THE INSTITUTE OF COST AND MANAGEMENT ACCOUNTANTS OF BANGLADESH
CMA DECEMBER, 2017 EXAMINATION
PROFESSIONAL LEVEL-II
SUBJECT: 201. ADVANCED FINANCIAL ACCOUNTING-I.

Solution

Solution to the Q. No. 1

(i)

Temporary Difference	Future Taxable (Deductible) Amounts	Tax Rate	Deferred Tax (Asset)	Deferred Tax Liability
Depreciation	Tk.120,000,000*	40%	Tk.48,000,000	

Non-current liabilities
Deferred tax liability.. Tk.48,000,000

(ii)

		Dr.	Cr.
Income Tax Expense	Dr.	178,000,000	
Deferred Tax Liability	Dr.		48,000,000
Income Taxes Payable	Cr.		130,000,000

Tk.130,000,000 taxes due for 2014 ÷ 40% 2014 tax rate = Tk.325,000,000 taxable income for 2014.

Taxable income for 2014..	Tk.325,000,000
Tax rate	X 40%
Income taxes payable for 2014 (also given data)	Tk.130,000,000

Deferred tax liability at the end of 2014...	Tk. 48,000,000
Deferred tax liability at the beginning of 2014	0
Deferred tax expense for 2014 (increase in deferred tax liability)	48,000,000
Current tax expense for 2014 (Income taxes payable)	130,000,000
Income tax expense for 2014..	Tk.178,000,000

(iii)

Income before income taxes.....................................		Tk.445,000,000[a]
Income tax expense		
Current..	Tk.130,000,000	
Deferred...	48,000,000	178,000,000
Net income..		Tk.267,000,000

[a]Pretax financial income..	Tk. X*
Less: Excess depreciation per books [from (a) above]................................	120,000,000[b]
Taxable income [from (b) above]..	Tk.325,000,000

Solving for X; X – Tk.120,000,000 = Tk.325,000,000; X = Tk.445,000,000 pretax financial income.

	Book Depreciation	Tax Depreciation	bDifference
2014	Tk.120,000,000	Tk.240,000,000*	Tk.(120,000,000)
2015	120,000,000	144,000,000	(24,000,000)
2016	120,000,000	86,400,000	33,600,000
2017	120,000,000	64,800,000	55,200,000
2018	120,000,000	64,800,000	55,200,000
Totals	Tk.600,000,000	Tk.600,000,000	Tk. 0

*(Tk.600,000,000 – 0) X (1 ÷ 5) X 2
**(Tk.600,000,000 – Tk.240,000,000 – Tk.144,000,000 – Tk.86,400,000) ÷ 2 yrs.

(iv)

Temporary Difference	Future Taxable (Deductible) Amounts	Tax Rate	Deferred Tax (Asset)	Deferred Tax Liability
Depreciation	Tk.144,000,000	40%		Tk.57,600,000
Unearned rent	(75,000,000)	40%	Tk. (30,000,000)	
Unearned rent	(75,000,000)	40%	(30,000,000)	
Totals	Tk. (6,000,000)		Tk. (60,000,000)	Tk.57,600,000

Temporary Difference	Resulting Deferred Tax (Asset)	Resulting Deferred Tax Liability
Depreciation		Tk.57,600,000
Unearned rent	Tk.(30,000,000)	
Unearned rent	(30,000,000)	
Totals	Tk.(60,000,000)	Tk.57,600,000

Other assets (non-current)
Deferred tax asset Tk.2,400,000

(v)

		Dr.	Cr.
Income Tax Expense	Dr.	53,600,000	
Deferred Tax Asset	Dr.	60,000,000	
Income Taxes Payable	Cr.		104,000,000
Deferred Tax Liability	Cr.		9,600,000

Tk.104,000,000 taxes due for 2015 ÷ 40% 2015
tax rate = Tk.260,000,000 taxable income for 2015.

Taxable income for 2015	Tk.260,000,000
Tax rate for 2015	40%
Income taxes payable for 2015 (also given data)	Tk.104,000,000

Deferred tax asset at the end of 2015	Tk. 60,000,000
Deferred tax asset at the beginning of 2015	0
Deferred tax benefit for 2015 (increase in deferred tax asset)	Tk. (60,000,000)

Deferred tax expense for 2015 (Tk.24,000,000 X .40)		Tk. 9,600,000
Deferred tax benefit for 2015		(60,000,000)
Current tax expense for 2015 (Income taxes payable)		104,000,000
Income tax expense for 2015..		Tk. 53,600,000

(vi)	Income before income taxes..		Tk.134,000,000[c]
	Income tax expense		
	Current..	Tk.104,000,000	
	Deferred...	(50,400,000)	53,600,000
	Net income...		Tk. 80,400,000

[c]Pretax financial income...	Tk.	Y
Excess rent collected over rent recognized		150,000,000
Excess depreciation (from schedule above)		(24,000,000)
Taxable income [from (e) above]...		Tk.260,000,000

Solving for Y:

Y + Tk.150,000,000 – Tk.24,000,000 = Tk.260,000,000

Y = Tk.260,000,000 – Tk.150,000,000 + Tk.24,000,000

Y = Tk.134,000,000

Solution to the Question No. 2(a)

The financial accounting term unguaranteed residual value refers to the worth of a lease property at the end of the agreement's term that is not the responsibility of the lessee.

Solution to the Question No. 2(b)

Lessees have available two lease accounting methods: (a) the operating method and (b) the capital-lease method. Under the operating method, the leased asset remains the property of the lessor with the payment of a lease rental recognized as rental expense.

Solution to the Question No. 2(c)

Note:

This lease is a capital lease to the lessee because the lease term (6 years) exceeds 75% of the remaining economic life of the asset (7 years). Also, the present value of the minimum lease payments exceeds 90% of the fair value of the asset.

Tk 91,637.36	Annual rental payment
X 4.88965	PV of an annuity due of 1 for n = 6, i = 9%
Tk 448,074.52	PV of minimum lease payments

(i)

CHELLS, INC. (Lessee)
Lease Amortization Schedule

Date	Annual Lease Payment	Interest (9%) on Liability	Reduction of Lease Liability	Lease Liability
1/1/14				Tk 448,074.52
1/1/14	Tk 91,637.36		Tk 91,637.36	356,437.16
1/1/15	91,637.36	Tk 32,079.34	59,558.02	296.879.14

1/1/16	91,637.36	26,719.12	64,918.24	231,960.90
1/1/17	91,637.36	20,876.48	70,760.88	161,200.21
1/1/18	91,637.36	14,508.00	77,129.36	84,070.85
1/1/19	91,637.36	7,566.51 *	84,070.85 *	0
	Tk 549,824.16	Tk 101,749.64	Tk 448,074.52	

* Rounded.

(ii)

Date	Account		Dr.	Cr.
1/1/14	Leased Equipment Under Capital Leases	Dr.	448,074.52	
	Lease Liability	Cr.		448,074.52
1/1/14	Lease Liability	Dr.	91,637.36	
	Cash	Cr.		91,637.36
	During 2014			
	Insurance Expense	Dr.	2,000.00	
	Cash	Cr.		2,000.00
	Property Tax Expense	Dr.	850.00	
	Cash	Cr.		850.00
12/31/14	Interest Expense	Dr.	32,079.34	
	Interest Payable	Cr.		32,079.34
	Depreciation Expense	Dr.	74,679.09	
	Accumulated Depreciation— Capital Leases	Cr.		74,679.09
	(Tk 448,074.52 ÷ 6 = Tk 74,679.09)			
1/1/15	Interest Payable	Dr.	32,079.34	
	Interest Expense	Cr.		32,079.34
	Interest Expense	Dr.	32,079.34	
	Lease Liability	Dr.	59,558.02	
	Cash	Cr.		91,637.36
	During 2015			
	Insurance Expense	Dr.	2,000.00	
	Cash	Cr,		2,000.00
	Property Tax Expense	Dr.	850.00	
	Cash	Cr.		850.00
12/31/1	Interest Expense	Dr.	26,719.12	
	Interest Payable	Cr		26,719.12
	Depreciation Expense	Dr.	74,679.09	
	Accumulated Depreciation— Capital Leases	Cr.		74,679.09

Note:

1. The lessor sets the annual rental payment as follows:

Fair market value of leased asset to lessor	Tk 460,000.00
Less: Present value of unguaranteed residual value Tk 20,000 X 0.59627 (present value of 1 at 9% for 6 periods)	11,925.40
Amount to be recovered through lease payments	Tk 448,074.60
Five periodic lease payments Tk 448,074.60 ÷ 4.88965*	Tk 91,637.36

*Present value of annuity due of 1 for 6 periods at 9%.

2. The unguaranteed residual value is not subtracted when depreciating the leased

Solution to the Question No. 3(a)

The main points of difference between trading and non-trading concerns may be summarized as follows:

Objective:
Trading Concerns: The main objective of these concerns is to earn profit.
Non-trading Concerns: The main objective of these concerns is to provide goods and services that fulfill a social need.

Source Of Income:
Trading Concerns: The main sources of income are revenue received from the sale of merchandise or from the services rendered to others.
Non-trading Concerns: The main sources of income of these concerns are entrance fees, subscriptions, donations, Govt. and municipals grants etc.

Distribution Of Net Income:
Trading Concerns: The net income or profit earned during a trading period is distributed among the partners or shareholders.
Non-trading Concerns: The excess of income over expenditure is not distributed but is used to fulfill the needs of the concerns.

Organization Form:
Trading Concerns: Trading concerns may be in the form of sole proprietorship, partnership, joint stock company or public enterprises.
Non-trading Concerns: Non-Trading concerns may be in the form of club, society, association and trust.

Ownership:
Trading Concerns: The ownership lies in the hands of the persons who contributed capital for trading concerns. In sole proprietorship, proprietor is the owner, in partnership the partners and in Joint-stock company, the shareholders are the owners of the business.
Non-trading Concerns: In non-trading concerns, the ownership does not lie in the hands of anyone. No one can claim the ownership of these concerns, All the persons carrying on the society or club or trust are its members.

Management:
Trading Concerns: The sole proprietorship is managed by the proprietor, the partnership by the partners or their representatives and joint stock company by the board of directors.
Non-trading Concerns: The control and management of non-trading concerns rest in the hands of trustees, governing body and committee of management.

Accounts:
Trading Concerns: The accounts of these concerns are maintained according to the double entry system. Trial balance drafted to know the arithmetic accuracy of books of accounts and income and expense summary is prepared to ascertain the net income or loss of the business.
Non-trading Concerns: The accounts of non-trading concerns are also maintained according to the double entry system of accounting. These institutions do not maintain a full set of books but only a cashbook is maintained. Receipts and payments account is prepared instead of trial balance and Income and expenditure account is prepared to present to the members showing how much income has exceeded expenditure or vice versa.

Solution to the Question No. 3(b)

Step 1: Determination of Outcome of the Contract
As the outcome of the contract is reliably measurable therefore, the contract revenue & cost will be recognized on the basis of stage of completion
Step 2: Calculation of Stage of Completion (Using Work Certified Method)

Contract	1	2
	Tk'000	Tk'000
Total Contract Revenue	11,000	2,400
Work Certified at 31 Dec 2013	6,600	1,680
Percentage of Completion *100	(6,600 /11,000)*100 = 60%	(1,680 / 2,400)*100 = 70%

Step 3: Estimated Total Profit/Loss on the Contract

	Tk'000	Tk'000
Total Contract Revenue	11,000	2,400
Total Contract Cost	(8,000)	(2,500)
Estimated Total Profit	3,000	(100)

Step 4: Profit to date

	Tk'000	Tk'000
Revenue to date (11,000*60) / (2,400*70%)	6,600	1,680
Cost to date (Balancing Fig)	(4,800)	(1,750)
Profit to date (3000*60%) / (100*70%)	1,800	(70)
- Profit already recognize in previous year	-	-
Profit/ (Loss) for the year	1,800	(70)

Step 5: Statement of Profit or Loss

	Tk'000	Tk'000
Revenue	6,600	1,680
Cost	(4,800)	(1,750)
Profit/ (Loss)	1,800	(70)
- Rectification Cost of Error by Contractor	-	-
- Provision for Onerous Cont. (100-30) Remaining loss	-	(30)
Profit/ (Loss) for the year	1,800	(100)

Step 6: Statement of Financial Position

	Tk'000	Tk'000
Cost to date	7,800	1,440
Profit / (loss) to date	1,800	(100)
- Progress Billings	(6,000)	(1,760)
Due from / (to)	3,600	(420)

Solution to the Question No. 3(c)

Step 1: Determination of Outcome of the Contract
As the outcome of the contract is not reliably measurable therefore, the contract revenue will be recognized only upto the extent of costs incurred on the contract to date, to the extent it is recoverable.

Step 2: Statement of Profit or Loss

	Tk'000
Revenue to date (up to extent, which is recoverable)	2,000
Cost to date	(2,400)
Loss to date	(400)

Step 3: Statement of Financial Position

Cost to date	2,400
-Loss to date	(400)
- Progress Billings	(1,800)
Due from	200

Solution to the Question No. 4(b)
Winding up a company is the process whereby is life is ended and its property administered for the benefit of its creditors and members.

Different method of winding up:

1. Compulsory winding up i.e. by court
2. Voluntary winding up
3. Voluntary winding up subject to the supervision of the court

Solution to the Question No. 4(c)

STATEMENT OF AFFAIRS
AS AT……………

ASSETS	BOOK VALUE	ESTIMATED TO PRODUCE	LIABILITIES	TAKA	EXPECTED TO RANK
Patents	70,000	45,000	Creditors Fully Secured	85,000	
Stock in Trade	80,000	60,000	Less: Fair Value of Free Hold Land 1,65,000 (-) Receiver's Fee (1,65,000 * 4%) (6,600)	(1,58,400)	
Fixture and Fittings	12,000	8,000			
Plant and Machinery	1,20,000	90,000			
Bill of Exchange	35,000	35,000			
Cash in Hand	2,000	2,000			
Calls in Arrear	4,000	2,000			
Debtors:					
Good	60,000	60,000	Surplus After Meeting Secured Creditors	73,400	
Doubtful	15,000	5,000	Less: Amount Paid to Partly Secured Creditors	(90,000)	
Bad	15,000	0			
	4,13,000	3,07,000	**Amount to be shown as Unsecured Creditors**	**16,600**	
Less: Receiver's fee (3,07,000 * 10%)		(30,700)	Debentures	2,00,000	0
Debentures Deducted as			Less: Deducted As per Contra	(2,00,000)	

per Contra					
			Preferential Creditors:		
		2,76,300	Income Tax Due	65,000	0
Preferential Creditors			25,000		
Deducted as per Contra		(2,00,000)	Salary		20,000
			40,000	(65,000)	
Amount Available for Bank Overdraft and Unsecured Creditors		76,300			
		(65,000)	Less: Deducted As per Contra		
Deficiency Account					
			Bank Overdraft	2,70,000	3,17,600
			Unsecured Creditors:	6,000	
		11,300	Trade Creditors	10,000	
			Unclaimed Dividends	15,000	
			Bills Payable		
		3,26,300	Bills Discounted	16,600	
			Amount Unsecured From Secured Creditors		
		3,37,600			3,37,600

DEFICIENCY ACCOUNT

Particulars	Taka	Particulars	Taka
Ordinary Share Capital	2,00,000	Calls in Arrear	2,000
6% Preference Share Capital	3,00,000	Bad Debt	25,000
		Bills Discounted	15,000
Deficiency Account (Balancing Figure)	**3,26,300**	Freehold Land	45,000
		Plant & Machinery	30,000
		Fixtures & Fittings	4,000
		Stock in Trade	20,000
		Patents	25,000
		Receiver's Fee (30,700 + 6,600)	37,300
		Business Loss	6,23,000
	8,26,300		8,26,300

Workings:

As the Available amount to pay the Bank Overdraft and 50% of Unsecured Creditors is not Enough, we have to perform the 100:50 test to make the distribution Schedule.

Bank Overdraft : 50% of Unsecured Creditors
= 20,000 : 1,58,800
= 1,78,800

So, Payment from the Available 11,300 will be distributed as follows:

Bank Overdraft = (11,300 * 20,000) / 1,78,800

= 1264

Unsecured Creditors = (11,300 * 1,58,800) / 1,78,800

= 10,036

NOTES:

1. Here Receiver's fee on Cash in Hand has been considered to be included.
2. The maximum amount of salary can be 2000 tk for each employee and rest of the amount will be shown as unsecured creditors.
3. Receivers fee:

1st 10,00,000 – 10% ; 10,00,001- 2 core – 5% ; Above 2 core – 1%
For Selling any mortgage Assets – 4 % of the sale proceeds.

Solution to the Question No. 5(a)

Surrender value is the sum of money an insurance company will pay to the policy holder or annuity holder in policy in the event of his policy being voluntarily terminated before its maturity or the insured event occurring.

How is Surrender value accounted for?

Payment of Periodic insurance premium

Dr. Insurance Expenses ***
Dr. Cash Surrender Value ***
Cr. Cash ***

Upon receipt of Death benefit at death

Dr. Cash ***
Cr. Cash Surrender Value ***
Cr. Insurance expenses *** (unexpired)
Cr. Gain of Life Insurance ***

Solution to the Question No. 5(b)

Sonar Bangla Insurance co. Ltd.
Fire revenue account for the year ended 31st December, 2014

	Amount(Tk.)		Amount(Tk.)
Claims under policies, less		Balance of Account at the	
reinsurance:		beginning of the year :	
Paid during the year 2062500		Reserve for unexpired	
Total estimated liability in		Risk 15,00,000	
respect of outstanding claims		Additional Reserve ------	15,00,000
at the end of the year, whether		Premium less re-insurance	37,50,000
due or intimated 375000		Interest, Dividend and Rent	
24,37,500		less Income-tax thereon	1,12,500
less: outstanding at the end of		Commission on reinsurance	
the previous year 562500	18,75,000	ceded	1,50,000
Commission on:			
Direct business 225000			
Reinsurance accepted 75000	3,00,000		
Expenses of management	6,48,750[1]		
Bad debts	11,250		
Foreign taxes	7,500		
Depreciation	30,000		
Audit fees	15,000		
Profit transferred to Profit and			
Loss A/C (balancing figure)	7,50,000		
Balance of account at the end			
of the Year as shown in the			
Balance Sheet:			
Reserve for Unexpired Risks @			
50% of premium			
income 18,75,000			

Additional Reserve -----------	18,75,000		
	55,12,500		55,12,500

Sonar Bangla Insurance Company Limited
Profit & Loss Account
For the year ended 31st December, 2014

	Amount		Amount
Investment reserve	75,000[2]	Profit from the Fire Revenue	7,50,000
Provision for Income-tax	2,92,500	A/C	
Balance for the year carried to			
Appropriation A/c	3,82,500		
	7,50,000		7,50,000

Sonar Bangla Insurance Company Limited
Profit and Loss Appropriation Account
For the year ended 31st December, 2014

	Amount		Amount
Balance at the end of the year		Balance b/f	1,50,000
as shown in the balance sheet	5,32,500	Balance of the year brought	
		forward from Profit & Loss A/c	3,82,500
	5,32,500		5,32,500

Balance sheet of Sonar Bangla Insurance Co. ltd
As at 31st December, 2014

Liabilities	Amount(Tk.)	**Assets**	Amount(Tk.)
Share capital:		**Investments:**	
Authorized	-------	Deposits with BB 15,00,000	
Issued, Subscribed and paid		Govt. Securities 18,75,000	
up :		Shares of Companies 7,50,000	41,25,000
37500 shares of $100 each,			
Fully paid	37,50,000	Agents' Balance	-
Reserve and contingency		Outstanding Premium	-
Accounts :		Amount due from other person	
General Reserve 7,50,000		Carrying on insurance business	30,00,000
Investment reserve 5,25,000		Sundry Debtors	3,75,000
Profit and loss		Cash at Bank	9,10,500
appropriation A/c 5,32,500	18,07,500	Cash in hand	19,500
		Motor Car, furniture etc. (net)	4,20,000
Balance of Funds and			
Accounts :			
Fire Insurance Fund	18,75,000		
Estimated liability in respect			
of outstanding claims,			
whether due or intimated	3,75,000		
Amount due to other persons			
carrying on insurance			
business	6,00,000		
Sundry creditors	1,50,00		
Provision for Taxation	2,92,500		
	88,50,000		88,50,000

Working notes:

[1]Expense of Management-

Establishment Charges	3,75,000
Rent, Rates and Taxes	90,000
Postages and telegram	11,250
Printing and Stationary	18,750
Policy stamps	3,750
Directors Fees	15,000
Managing Directors Remuneration	1,35,000
	6,48,750

[2]**Additional Investment Reserve Required**

Book value of investment (18,75,000+7, 50,000)	26,25,000
Market Value	21,00,000
Reserve required	5,25,000
Les: Existing Reserve	4,50,000
	75,000