K. J. SOMAIYA INSTITUTE OF MANAGEMENT STUDIES AND RESEARCH

Program: PGDM, 1st Trimester (Batch 2016-2018) Subject: Financial Accounting (End Term Examination)

Maximum Marks: 60 Duration: 3 hours

Date: 19th September, 2016.

Notes:

- 1. All questions carry equal marks
- 2. Answer all questions
- 3. Make suitable assumptions if required and state them
- 4. It is an <u>OPEN BOOK</u> examination and students are allowed to use <u>ONLY OWN</u> books, notebooks and calculators.

Question 1

The following is a news item excerpt on the change in Indian accounting standards to a new accounting standard called Ind-AS.

Maruti Suzuki, Tata Steel, BPCL, UltraTech and Coal India may report 3-12% increase in earnings after to the implementation of new Indian Accounting Standard (Ind-AS). On the other hand, earnings of ITC, Bharti Infratel, Lupin, and Arvind may fall by 4-10%. The transition will have a considerable impact on the computation of revenue, operating profit, net profit, and networth of the listed companies. Sectors including metals, telecoms, oil & gas, and real estate are likely to be impacted most. According to analyst estimates, the new norms will increase revenues by 4-5%, while overall EBITDA may drop by 2-3%.

As we can see that the new accounting standards will change the income statement and balance sheet. Since the accounting information presented changes as the standards change, should accounting information be used to take decisions? Please comment.

Question 2

Below is an extract from the balance sheet of a company. All figures in Rs. crores Assets

Cash 2
Accounts Receivable 10
Fixed Assets 60

Share Capital 10 Retained Earnings 50

The CEO had called the controller and said that there seems to be some problem in

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the balance sheet. The company is proposing to invest Rs. 20 crores in the new plant and while the retained earnings are Rs. 50 crores, the cash balance is only Rs 2 crores. The CEO says that has per her understanding, retained earnings represented the net income which has been retained by the company and so the cash balance should atleast be equal to Rs. 50 crores. She asks the controller to check with the bank to get the correct cash balance and also to correct the balance sheet so that it gives a "true and fair" picture.

How should the controller respond to this request?

Question 3

Explain using a numerical example **EITHER**

(i) how the use of LIFO when FIFO should be used

OR

(ii) how the use of FIFO when LIFO should be used results in incorrect gross margin.

Specifically also explain what is a "correct" gross margin. (choose only (i) or (ii)).

Question 4

Traces Corporation maintains its records on a cash basis. At the end of each year the company's accountant obtains the necessary information to prepare accrual basis financial statements. The following cash flows occurred during the year ended December 31, 2013:

Cash receipts:

From customers Rs	. 725,000
Interest on note	5,400
Loan from a local bar	nk 75,000

Total cash receipts Rs. 805,400

Cash disbursements:

Purchase of merchandise Rs.	400,000
Annual insurance payment	7,200
Payment of salaries	220,000
Dividends paid to shareholders	11,000
Annual rent payment	29,000

Total cash disbursements Rs. 667,200

Selected balance sheet information:

	31/12/2012	31	/12/2013
Cash	30,000		168,200
Accounts receivable	67,000		102,000
Inventory	90,000		67,000
Prepaid insurance	3,500	?	

12,000	?	
4,050	?	
60,000		60,000
150,000		150,000
-45,000		-60,000
115,000		132,000
21,000		26,000
0		75,000
0	?	
	4,050 60,000 150,000 -45,000 115,000 21,000	4,050 ? 60,000 150,000 -45,000 115,000 21,000 0

Additional information:

- 1. On March 31, 2012, Traces lent a customer Rs.60,000. Interest at 9% is payable annually on each March 31. Principal is due in 2016.
- 2. The annual insurance payment is made in advance on April 30. The policy period begins on May 1.
- 3. On October 31, 2013, Traces borrowed Rs.75,000 from a local bank. Principal and interest at 6% are due on October 31, 2014.
- 4. Annual rent on the company's facilities is paid in advance on June 30. The rental period begins on July 1.

Prepare an accrual basis income statement for 2013 (ignore income taxes).

Question 5

Arina Music Company was started by Arina early in 2013. Initial capital was acquired by issuing shares of common stock to various investors and by obtaining a bank loan. The company operates a retail store that sells records, tapes, and compact discs. Arina asks for your help in preparing the balance sheet and presents you with the following information for the year ending December 31, 2013:

a. Cash receipts consisted of the following:

From customers Rs.360,000
From issue of common stock 100,000
From bank loan 100,000

b. Cash disbursements were as follows:

Purchase of inventory
Rent
15,000
Salaries
30,000
Utilities
5,000
Insurance
3,000

Purchase of equipment and furniture 40,000

- c. The bank loan was made on March 31, 2013. A note was signed requiring payment of interest and principal on March 31, 2014. The interest rate is 12%.
- d. The equipment and furniture were purchased on January 3, 2013, and have an estimated useful life of 10 years with no anticipated salvage value. Depreciation per year is Rs.4,000.

- e. Inventories on hand at the end of the year cost Rs.100,000.
- f. Amounts owed at December 31, 2013, were as follows:

To suppliers of inventory Rs.20,000

To the utility company 1,000

- g. Rent on the store building is Rs.1,000 per month. On December 1, 2013, four months' rent was paid in advance.
- h. Net income for the year was Rs.76,000. Ignore income taxes
- i. One hundred thousand shares of Rs. 10 par value common stock are authorized, of which 10,000 shares were issued and are outstanding. Required:

Prepare a balance sheet at December 31, 2013.

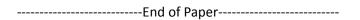
Question 6

Pfizzel Inc. reported the following information in its property, plant, and equipment note to the 1999 financial statements (Rupees in millions):

	1999	1998	1997
Land	85.2	81.8	71.7
Buildings	1,218.6	1,093.8	953.9
Machinery and equipment	2,108.4	1,897.8	1,706.9
Furniture, fixtures, and other	940.2	812.8	698.3
Construction in progress	640.5	414.5	385.6
Total PPE	4,992.9	4,300.7	3,816.4
Less accumulated depreciation	1,919.7	1,668.2	1,511.3
Book value PPE	3,073.2	2,632.5	2,305.1

Required

- a. During which year(s) did Pfizzel acquire substantial fixed assets? How can you tell?
- b. During which year(s) did Pfizzel sell some fixed assets? How can you tell? evidence supports your conclusion?
- c. Calculate the percentage of PPE depreciated for each year. Discuss the meaning and implications of your results.



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