

# THE PUBLIC ACCOUNTANTS EXAMINATIONS BOARD

*A Committee of the Council of ICPAU*

## ATC(U) EXAMINATIONS

### LEVEL THREE

#### INTRODUCTION TO FINANCIAL REPORTING – PAPER 12

**TUESDAY, 12 DECEMBER 2006**

#### **INSTRUCTIONS TO CANDIDATES:**

1. Time allowed: **3 hours**
2. Attempt **all** the questions in Section **A**, any **two** questions in Section **B** and any **two** questions in Section **C**.
3. Section **A** has **one** compulsory question carrying 20 marks.
4. Section **B** has **three** questions and only **two** are to be attempted. Each question carries 20 marks.
5. Section **C** has **three** questions and only **two** are to be attempted. Each question carries 20 marks.
6. Please read further instructions on the answer booklet.

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## SECTION A: FINANCIAL REPORTING

### Question 1

- (a) The financial statements portray the financial effects of transactions and other events by grouping them into broad classes according to their economic characteristics. These broad classes are termed the elements of financial statements.

(i) List **three** elements directly related to the measurement of financial position in the balance sheet.

**(3 marks)**

(ii) List **two** elements directly related to the measurement of financial performance in the income statement.

**(2 marks)**

- (b) Recognition is the process of incorporating in the balance sheet or income statement an item that meets the definition of an element and satisfies the criteria for recognition.

Give the recognition criteria of an item that meets the definition of an element.

**(5 marks)**

- (c) Measurement is the process of determining the monetary amounts at which the elements of the financial statements are to be recognised and carried in the balance sheet and income statement. This involves the selection of the particular measurement basis.

Identify and briefly describe **four** bases of measurement.

**(10 marks)**

**(Total 20 marks)**

**SECTION B: FINANCIAL REPORTING****Question 2**

The following is available for ABC, a limited company:

**Balance Sheet as at 30 November**

	<b>2006</b>		<b>2005</b>	
	<b>Shs '000</b>	<b>Shs '000</b>	<b>Shs '000</b>	<b>Shs '000</b>
Non-current assets				
Cost or valuation		99,000		72,000
Accumulated depreciation		<u>(50,400)</u>		<u>(43,200)</u>
Net book value		48,600		28,800
Current Assets:				
Inventories	30,600		34,200	
Receivables	34,200		26,100	
Cash at bank	<u>3,600</u>		<u>900</u>	
	<u>68,400</u>		<u>61,200</u>	
Current liabilities:				
Trade payables	33,300		28,800	
Income tax	<u>6,300</u>		<u>5,400</u>	
	<u>39,600</u>		<u>34,200</u>	
Net current assets		<u>28,800</u>		<u>27,000</u>
Total assets less current liabilities		<u>77,400</u>		<u>55,800</u>
Equity and non-current liabilities:				
Capital and Reserves				
Ordinary share capital	9,000		9,000	
Revaluation reserve	13,500		9,000	
Retained earnings	<u>27,900</u>		<u>19,800</u>	
		50,400		37,800
Non-current liabilities				
10% loan notes		<u>27,000</u>		<u>18,000</u>
Total Equity and non-current Liabilities		<u>77,400</u>		<u>55,800</u>

Summarised Statement of Income for the year ended 30 November 2006:

	<b>Shs '000'</b>
Profit from operations	23,850
Finance cost (loan note interest)	<u>(2,700)</u>
	21,150
Income tax expense	<u>6,300</u>
Net profit for the period	<u>14,850</u>

**Notes:**

1. The revaluation surplus arose from the revaluation of a land that was not being depreciated.
2. Dividends paid during the year amounted to Shs 6,750,000.
3. The 2005 income tax liability was settled at the amount provided for during the year ended 30 November 2006.
4. Additional loan notes were issued on 1 December 2005. Interest was paid on 31 May 2006 and 30 November 2006.
5. During the year, non-current assets which had cost Shs 7,200,000 with a net book value of Shs 3,150,000 were sold for Shs 4,500,000.

**Required:**

Prepare the company's cash flow statement for the year ended 30 November 2006, using the indirect method, adopting the format in IAS 7: Cash Flow Statements.

**(20 marks)**

**Question 3**

- (a) Identify any **five** items that are presented on the face of the statement of changes in equity.

**(10 marks)**

- (b) The following have been extracted from the records of Bigwood, a public limited company for the year ended 30 September 2006.

- (i) The profit for the year ended 30 September 2006 was Shs 50 million but had amounted to Shs 23.5 million in the preceding year.
- (ii) The loss on revaluation of property amounted to Shs 30 million for the year ended 30 September 2006 but the company had recognised a revaluation gain on property of Shs 65 million during the year ended 30 September 2005.

- (iii) During the 30 September 2006, the available-for-sale investments recorded gains of Shs 4 million. No gain or lost was recognised in the preceding period.
- (iv) An exchange loss of Shs 6 million arose on translating foreign operations during the year. The company had recognised an exchange gain of Shs 8 million in the year ended 30 September 2005.

**Required:**

A statement of recognised income and expense for Bigwood Public Limited company for the year ended 30 September 2006 including comparatives.

**(10 marks)****(Total 20 marks)****Question 4**

- (a) The urban authorities maintain their books of account on accruals basis whereas the districts and lower local governments apply cash basis of accounting.

Describe the following terms from the stand point of revenues and expenses:

- (i) Cash basis of accounting. **(2 marks)**
- (ii) Accrual basis of accounting. **(2 marks)**

- (b) revenues due to a local government, as shown in the revenue estimates, must be recorded in revenue registers by the revenue collectors, or the revenue controller in the finance department, as the case may be. Each revenue register must show; all revenue due, revenue received, amount paid out/banked and arrears brought forward and carried forward.

**Required:**

Using a general purpose revenue register format, enter the following information in a revenue register of a lower local government:

- (i) Arrears brought forward:

	<b>Shs '000</b>	<b>Code</b>	<b>Date</b>
Market dues	4,000	31	1/7/05
Trading licences	3,700	66	1/7/05
Development tax	1,000	63	1/7/05
Taxi park fees	5,000	32	1/7/05

(ii)

<b>Annual estimates of revenue</b>	<b>Shs '000</b>	<b>Tender awarded to</b>
Market dues	12,000	Honeypot Enterprises
Trading licence	6,000	Mr. Jamada Mohamed
Development tax	18,000	Mrs. Kasozi Winnie
Taxi park fees	48,000	UDOTA

(iii) Revenues received during the year for which receipts were verified:

	<b>Shs '000</b>
Market dues	16,000
Trading licenses	7,000
Development tax	16,500
Taxi park fees	50,000

All receipts were banked intact to the collection account code 4402.

Use the first or last day in the year ended 30/6/2006 as may be applicable.  
The annual estimates of revenue do not include the arrears brought forward.

**(20 marks)**

### **SECTION C: AUDITING**

#### **Question 5**

- (a) The International Federation of Accountants' code of ethics for professional accountants recognises that the objectives of the accountancy profession are to work to the highest standards of professionalism, to attain the highest levels of performance and generally, to meet the public interest requirement set out. These objectives require four basic needs to be met:

**Required:**

Identify and briefly explain the **four** basic needs.

**(10 marks)**

- (b) Identify and briefly explain matters that are covered by the fundamental principles of the code of ethics for professional accountants.

**(10 marks)****(Total 20 marks)**

### Question 6

- (a) The auditor should obtain written representations from management on matters material to the financial statements when other sufficient appropriate audit evidence cannot reasonably be expected to exist.
- (i) State two areas where management are required to provide written representations for.  
(4 marks)
- (ii) State the basic elements of a management representation letter.  
(10 marks)
- (iii) What action is taken if management refuses to provide representations?  
(6 marks)
- (Total 20 marks)**

### Question 7

Audit sampling is a technically difficult area to understand in terms of its detailed application. However, emphasis ought to be put on the general principles of why samples are taken in the first place, and what conditions are necessary for sampling.

- (a) Define audit sampling.  
(2 marks)
- (b) When is sampling considered inevitable for audit?  
(2 marks)
- (c) Identify **five** cases where statistical sampling is not appropriate.  
(10 marks)
- (d) Identify any **three** conditions that need to be present if statistical sampling is to be used.  
(6 marks)
- (Total 20 marks)**