every level is to help employee understand clearly just what they are expected to accomplish and to help each individual plan effectively to achieve his or her targeted goals.

4. **Autonomy in implementation of plans**. Once the objectives have been agreed upon, the individual enjoys wide discretion in choosing the means for achieving them, without being directed by higher ranking manager.

5. **Performance Review**. Managers and employees periodically meet to review progress. During the review, they decide what problems exist and what they can each do to resolve them. If necessary, objectives may be modified for the next review period.

(2.4 marks for each point)

(Total Marks 12)

Ans. 8 (a) **06**

1. Physical noise
2. Technical noise
3. Social noise
4. Psychological noise
5. Distortion
6. Filtering

(1 mark for each point)

Ans. 8 (b) **06**

Negotiation is a back and forth communication process designed to anticipate, contain and resolve disputes so that parties with some shared and some opposing interests can reach mutually acceptable solutions. Negotiation refers to a voluntary, two-way communication in which parties involved control both the process and the outcome.

Negotiation involves five key components:

1. The parties involved
2. The interests involved
3. The relationship between parties
4. Their interactions throughout the negotiation process
5. The results achieved.

(0.75 mark for each point)

(Total Marks 12)

Ans. 9	1) **Define the problem.** The process begins by defining the problem. A problem exists when there is a discrepancy between an existing and a desired state of affairs. 2) **Identify the decision criteria.** Identify the decision criteria that will be important in solving the problem. In this step, the decision maker determines what is relevant in making the decision. 3) **Allocate weights to the criteria.** The criteria identified are rarely equal in importance. So the third step requires the decision maker to weight the identified criteria in order to give them the correct priority in the decision. 4) **Develop the alternatives.** The fourth step requires generating possible alternatives that could succeed in resolving the problem. 5) **Evaluate the alternatives.** All alternatives must be critically analyzed and evaluated. This is done by rating each alternative on each criterion. The strengths and weaknesses of each alternative become evident as they are compared with the criteria and weighted criteria. 6) **Select the best alternative.** The last step is selecting the alternative with the highest total score. **(1.33 marks for each point)**	
		(Total Marks 08)

Business Laws

(Intermediate Level)

Ans. 1(a)	**Historical sources of law** There are instances where rules, subsequently turned into legal principles, where first to be found in an un-authoritative form. They are not allowed by the Law Courts as of right. Some examples are religions, morality and opinions of text writers. These are set of rules framed traditionally in unauthorized way but later adopted and accepted as legal rules or principles by usage rule as common law and equity.	**1.5**
	Legal Sources of law	
	i) Legislation	**0.5**
	ii) Precedent	**0.5**
	iii) Custom	**0.5**
	iv) Agreement	**0.5**
	v) Professional Opinion	**0.5**
Ans. 1(b)	**Process of legislation:**	
	i) A bill may originate either in National Assembly or in Senate.	**01**
	ii) A bill when passed by the house where it was originated is sent to the other house. If the second house passes the bill without an amendment, the same is presented to the president for assent to enact it as a law. If the bill is transmitted to the house and passed with amendment it shall be sent back to the house of origination. If the originating house passes the bill with amendments than it is presented to the President for assent.	**02**
	iii) When a bill is passed by one house but is rejected or not passed by the other house within 90 days or is passed with amendments it is considered in a joint sitting of the National Assembly and Senate. If passed by majority votes by both houses it is presented to president for assent to enact it as a law.	**02**
	iv) The President shall within 30 days: ➢ Give assent to the bill or ➢ Return the same for reconsideration or amendment.	**02**
	v) If both the houses again pass the bill. President shall assent and the bill shall become Act of Parliament.	**01**
		Total Marks 12

Ans. 2(a)	Section 23 mentions follwoing situations when the object and consideration of an agreement is deemed unlawful: i) If it is forbidden by law. ii) If it is of such a nature that, if permitted, it would defeat the provision of any law. iii) If it is fraudulent. iv) If it involves injury to a person or property of another. v) If the court regards it as immoral, or If it is opposed to public policy.	 **01** **01** **01** **01** **01**
Ans. 2(b)	Mr. Adnan's contention is not valid due to the following reasons. • The offer of Mr. Adnan is rejected by Mr. Rehan, as he gave the counter offer. • A counter offer terminates the original offer and is not an acceptance.	**01** **01** **01**
		Total Marks 08
Ans. 3(a)	**<u>Rights of Unpaid Seller</u>** The rights of unpaid seller of goods are as follows: i) Right of lien on the goods for the price, so long as the goods are in possession of seller. ii) Right of stopping the goods while they are in transit after the seller has parted with the possession of them provided the buyer has become insolvent. iii) Right of resale of goods after stopping them in transit and taking them back. iv) Right to sue for price or for damages. **(One mark each for any 3 items)**	**03**
Ans. 3(b)	• Mr. Adeel may sue for refund of price already paid to Mr. Shakir since the time was an essence of contract. • Mr. Adeel may demand damages for non delivery. • The court may award interest at such rate as it thinks fit.	**01** **01** **01**

Ans. 3(c)	A bill of exchange in order to be effective in law must fulfill these conditions: a) It must be in writing, b) Signed by the maker, c) It must contain an order, d) Which must be unconditional, e) It must direct a certain person, f) To pay certain sum of money only, g) To a certain person or his order or to bearer, h) It must be properly stamped.	**0.5** **0.5** **0.5** **0.5** **0.5** **0.5** **0.5** **0.5**
		Total Marks 10
Ans. 4(a)	The Directors of a company having a share capital are elected by the members in a general meeting on the basis of cumulative voting system which shall be as under:- i) Every member has number of votes equal to the product of his shares and the number of directors to be elected. ii) The member may cast all his votes to a single candidate or divide them between more than one candidates as he likes. iii) The candidate who gets the highest number of votes stands elected as director and then the candidate who gets the next highest number of votes stands elected and so on until the required number of directors stand elected. iv) A member can cast the votes both of his own and held through proxies.	**01** **02** **02** **01**
Ans. 4(b)	**Benefits of incorporating a Single Member Company** • A single individual or person may form a company just by subscribing to memorandum of association. • The single member is able to enjoy the privilege of limited liabilities as envisaged under the provisions of the Companies Ordinance. • The benefit of having a status of a company shall also be availed by such a single member. • The SMC shall have all the rights and privileges as well as obligations and liabilities as are applicable to private companies.	**01** **01** **01** **01**

Ans. 4(c)	A public company shall not make any allotment of any share capital offered to the public for subscription unless the following conditions are fulfilled. 1) Minimum subscription has been subscribed. 2) Minimum subscription as determined is exclusive of any amount payable otherwise than in cash. 3) All moneys received from applications for shares has been deposited in a separate bank account in a schedule bank until the certificate to commencement of business has been obtained by the company or the money so received have been returned to the applicant. 4) The amount payable on application on each share has been received in full amount of offered shares. 5) Where the minimum subscription has not been obtained within 40 days after the first issue of prospectus, all moneys received from the applicant are to be returned without surcharge and if any such money is not paid within 50^{th} day, the director shall be liable to pay surcharge at 1½% for default month.	01 01 02 01 02
		Total Marks 17
Ans. 5(a)	A partnership may be dissolved in any one of the following ways: 1) By mutual consent. 2) By notice of dissolution in case of partnership at will. 3) By operation of law. 4) By the happening of certain contingencies. 5) By court. **(0.5 mark each for any 04 items)**	02
Ans. 5(b)	**Test of partnership** In determining whether a partnership exists is to see whether the relation of principal and agent exists between the parties and not merely whether the parties share in the profits or the business is carried on for the benefit of all.	03
Ans. 5(c)	i) A and B are not partners as relationship is of master and servant. ii) A and B are partners as they are conducting the business as an agent and principal. iii) A and B are partners as the relationship of principal and agent exist. iv) A & B are not partners because they are acting as co-owners. v) A & B are partners as they are sharing common profit.	01 01 01 01 01
		Total Marks 10

Ans. 6(a)	No person shall be appointed as a director of a company if he; a) is a minor; b) is of unsound mind; c) has applied to be adjudicated as an insolvent and his application is pending; d) is an undischarged insolvent; e) has been convicted by a court of law for an offence involving moral turpitude; f) has been debarred from holding such office under any provision of the Ordinance; g) has betrayed lack of fiduciary behavior and a declaration to this effect has been made by the Court at any time during the preceding five years. h) Is not a member. i) Has been declared by a court as defaulter in payment of loan to a financial institution. j) Is engaged in the business of brokerage or is a spouse of such person.	 **0.5** **0.5** **01** **0.5** **01** **01** **01** **0.5** **0.5** **0.5**
Ans. 6(b)	**<u>Appointment of Subsequent Chief Executive.</u>** 1) Within fourteen days <u>from the date of election</u> of directors or the office of the Chief Executive <u>falling vacant</u>, as the case may be, the directors of a company shall appoint any person, including an elected <u>director</u>, to be the Chief Executive, but such appointment shall not be for a period exceeding <u>three years from the date of appointment</u>. 2) On the expiry of his term of office a chief executive shall be eligible for reappointment. 3) The Chief Executive shall continue to perform his functions until his successor is appointed unless non-appointment of his successor is due to any fault on his part or his office is expressly terminated.	 **04** **01** **01**
	Total Marks 13	

Taxation

(Intermediate Level)

Ans. 1

Assessment

Means the determination of Taxable Income and the Tax Liability or Tax Refundable to a tax payer. This term also includes provisional assessment, reassessment and amended assessment. **02**

Business

is the activity undertaken with a motive to earn profits. Business includes any; **02**

a) Trade
b) Commerce
c) Manufacture
d) Profession
e) Vocation or
f) Adventure of concern in the nature of trade, comer, manufacture, profession or vocation.

However, it does not include an employment.

Total Marks 04

Ans. 2

	Taxable Salary Income		1,200,000	
Add:	Tax paid by the employer	Note 1	62,500	**(a)**
	Taxable Income including Tax		1,262,500	
	Tax on Tax Amount of Rs. 62,500 @10%		6,250	**(b)**
	Total tax Payable (a+b)		**68,750**	

Note 1

Income upto Rs. 400,000	@0%	Nil
Income upto Rs. 400,001 to 750,000	@5%	17,500
Income upto Rs. 750,001 to 1,400,000	@10%	45,000
	Total	62,500

Total Marks 06

Ans. 3

	Fair Market Value of Shares	70,000
Less:	Cost of Right	(4,000)
	Consideration Paid	(40,000)
	Amount to be included in taxable salary	26,000

Total Marks 05

Ans. 4

Registered Person

"Registered person means a person who is registered or is liable to be registered under this Act: **02**

Provided that a person liable to be registered but not registered shall not be entitled to any benefit available to a registered person under any of the provisions of this Act or the rules made there under.

Tax Fraction

It means the amount worked out according to the following formula: **03**

$$\frac{a}{100 + a}$$

Here "a" is the rate of sales tax as specified in Section 3. Tax Fraction is applied in following cases.

1- Computation of output Tax in case person who is liable to be registered but has not been registered and

2- Determination of output tax in respect of such supplies made by a registered person on which sales tax has not been charged and collected.

Total Marks 05

Ans. 5

Output Tax

Sales to Registered Person		1,360,000
Sales to un-registered Persons - consumers		340,000
Output Tax	**(A)**	1,700,000

Input Tax

Purchase against Tax invoices		850,000
Purchase against import		425,000
Input Tax	**(A)**	1,275,000

Total Marks 06

Ans. 6

Rules relating to collection of Excess Tax

Where any amount of Tax or charge, which was not payable or which is in excess of the Tax or charge actually payable, has been collected and the effect of the tax so collected has been passed on to the customer, the person collecting such tax or charge is required to pay the amount so collected to the Federal Government. The Government may recover such amount as arrears of Tax. In respect of such amount a claim of refund shall not be admissible.

Total Marks 04

Financial Reporting

(Final Level)

Ans. 1.

Statement of Cash Flows
For the year ended June 30, 2014

	Rs. (000)	Rs. (000)
CASH FLOWS FROM OPERATING ACTIVITIES		
Profit before tax (12,060+3,870)		15,930
Adjustments for: -		
Provision for doubtful debts	350	
Interest expense	1,200	
Fair value gain	(7,400)	
Gain on disposal of investments	(250)	
Amortization of intangible assets	560	
Depreciation for the year	4,550	
Loss on disposal	2,300	1,310
Operating profit before working capital changes		17,240
(Increase)/decrease in current assets		
Inventory	(8,115)	
Trade debtors (8,200-11,320)	(3,120)	
Advances, deposits and prepayments	(1,935)	
Increase /(decrease) in current liabilities		
Trade creditors	12,600	
Accrued expenses (6,290-4,860)	(1,430)	(2,000)
		15,240
Taxes paid		(1,230)
Interest paid (120+1200-350)		(970)
Net cash inflows from operating activities		13,040
CASH FLOWS FROM INVESTING ACTIVITIES		
Disposal proceeds of investments	3,450	
Intangible assets acquired	(710)	
Disposal proceeds PPE	1,150	
PPE acquired	(19,050)	
Net cash outflow from investing activities		(15,160)
CASH FLOWS FROM FINANCING ACTIVITIES		
14% term finance certificate (2,000-1,500)	500	
Dividend paid	(7,000)	
Share capital issued	10,000	
Net cash inflow from financing activities		3,500
Increase / (decrease) in cash and cash equivalents		1,380
Opening balance of cash and cash equivalents		1,285
Closing balance of cash and cash equivalents		2,665

W-1 Property, Plant and Equipment

Opening balance	32,500
Depreciation for the year	(4,550)
Acquired through issuing TFC	1,500
Disposal during the year	(3,450)
Acquired during the year	19,050
Closing balance	45,050

W-2 Intangible Assets

Opening balance	5,100
Amortization	(560)
Acquired during the year	710
Closing balance	5,250

W-3 Investment

Opening balance	10,450
Disposal	(3,200)
Fair value gain	7,400
Closing balance	14,650

W-4 Retained Earnings

Opening balance	20,350
Profit after tax	12,060
Dividend paid	(7,000)
Closing retained earnings	25,410

W-5 Tax Expense

Opening balance	7,690
Tax expense	3,870
Taxes paid	(1,230)
Closing balance	10,330

Total Marks 20

Ans. 2.

	2014 Rs. (000)	2013 Rs. (000)
Tax expense-Profit or loss a/c		
Current tax	2,578,050	
Deferred tax	(88,620)	2,489,430
Tax expense-OCI		
Deferred tax		110,500
W-1 Calculation of Current Tax		7,350,000
Profit before tax		
Add: - Accrued expenses-closing	12,000	
Bad debt expense	1,100	
Advance income-closing	4,000	
Gratuity expense	5,000	
Depreciation for the year-accounting	455,000	477,100
Less: - Bad debts written off	600	
Advance income - opening	5,000	
Gratuity paid	2,000	
Accrued expenses-opening	22,000	
Depreciation for the year-tax	215,000	(244,600)
Taxable profit		7,582,500
Current tax @ 34%		2,578,050

W-2 Property, Plant and Equipment-Accounting

Opening balance	1,550,000
Addition for the year	615,000
Depreciation for the year	(455,000)
Revaluation surplus	325,000
Closing balance	2,035,000

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W-3 Property, plant and Equipment-Tax

Opening balance	550,000
Addition	615,000
Depreciation for the year	(215,000)
Closing	950,000

W-4 Calculation of Deferred Tax

Opening	**CV**	**TB**	**TTD**	**DTD**
Property, plant and equipment	1,550,000	550,000	1,000,000	
Accrued expenses	22,000	--	--	22,000
Provision for DD	1,000	--	--	1,000
Advance income	5,000	--	--	5,000
Gratuity payable	15,000	--	--	15,000
			1,000,000	43,000
Deferred Tax Liability				334,950
Property, Plant and Equipment	2,035,000	950,000	1,085,000	-
Accrued expenses	12,000			12,000
Provision for DD	1,500			1,500
Advance income	4,000			4,000
Gratuity payable	18,000			18,000
			1,085,000	35,500
				356,830
Deferred Tax Expense				
Profit or loss account				(88,620)
Revaluation surplus				110,500
				21,880

Total Marks 15

Ans. 3.

a) The revenue should be recognized as soon as the customer accepted the goods as the goods are separated and delivery is delayed on the request of customer.

b) The revenue cannot be recognized until and unless the goods have been inspected and installed as the risk and rewards only transfers when goods are properly installed.

c) This is not sale as the transaction is not at fair value of the goods but a financing arrangement and loan will be recognized at the time of receipt of money and subsequently interest will be accrued over the period of two years. The stock will continue to be recognized by the entity at cost.

d) The revenue will be recognized over the four months on straight line basis as there is no other pattern identified for delivery of services.

Total Marks 10

Ans. 4.

PARENT COMPANY-GROUP
Consolidated Statement of Financial Position
as at June 30, 2014

	Rs. (000)	Rs. (000)
Assets		
Non-current assets		
Property, plant and equipment (15,450+10,250)	25,700	
Goodwill (4,170-500)	3,670	29,370
Current assets (8,520+6,750)		15,270
		44,640
Equity and liabilities		
Equity		
Ordinary share capital	15,000	
Share issue reserve	600	
Consolidated retained earnings **(W-2)**	6,280	21,880
		1,155
		23,035
Non-current liabilities (16,000-3000)		13,000
Current liabilities		8,605
		44,640

W-1 Goodwill

Cost of investment	9,000	
Contingent consideration (30x20)	600	9,600
Fair value of NCI		600
		10,200
Fair Value of net assets		
Share capital	2,000	
Pre-acquisition reserve	4,030	6,030
		4,170

W-2 Consolidated retained earnings

Parent company		4,615
Subsidiary company reserves-post		2,040
		6,655
Impairment loss		(375)
		6,280

W-3 Subsidiary company retained earnings

	Pre	**Post**
Balance	2,530	4,220
Fair value gain	1,500	(1,500)
	4,030	2,720
Group 75%	3,022.50	2,040
NCI 25%	1,007.50	680

W-5 Non-controlling interest (NCI)

Fair value of NCI (50x12)		600
Post acquisition profit share		680
		1,280
Impairment loss		(125)
		1,155

Total Marks 20

Ans. 5.

Partners Capital Account

	X Rs. (000)	Y Rs. (000)	Z Rs. (000)		X Rs. (000)	Y Rs. (000)	Z Rs. (000)
Current a/c	--	--	2,000	B/ f	18,000	12,000	6,000
Realization a/c	4,000	--	--	Realization a/c	--	2,000	--
Share in CSL	30,000	20,000	10,000	Realization a/c	15,550	10,367	5,183
Cash	--	4,367	--	Cash	450	--	817
	34,000	24,367	12,000		34,000	24,367	12,000

Realization Account

	Rs. (000)		Rs. (000)
Property, plant and equipment	25,280	Loan Mr. Y	20,000
Intangible assets	15,620	Trade payable	22,450
Investments	3,450	Taxes payable	2,000
Inventory	18,775	Mr. X	4,000
Trade receivables	12,225	Purchase consideration	60,000
Taxes payable	2,000		
Mr. X (31,100 x 3/6)	15,550		
Mr. Y (31,100 x 2/6)	10,367		
Mr. Z (31,100 x 1/6)	5,183		
	108,450		108,450

Cash Account

	Rs. (000)		Rs. (000)
B / f	3,100	Mr. Y	4,367
Mr. X	450		
Mr. Z	817		
	4,367		4,367

CSL
Statement of Financial Position
as at January 01, 2014

	Rs. (000)	Rs. (000)
Assets		
Non-current assets		
Property, plant and equipment	30,000	
Intangible assets (12,000+1,500)	13,500	
Goodwill	28,950	72,450
Current assets		
Inventory	19,000	
Trade receivables	11,000	30,000
Total assets		**102,450**

Capital and liabilities	
Capital	
8 Million Ordinary share capital of Rs. 10 each	80,000
Current liabilities	
Trade creditors	22,450
Total capital and liabilities	**102,450**

Total Marks 20

Ans. 6.

	Contract A	Contract B
Statement of Financial Position	**Rs. (000)**	**Rs. (000)**
Contract cost to date	6,850	8,050
Profit / (loss) to date	1,527.75	(400)
Contract work in progress	8,377.75	7,650
Progress billings to date	(6,900)	(7,250)
Due from / (due to) customers	1,477.75	400
Progress billings to date	6,900	7,250
Receipts to date	(4,660)	(5,305)
Adjustment against mobilization advance	(1,550)	(1,220)
Retention money	(690)	(725)
Receivable / (payable)	--	--
Statement of Comprehensive Income		
Revenue for the year	7,520	8,910
Cost of sales / expenses for the year	(5,992.25)	(9,202)
Profit / (loss) for the year	1,527.75	(292)
Provision for onerous contract	--	(108)
Net profit / (loss) for the year	1,527.75	(400)

W-1 Estimated Profit / (Loss)

Total revenue	15,500	12,200
Total cost		
Cost to date (6,550+300)/(7,750+300)	6,850	8,050
Future cost (5,200+300) / (4,250+300)	5,500	4,550
	12,350	(12,600)
Expected profit / (loss)	3,150	(400)

W-2 Stage of Completion

Revenue certified	7,520	8,910
Total revenue	15,500	12,200
% of completion	**48.5%**	**73.0%**

Total Marks 15

Management Accounting

(Final Level)

Ans. 1

Products	A	B	C	D
	Rs.	Rs.	Rs.	Rs.
Selling Price per Litter(If further processed)	4	3	2	5
Expected selling Price at end of initial production	2.5	2.8	1.2	3
Incremental Selling Price	**1.5**	**0.2**	**0.8**	**2**

04

Product	A	B	C	D
Out Put (Litters)	22,000 X	20,000 X	10,000 X	18,000 X
Incremental Revenue/Litter	Rs.1.50	Rs.0.20	Rs.0.80	Rs.2
Total Incremental Revenue	**Rs.33,000**	**Rs.4,000**	**Rs.8,000**	**Rs.36,000**

02

Total Incremental Revenue	Rs. 33,000	Rs. 4,000	Rs. 8,000	Rs. 36,000
Direct Cost to be Incurred as a result of further processing(Wages)	(Rs.12,000)	(Rs.8,000)	(Rs.4,000)	(Rs.16,000)
Production O/H	-	-	-	-
Incremental Cost/Benefit of further Processing	**Rs. 21,000**	**(Rs.4,000)**	**Rs.4,000**	**Rs.20,000**

06

The Analysis indicate that the product A, C, D should be further processed and Product B should not be as it incurred Loss of Rs. 4,000. If Product B. sold before further processing, it would generate savings of Rs. 4,000. Production O/H are assumed to be unavoidable. 03

If these are assumed to be avoidable then Product B would generate savings of more than Rs. 4,000.

Total Marks 15

Ans. 2

Scrip Dividend:
The reasons for making a scrip dividend include the following.

i. A scrip dividend is a means of paying a return to shareholders without any cash transfer being made. Effectively, it converts retained profits into issued share capital. It therefore represents a means of transferring profits to the shareholders without actually making a cash dividend payment. Thus the company's liquidity position is preserved.

A scrip dividend is therefore beneficial for companies which wish to use all their internally generated funds for future investment.

ii. A scrip dividend may indicate to the market that the company has identified worthwhile profitable investments for which it requires substantial funds. As a result the share price might rise.

iii. A scrip dividend has the effect of increasing the number of shares in issue and reducing their value. The fact that the shares are of a smaller denomination may make them more marketable.

Share (Stock) Split:
The reasons why a company may wish to make a share split include the following:

i. The major reason for a share split is to enhance the marketability of the company's shares. The same logic applies as with the scrip dividend, except for the latter it was a subsidiary effect to the main purpose.
A share split simply increases the number of shares in issue by a certain factor and therefore the market price falls. The desired effect is for trading in the shares to become more active.

ii. A company which undertakes a share split is often perceived by the market to be planning for substantial earnings growth in the future. Therefore there is frequently an associated price rise.

Total Marks 05

Ans. 3(a) 3.5

Profit Statements for the year ending 30 Sept,2014
Marginal Costing Basis

	Six months ending 31 Mar,2014		Six Months ending 30 Sept,2014	
	Rs.000	Rs.000	Rs.000	Rs.000
Sales(Rs.140/ unit)		980		1,120
Opening Inventory			73.5	
Std. Variable production Cost(Rs.49/Unit)	416.5		343	
Less: Closing Inventory(W1)	(73.5)		(24.5)	
		(343)		(392)
		637		728
Variable selling and so on costs		(196)		(224)
Contribution		441		504
Fixed Costs: Production(W2)	160		160	
Selling and so on	90	(250)	90	(250)
Net Profit		191		254

Profit Statements for the year ending 30 Sept,2014
Absorption Costing Basis

3.5

	Six months ending 31 Mar,2014		Six Months ending 30 Sept,2014	
	Rs.000	Rs.000	Rs.000	Rs.000
Sales		980		1,120
Opening Stock	-		103.5	
Production	586.5		483	
Closing Stock	(103.5)	(483)	(34.5)	(552)
Under/over Absorbed Overhead		10		(20)
Gross Profit		507		548
Fixed Cost	90		90	
Variable Selling Cost	196	(286)	224	(314)
Profit		221		234

Workings

03

W.1

	Six months ending 31-Mar,2014	Six Months ending 30-Sept,2014
	Units	**Units**
Opening Inventory		1500
Production	8500	7000
	8500	8500
Sales	7000	8000
Closing Inventory	1500	500
Marginal Cost Valuation x Rs.49	**Rs.73,500**	**Rs.24,500**
Absorption Cost Valuation x Rs.69	**Rs.103,500**	**Rs.34,500**

W.2

Budgeted Fixed Production O/H = 16000 units x Rs. 20 =Rs.320,000 P.a = Rs.160,000 six monthly 02

W.3

03

	Six months ending 31-Mar,2014	Six Months ending 30-Sept,2014
	Units	**Units**
Normal Output	8000	8000
Budgeted Output	8500	7000
	(500)	1000
	x	x
	Rs.20	Rs.20
(Over)/under Absorbed	(Rs.10,000)	Rs.20,000

Ans. 3 (b)	Difference between absorption costing profit and marginal costing profit is because of the treatment of fixed production cost and difference in stock levels. Under absorption costing fixed production cost is part of product cost while under marginal costing fixed production cost is to be treated as period cost.	05
	Total Marks 20	

Ans. 4

Step 1 — 2.5

		Mash	Sauce	Total
Labour hours per unit	(Hours)	2	1	
Sales demand	(Units)	3000	5000	
Labour hours needed	(Hours)	6000	5000	11000 hrs
Labour hours available				8000 hrs
Shortfall				3000 hrs

Labour is the limit factor on production.

Step2 — 2.5

Identify the contribution earned by each product per unit of scarce resource, that is, per labour hour worked.

	Mash	Sauce
Sales price	14	11
Variable Cost	8	7
Unit contribution	6	4
Labour hours per unit	2 hrs	1 hr
Contribution per labour hour(=per unit of limiting factor)	Rs. 3	Rs. 4

Although Mash has a higher unit contribution than Sauce, two sauces can be made in the time to make one Mash. Because labour is in short supply it is more profitable to make Sauce than Mash.

Step 3 — 05

Determine the budgeted production and sales. Sufficient Sauce will be made to meet the full sales demand and the remaining labour hours available will then be used to make Mash.

(a)

Product manufacture	Demand	Hours required	Hours available	Priority for
Sauce	5,000	5,000	5,000	1st
Mash	3,000	6,000	3,000	2nd
		11,000	8,000	

(b) 05

Product manufacture	Units	Hours Needed	Contribution per unit	Total Rs.
Sauce	5,000	5,000	4	20,000
Mash (bal)	1,500	3,000	6	9,000
		8,000	8,000	29,000
Less fixed costs				20,000
Profit				9,000

Conclusion 05

(a) Unit contribution is not the correct way to decide priorities.

(b) Labour Hours are scarce resource; therefore contribution per labour hour is the correct way to decide priorities.

(c) The Sauce earn Rs. 4 contribution per labour hour, and the Mash earns Rs. 3 contribution per labour hour. Sauce therefore make more profitable use of the scarce resource, and should be manufactured first.

Total Marks 20

Ans. 5

	2014	2013	2012	2011
Ordinary shares	5.5	5.5	5.5	5.5
Reserves	13.7	10.4	7.6	5.1
Total Equity	19.2	15.9	13.1	10.6
Bonds	20	20	20	20
Capital Employed	39.2	35.9	33.1	30.6
PBIT	9.8	8.5	7.5	6.8
ROCE	25%	24%	23%	22%
Earnings	5.5	4.7	4.1	3.6
ROE	29%	30%	31%	34%

Comments

Return on Capital Employed:
It is increasing each year from 2011 to 2014 and in year 2014 equal to the industry average. It shows that company is able to generate good return for its capital providers.

Return on Share Holder's Fund:
Although ROE is declining each year but still it is above than industry average. Earnings are increasing each year so decline is because of increasing reserves.

3 marks for ratio and 2 for comment in each ratio

Total Marks 10

Ans. 06

a. NPV

	T0	T1	T2	T3	
Sales (60,000 × Rs.40)		2,400	2,400	2,400	02
Variable costs (60,000 × Rs.25)		(1,500)	(1,500)	(1,500)	02
Fixed costs **(W1)**		(355)	(355)	(355)	04
Rent	(80)	(80)	(80)		01
Net operating cash flows	(80)	465	465	545	
Initial cost	(1,200)				
Residual value				600	
Net Cash Flows	**(1,280)**	**465**	**465**	**1,145**	02
D.F @ 10%	**1**	**0.909**	**0.826**	**0.751**	01
Disc Cash Flows	**(1,280)**	**423**	**384**	**860**	

NPV = Rs.387 01

Hence the NPV of the Project is Positive so the project should be accepted on the Basis of NPV 02

Workings:

W-1 Relevant Fixed Cost

	Rs.000
Amount charged to project	715
Bank interest (not relevant – covered by discount rate)	(86)
Head office overheads (not incremental)	(74)
Depreciation (non-cash - Rs1.2m - Rs.0.6m ÷ 3)	(200)
Relevant fixed costs	355

b. Pay Back Period

03

Yr.	Cash Flows	Disc. Factor	Disc. Cash Flows	Cum. Disc. Cash Flows
0	(1280)	1	(1280)	(1280)
1	465	0.909	423	(857)
2	465	0.826	384	(473)
3	1145	0.751	860	387

Discounted Pay Back period will be 2 yr. and 6 months. As it is more than targeted payback period of company so it should also be accepted on the basis of pay back as well. 02

Total Marks 20

Ans. 7(a)	The cash operating cycle is the period of time which elapses between the point at which cash begins to be expended on the production of a product and the collection of cash from a customer. The cash operating cycle in a manufacturing business equals the average time that raw materials remain in inventory less the average period of credit taken from suppliers plus the average time taken to produce the goods plus average the time taken by customers to pay for the goods.	**02**
(b)	There is a relationship between the cash operating cycle and the level of investment in working capital. If the turnover periods for inventories and accounts receivable lengthen, or the payment period to accounts payable shortens, then the operating cycle will lengthen and the investment in working capital will increase. The length of the cash operating cycle depends on the working capital policy which will determine the level of investment in working capital.	**02**
(c)	**Inventory days** $= \frac{Inventory}{Cost\ Of\ Sales} \times 365$ $=$ **4,500 / 16,400 × 365 = 100 days**	**1.5**
	Trade receivables days $= \frac{Trade\ Receivables}{Sales} \times 365$ $=$ **3,500 / 21,300 × 365 = 60 days**	**1.5**
	Trade payables days $= \frac{Trade\ Payables}{Cost\ Of\ Sales} \times 365$ $=$ **4,500 / 16,400 × 365 = 67 days**	**1.5**
	Cash Operating Cycle = Inventory days + Trade Receivable Days – Trade Payable Days =100 + 60 – 67 = **93 days**	**1.5**
		Total Marks 10

Auditing

(Final Level)

Ans. 1. (a)	Adjusting events subsequent to the balance sheet date are those that provide evidence of conditions that existed at the end of the reporting period. These could pertain finalization or identification of further / final information about events or circumstances that were ongoing during the reporting year or existed at the reporting date. An example of an adjusting event would be the culmination of a legal case in the court wherein that case was in process during the year but a final outcome was unknown at the reporting date. Another example would the announcement of bankruptcy by a debtor who was facing a difficult financial position as at the entity's reporting date and at that time it was imminent that the amount receivable by the entity would likely not be received." Non-adjusting events subsequent to the balance sheet date are those that are indicative of conditions that arose after the reporting period. These could be material by amount or in their nature but the related events or circumstances did not exist at the reporting date. Examples of non-adjusting events subsequent to the balance sheet date could include a flood or fire in the entity's premises or godowns resulting in loss of stock or fixed assets. The major difference apart from the description stated above arises in terms of the accounting treatment of adjusting and non-adjusting events. Adjusting events are required to be accounted in the period to which they relate i.e. the financial statements need to be 'adjusted' to include the effect of such events. However, since non-adjusting events are no indicative or events or circumstances at the balance sheet date, these are not required to be adjusted but rather only disclosed in the financial statements for the knowledge of users of the financial statements. **2 marks each for an adequate description of adjusting and non-adjusting event along with example and up to 2 marks for an appropriate distinction by reference to accounting treatment**	**06**
Ans. 1. (b)	The auditor's responsibilities in relation to events subsequent to the balance sheet date are stipulated in ISA 560. These include the following: • Obtain evidence that all events up to date of auditor's report that require adjustment or disclosure, have been identified. • Take into account the auditor's risk assessment in determining the nature and extent of audit procedures, which shall include the following: **(a)** Obtaining an understanding of any procedures management has established to ensure that subsequent events are identified. **(b)** Inquiring of management and, where appropriate, those charged with governance as to whether any subsequent events have occurred which might affect the financial statements. **(c)** Reading minutes, if any, of the meetings, of the entity's owners, management and those charged with governance, that have been held after the date of the financial statements and inquiring about matters discussed at any such meetings for which minutes are not yet available. **(d)** Reading the entity's latest subsequent interim financial statements, if any. • If event is after auditor's report but before issuance of FIS, and is material, auditor should consider whether F/S need amendment and discuss with management.	**07**

- If auditor's report not issued and management disagrees on amendment to FIS, express qualified or adverse opinion.
- Obtain written representations.

Total Marks 13

Ans. 2.

Rights / Powers

- The right of access at all times to the books and accounts and vouchers of the Company.
- The right to require from the officers of the company such information and explanations as he thinks are necessary for the performance of his duty.
- Right of access to such copies and documents from the books and papers of a branch outside Pakistan as have been transmitted to the principal office in Pakistan.
- The right to receive notices of general meetings of the company and speak on the matters which concern him as auditor.
- The right to be sent by the company a copy of a notice of intention to propose his removal or replacement and the right to make written representations.
- Right to speak at general meetings.
- Right to require laying of accounts.

Responsibilities

- To report to the members whether in their opinion the financial statements give a true and fair view of the financial position and finance performance of the company.
- To conduct their audit in a professional and ethical manner and to comply with all applicable professional and ethical standards.

To report:

- Whether they have received all information and explanations which to the best of their knowledge and belief were necessary for the purposes of the audit.
- Whether in their opinion proper books of account have been kept by the company.
- Whether the balance sheet and profit and loss account have been drawn up in conformity with the Ordinance and are in agreement with the books of account.
- Whether the expenditure incurred was for the purpose of the company's business.
- Whether the business conducted, investments made and expenditure were in accordance with the objects of the company.
- Whether in their opinion Zakat (if applicable) was deducted at source by the company and deposited in the Central Zakat Fund.

1 mark for each right / power and responsibility if adequately described; vague responses to only be given ½ mark.

Total Marks 10

Ans. 3	**Inherent risk factors** Complexity and extent of regulation is much less for charities; usually commercial organizations are subject to corporate laws and oversight by SECP as well as tax compliance monitored by entities such as the FBR. In case of charities no such regulation and oversight exists. A significant amount of revenue of charities arises from donations and cash receipts. This raises overall inherent risk as compared to commercial entities which use banking channels. Lack of predictable income and precisely identifiable relationships between income and expenditure, conversely, commercial entities usually have a proper budget-making process. Importance of restricted funds and donations-in-kind raise the risk over completeness and valuation of income. At times a single charitable organization runs several different projects, this raises the risk of funds not being utilized for the purpose they were provided for initially. **Control risk factors** Due to significant focus being. targeted towards charity work, administrative and specifically finance functions are not given as much importance, leading to reduced oversight and monitoring and higher risk of controls being overridden or there being no controls at all. Since the focus is not to earn a profit, high qualified finance staff cannot be hired at the relatively lower salary range offered by charity organizations. This leads to an overall weak control structure as regards finance and accounts. Similar to the reason of focus towards charitable work as described above, the board of governors or trustees is not likely to devote substantial time to internal control. Frequency and regularity of trustee meetings along with attendance at such meetings is likely to be low. Lack of segregation of duties is likely to be a feature in charity organizations; this could result in more-than-required authority being passed on to one or a few individuals, potentially raising the risk of override of controls and consequently fraud. The expenditures of charities are likely to be services provided or gifts / food items /rehabilitation work done, for which substantial/concrete evidence is unlikely to be available. **Up to 1.5 mark for an adequately explained feature of-charities and link to the audit. Marks to be limited where vague / unclear descriptions are provided.**	
	Total Marks 15	
Ans. 4	**Reasonable Assurance** A high, but not absolute level of assurance that certain information is free of material misstatement. Such an assurance is usually provided in engagements to audit financial statements.	

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	Limited Assurance The level of assurance obtained where engagement risk is reduced to a level that is acceptable in the circumstances of the engagement, but where that risk is greater than for a reasonable assurance engagement, as the basis for expressing a conclusion. The combination of the nature, timing and extent of evidence gathering procedures is at least sufficient for the practitioner to obtain a meaningful level of assurance. To be meaningful, the level of assurance obtained by the practitioner is likely to enhance the intended users' confidence about the financial statements. Reasonable assurance engagements are usually audit engagements (whether their scope pertains to financial statements or other financial information) and therefore the nature, timing and extent of procedures in such engagement include various procedures dependent upon the auditor's judgment. The procedures in an audit engagement would include inspection of records, inspection of assets, inquiries, analytical review, re-performance, recalculation and observation. However, since a limited assurance engagement results in the expression of negative form of assurance, the procedures are limited usually to inquiries and analytical reviews. A reasonable assurance engagement would result in the auditor expressing an opinion on whether the financial statements give a true and fair view and is therefore a positive form of assurance. However, since the procedures in a limited assurance engagement are only inquiry and analytics as explained above, the expression of assurance takes the 'negative form' in that the practitioner states whether anything has come to his attention that causes him to believe that the financial statements do not give a true and fair view. **2 marks each for the definitions of reasonable and limited (negative) assurance. Upto one mark for each point provided adequately explained.**	
	Total Marks 10	
Ans. 5. (a)	A "forecast" means prospective financial information prepared on the basis of assumptions as to future events which management expects to take place and the actions management expects to take as of the date the information is prepared (best-estimate assumptions). A "projection" means prospective financial information prepared on the basis of: **(a)** Hypothetical assumptions about future events and management actions which are not necessarily expected to take place, such as when some entities are in a start-up phase or are considering a major change in the nature of operations; **or** **(b)** A mixture of best-estimate and hypothetical assumptions. **2 marks for a proper description; mark to be limited to one each in case vague description is provided not sufficient to draw a distinction between the two terms**	**02** **02**
Ans. 5. (b)	• Obtain sufficient appropriate evidence as to whether: (a) Management's: best-estimate assumptions on which the prospective financial information is based are not unreasonable and, in the case of hypothetical assumptions, such assumptions are consistent with the purpose of the information; (b) The prospective financial information is properly prepared on the basis of the assumptions;	**10**

(c) The prospective financial information is properly presented and a "material assumptions are adequately disclosed, including a clear indication as to whether they are best-estimate assumptions or hypothetical assumptions; and
(d) The prospective financial information is prepared on a consistent basis with historical financial statements, using appropriate accounting principles.

- Considerations apply when accepting engagement and in using knowledge of the business when evaluating whether significant assumptions have been identified.
- Consider the extent to which reliance on the entity's historical financial information is justified.
- Consider the period of time covered by the prospective financial information.
- When determining the nature, timing and extent of examination procedures, the auditor's considerations should include:
  (a) The likelihood of material misstatement;
  (b) The knowledge obtained during any previous engagements;
  (c) Management's competence regarding the preparation of prospective financial information;
  (d) The extent to which the prospective financial information is affected by the management's judgment; and
  (e) The adequacy and reliability of the underlying data.
- The auditor should obtain written representations from management regarding the intended use of the prospective financial information, the completeness of significant management assumptions and management's acceptance of its responsibility for the prospective financial information.
- Special reporting considerations apply.

One mark for each valid point from ISAE 3400

Total Marks 14

Ans. 6

Gross profit has gone down from 35% to 21.5%, implying that the Company may be facing rising cost of inputs the effect of which it is unable to pass on to the consumers.

There has been a 65% increase in profits but that has not resulted in increase in overall profitability for Alfa Foods as the net profit has experienced a decrease of around 12%.

Discussion with management would enable more information to be made available as regards the business model/strategy of the company.

Linked to the profitability issue above is also the fact that the company is holding a huge amount of inventory on hand. The increase in inventory balances is manifold and does not bode well for a business already running low on profitability.

It is apparent that the company is facing a cash crunch as the much better positive cash position of June 2013 is expected to be changed into a net borrowing position with limited cash available and significant amount of overdraft.

There are possible signs of overtrading since there has been an increase in sales along with a 4 times increase in long term borrowing as well. Financing of short term operational and liquidity needs by utilizing long term financing options is not just a dangerous commercial strategy to have, it is also likely to have serious financial statements implications since the company's fixed assets are secured against the loan to the extent of Rs. 7.5 million. Alfa's inability to generate sufficient cash to payoff the loan may result in the secured assets being taken over by the bank leading to significant issues for the long term operation of the company.

The company being engaged in the food business is likely to experience the issue of food items being expired or of unusable condition. In such a business, since reputational damage arising from selling expired food stuff cannot be absorbed as a risk, it would be important from an audit point of view to ensure that any obsolete, slow-moving or expired inventory is identified and adjusted in the financial statements.

There is a likely chance of misstatement in this area since it is subjective to some extent. However," inventory appears to be material to the financial statements being much greater than 5%of the estimated profit for the year. The company's property, plant and equipment has experienced a decrease and it is apparent that such assets are not generating increasing profitability, It would therefore be important as an audit risk to identify whether any indicators for the impairment of property, plant and equipment exist. If such indicators are found, we may have to discuss with management whether an impairment test has been performed and if impairment needs to be recognized in the financial statements.

The short term bank overdraft facility and long term loan from a commercial bank is likely to carry certain financial conditions and covenants with them. Breach of the covenants could not just put the secured assets at risk, they may also result in the reclassification of the long term loan as a current liability. This would further deteriorate the financial outlook of Alfa Foods. Trade creditors have increased by over 35% which could demonstrate the impact of rising cost of sales and may also (if probed further) highlight Alfa's inability to pay debts on due dates. It would have to confirmed through inquiries of management whether there are any issues with supplier management or if any disputes have come to light. There is also a possibility of the trade creditors applying a late payment surcharge or penalty in case Alfa does not pay its dues on time.

Accrued expenses have more than doubled to reach Rs. 1.57 million. This would also have to be inquired from the client. The rapid increase in sales and cost of sales may be a possible cause of the same, but it would have to be ascertained through inquiry and analysis of further information available from management.

The bankruptcy of a major debtor owing Rs. 10 million raises serious concern about the recoverability of trade receivable balances. Despite management's claims of a good working relationship, it would have to be assessed that after the announcement of bankruptcy does the debtor have enough financial resources to pay the amount of Rs. 10 million to Alfa Foods. In case that is not possible, Alfa would be suggested to adjust its financial statements by recording a provision for doubtful debts for the amount not expected to be recovered.

Overall, an analysis of the financial position and performance of Alfa Foods also raises the risk about the long term survival of the company vis-a-vis going concern. However, further analysis needs to carried out along with discussions with management to know their point of view on the matter. It is possible that the recovery of doubtful receivables, non-adjustment for any expired stock and non-disclosure or reclassification for breach of financial covenants may be so significant that they might impact the opinion expressed in our audit report. It would therefore be important to assess the above risks prior to commencing the substantive testing stage of the audit.

Up to three (3) marks to be awarded for each valid risk if the risk has been properly identified supported by appropriate working as applicable and financial statement and/or audit implications have been explained.

Total Marks 15

<table>
<tr>
<td>Ans. 7. (a)</td>
<td>
An audit committee is a sub-committee of the board of directors, usually containing a number of non-executive directors. An audit committee can help a company maintain objectivity with regard to financial reporting and the audit of financial statements.
Audit committees play an important role in improving the internal control environment of an entity. They exercise the oversight function vis-a-vis monitoring the various components of internal control.

An audit committee can:

Improve the quality of financial reporting by reviewing the financial statements on behalf of the Board.
Create a climate of discipline and control which will reduce the opportunity for fraud.
Enable the non-executive directors to contribute an independent judgment and play a positive role.
Help the finance director by providing a forum in which he can raise issues of concern and which he can use to get things done which might otherwise be difficult.
Strengthen the position of the external auditor by providing a channel of communication and forum for issues of concern.
Provide a framework within which the external auditor can assert his independence in the event of a dispute with management.
Strengthen the position of the internal audit function by providing a greater degree of independence from management.
Increase public confidence in the credibility and objectivity of Financial Statements

Up to 3 marks for introduction and description of an audit committee and one mark for each way of improving the control environment.
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<tr>
<td>Ans. 7. (b)</td>
<td>

The executive directors may not understand the purpose of an audit committee and may perceive that it detracts from their authority.
There may be difficulty selecting sufficient non-executive directors with the necessary competence in auditing matters for the committee to be really effective.
The establishment of such a formalized reporting procedure may dissuade the auditors from raising matters of judgment and limit them to reporting only on matters of fact.
Costs may be increase

One mark for each point
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<td></td>
<td colspan="2" align="right">Total Marks 12</td>
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<tr>
<td>Ans. 8. (a)</td>
<td>
Emphasis of Matter paragraph - A paragraph included in the auditor's report that refers to a matter appropriately presented or disclosed in the financial statements that, in the auditor's judgment, is of such importance that it is fundamental to users' understanding of the Financial Statements.
If the auditor considers it necessary to draw users' attention to a matter presented or disclosed in the financial statements that, in the auditor's judgment, is of such importance that it is fundamental to users' understanding of the financial statements, the auditor shall
</td>
<td>08</td>
</tr>
</table>

	include an Emphasis of Matter paragraph in the auditor's report provided the auditor has obtained sufficient appropriate audit evidence that the matter is not materially misstated in the financial statements. If the auditor considers it necessary to communicate a matter other than those that are presented or disclosed in the financial statements that, in the auditor's judgment, is relevant to users' understanding of the audit, the auditor's responsibilities or the auditor's report and this is not prohibited by law or regulation, the auditor shall do so in a paragraph in the auditor's report, with the heading "Other Matter," or other appropriate heading.	
Ans. 8. (b)	Examples of circumstances where the auditor may consider it necessary to include an Emphasis of Matter paragraph are: • An uncertainty relating to the future outcome of exceptional litigation or regulatory action. • Early application (where permitted) of a new accounting standard (for example, a new International Financial Reporting Standard) that has a pervasive effect on the financial statements in advance of its effective date. • A major catastrophe that has had, or continues to have, a significant effect on the entity's financial position. • Inability or significant doubts over an entity's ability to continue as a going concern when adequate disclosure has been given in the Financial Statements **One mark for each example if properly explained.**	**03**
	Total Marks 11	