Pakistan Institute
of Public Finance Accountants

Model Solutions

Budgeting, Accounting and Financial Reporting (Application)

WAPDA

Winter Exam-2024

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Solutions – Budgeting, Accounting and Financial Reporting (Application)

Q.1. WAPDA develops the Hydel power projects on Build, Own and Operate (BOO) basis, therefore, multiple options are explored for financing the project during construction. The options are as follows:

i. Sale proceeds of bonds issued under the authority of the Government.
ii. Loans obtained by the Authority with the special or general sanction of the Government.
iii. Direct loans negotiated by the Authority from local and foreign financial institutions.
iv. Foreign aid and loans obtained from the International Bank of Reconstruction and Development, ADB, KFW etc. with the sanction of and on such terms and conditions as may be approved by the Government.
v. Income from sale of electricity.
vi. Any other sums received by the Authority.

For borrowing money under the WAPDA Act, the Authority shall be deemed to be local Authority under the Local Authorities Loans Act, 1914. The Authority is permitted to borrow money for the making and execution of any scheme in furtherance of the objective as defined in the WAPDA Act. The liability of the Government to the Creditors of Authority shall be limited to the extent of grants made by the Government and the loans raised by the Authority with the sanction of the Government.

Project Financing advantages and disadvantages:
Definition: Project Finance is the funding of long-term infrastructure, industrial projects, and public services using a non-recourse or limited-recourse financial structure. The debt and equity used to finance the project are paid back from the cash flow generated by the project.

Advantages:
1.The main benefit of project finance is that it can improve the capacity to raise large amounts of long- term equity and debt finance from both domestic and international sources. This is achieved because:

i) If risks are appropriately allocated, sponsors may be willing to undertake projects with more risk than they would independently.
ii) Financing arrangements can be closely tailored to suit the specific project.
iii) Multiple investors of different size can contribute to projects they could not independently support.
iv) High leverage can make it easier to achieve required equity rates of return.
v) Investors can hold the debt "off-balance sheet" – increasing their capacity to borrow.
vi) Takes advantage of the relative ease of raising debt compared to equity

2.The increased level of finance that project finance allows can also results in benefits of:

i. Greater competition through expanded capacity of more investors to support projects.
ii. Improved due diligence through detailed investor scrutiny of projected cashflows.
iii. Transparency.

Disadvantages of project finance:
While many projects benefit from project finance techniques, this is not always the case. Project finance can often be complex. Therefore:

- it can have significant lead times as compared to other sources of finance; and
- it can be costly to establish

New structures and arrangements may not be well understood by partners. This highly leveraged model can be susceptible to failure. Contracts may require intrusive supervision from investors and constrain management actions.

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Q.2. a An asset is impaired when its carrying amount exceeds its recoverable amount.

Causes of Impairment:
These impairment indicators are used to determine if there is an 'indication of impairment'. There are usually two groups of indicators which may be external or internal.

External indicators/causes are:

i. A significant decline in an asset's market value as a result of the passage of time or normal use.

ii. Significant changes with an adverse effect in the technological, market, economic or legal environment of the relevant asset.

iii. An increase in market interest rates or other market rates of return on investments that are likely to increase the discount rate included in the cash flow calculation when determining value in use.

Internal indicators/cause are:

i. Evidence of obsolescence or physical damage to an asset.
ii. Significant changes regarding the way an asset is used or is expected to be used.
iii. Evidence from internal reporting indicates that the economic performance of an asset is, or will be, worse than expected.

From above it can be concluded that specific situations in which an asset might become impaired and unrecoverable include when a significant change occurs to an asset's intended use when there is a decrease in consumer demand for the asset, damage to the asset, or adverse changes to legal factors that affect the asset and obsolescence etc.

Q.2. b **Accounting of asset impairment:**
An impairment loss for an individual asset shall be recorded when the recoverable amount is less than the carrying amount. The amount of the impairment loss is the difference between the recoverable amount and the carrying amount. While making entries, impairment loss will be debited whereas accumulated impairment loss will be credited.

Q.3. a For determining depreciation rate for some new asset, following factors will be considered:

- Expected useful life of the equipment.
- Expected physical wear and tear.
- Obsolescence factors.
- Usage limits legally, etc.

Q.3. b To calculate depreciation of the official vehicle for its first year, we need to know the useful life, and the residual value. For official vehicles the prescribed useful life is five years (which means the depreciation rate is 20%) and residual value is 05%.

Cost	= 5,000,000	
Residual value	= 5,000,000 x 5%	=250,000
Formula	= cost-residual value/useful life	
	= 5,000,000-250,000/5	
	= 4,750,000/5	
	= 950,000	

Hence, depreciation for the first year will be Rs. 950,000.

Q.4. Letter of Credit:

A letter of credit is a document sent from a bank or financial institution that guarantees that a seller will receive a buyer's payment on time and for the full amount.

Parties to a Letter of Credit:

- Applicant (importer) requests the bank to issue the LC.
- Issuing bank (importer's bank which issues the LC [also known as the Opening banker of LC]).
- Beneficiary (exporter).

Letter of credit and bank guarantee differences:

- A bank guarantee is a promise from a lending institution that ensures the bank will step up if a debtor can't cover a debt.
- Letters of credit are also financial promises on behalf of one party in a transaction and are especially significant in international trade.
- Bank guarantees are often used in real estate contracts and infrastructure projects, while letters of credit are primarily used in global transactions.
- In BG, the bank only pays if the buyer doesn't, so its responsibility comes after the buyer's. whereas in LC the bank pays the seller first and is mainly responsible for payment.
- In BG the seller and customer bear more risk whereas in LC the bank assumes greater risk.

Procedure for opening LC is given in A&FR Manual section-16.4, the examinees are expected to write down this part of the question accordingly in their own words.

Q.5. **Bookkeeping** refers to daily operations of an accounting system and is concerned with only recording and classifying routine transactions. It is a skill that an individual may acquire in a very short time. Bookkeeping can be performed more efficiently by computers.

Accounting is the art of measuring, interpreting and communicating the results of economic activities. Basic objective of accounting is to provide decision makers with information useful in making economic decisions. A professional accountant has a much broader range of knowledge as compared to a bookkeeper. Accountants must be able to exercise professional judgment. Accounting is not a skill it is a profession.

Financial Management is concerned with acquisition, financing and management of assets with some goal in mind. Financial management has three main functional areas: investment, financing and asset management decisions.

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