



**THE INSTITUTE OF CHARTERED ACCOUNTANTS  
OF NIGERIA**

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# **PATHFINDER**

**MAY 2014 PROFESSIONAL EXAMINATION I**

**Question Papers**

**Suggested Solutions**

**Plus**

**Examiners' Reports**

# **PATHFINDER**

## **FOREWORD**

This issue of the **PATHFINDER** is published principally, in response to a growing demand for an aid to:

- (i) Candidates preparing to write future examinations of the Institute of Chartered Accountants of Nigeria (ICAN);
- (ii) Unsuccessful candidates in the identification of those areas in which they lost marks and need to improve their knowledge and presentation;
- (iii) Lecturers and students interested in acquisition of knowledge in the relevant subjects contained herein; and
- (iv) The profession; in improving pre-examinations and screening processes, and thus the professional performance of candidates.

The answers provided in this publication do not exhaust all possible alternative approaches to solving these questions. Efforts had been made to use the methods, which will save much of the scarce examination time. Also, in order to facilitate teaching, questions may be edited so that some principles or their application may be more clearly demonstrated.

It is hoped that the suggested answers will prove to be of tremendous assistance to students and those who assist them in their preparations for the Institute's Examinations.

### **NOTES**

Although these suggested solutions have been published under the Institute's name, they do not represent the views of the Council of the Institute. The suggested solutions are entirely the responsibility of their authors and the Institute will not enter into any correspondence on them.

# **PATHFINDER**

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# **PATHFINDER**

**THE INSTITUTE OF CHARTERED ACCOUNTANTS OF NIGERIA**

**PROFESSIONAL EXAMINATION I – MAY 2014**

**INFORMATION TECHNOLOGY**

**Time Allowed: 3 hours**

**SECTION A: PART I      MULTIPLE-CHOICE QUESTIONS      (20 Marks)**

**ATTEMPT ALL QUESTIONS IN THIS SECTION**

**Write ONLY the alphabet (A, B, C, D or E) that corresponds to the correct option in each of the following questions/statements:**

1. Computers with high programmable speed that perform mathematical calculations, compare values and store results using discrete signals are known as
  - A. Analog Computers
  - B. Digital Computers
  - C. Peripheral
  - D. Hybrid Computers
  - E. Hardware
  
2. Which of these is **NOT** an example of a magnetic storage?
  - A. Disk cartridge
  - B. Floppy disk
  - C. Hard disk
  - D. Magnetic tape
  - E. USB flash drive
  
3. Which of the following is **NOT** an output device?
  - A. Liquid Crystal Display (LCD)
  - B. EPSON Dot Matrix Printer
  - C. Inkjet Printer
  - D. Bar Code Reader
  - E. Visual Display Unit (VDU)

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4. A Metropolitan Area Network (MAN) is
  - A. Limited to a geographical area such as a building
  - B. A large computer network usually spanning a campus
  - C. Usually built of leased lines
  - D. A large network which is linked to the internet
  - E. A Wide Area Network (WAN)
5. Digital Certificate does **NOT** contain
  - A. Owner's public key
  - B. Owner's name
  - C. Digital signature
  - D. Expiration date of the public key
  - E. Digital signature of the owner
6. Computer crime does **NOT** include
  - A. Wiretapping
  - B. Data diddling
  - C. Privacy
  - D. Impersonation
  - E. Data leakage
7. Activities in Computer Forensic investigation does **NOT** include
  - A. Media analysis
  - B. Data communication analysis
  - C. Network misuse
  - D. Data interception
  - E. Hardware acquisition
8. In the generation of phones, GPRS is an acronym for
  - A. General Packet Radio Signals
  - B. General Packet Radio Services
  - C. General Parcel Radio Signals
  - D. General Packet Radio Server
  - E. General Packet Rader Service

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9. Production Support Systems team may comprise **ONE** of the following:
- A. System Engineer
  - B. Production Engineer
  - C. Administrative Manager
  - D. Administrative Officer
  - E. Production Manager
10. A good system documentation does **NOT** include **ONE** of the following summarised points.
- A. Facilitates revision on modification of systems
  - B. Assists in the training of system operation staff
  - C. Assists the auditor in the computer audit process
  - D. Assists the developer in modifying the system designed
  - E. Makes modification difficult for the developer
11. The following are some of the major reasons for implementing a distributed system **EXCEPT**
- A. Allows resources sharing
  - B. Processing tasks are performed at dispersed locations
  - C. Allows concurrent processes
  - D. Connects users and resources in a transparent, open and scalable way
  - E. It does not allow additional hardware to be connected on the network
12. Special policies and procedures must be incorporated into the design, implementation and continual usage of information system to minimise the following **EXCEPT**
- A. Error
  - B. Disaster
  - C. Computer crime
  - D. Data backup
  - E. Breach of security

## PATHFINDER

13. A computer software that connects other software components or applications, allowing them to communicate with each other and to exchange data is known as
- A. Middleware
  - B. System software
  - C. Application software
  - D. Operating system
  - E. Business software
14. A mechanism for interacting with a computer operating system or software by typing commands to perform specific tasks is known as
- A. Graphical User Interface (GUI)
  - B. Menu driven interface
  - C. Online driven interface
  - D. Command driven interface
  - E. Offline driven interface
15. Which of the following is **NOT** a part of firewall techniques?
- A. Packet filter
  - B. Application gateway
  - C. Packet gateway
  - D. Circuit-level gateway
  - E. Proxy server
16. Standard Accounting Software has the following features and functionalities.
- I. New company setup
  - II. Setting up accounting structure
  - III. General ledger
  - IV. Payroll
  - V. Inventory
- A. IV and V
  - B. III, IV and V
  - C. I, II, III, IV, and V
  - D. I, II and III
  - E. I and II

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17. Analysis of IT Risk Assessment can be carried out using
- A. Experimental and qualitative approaches
  - B. Empirical and quantitative approaches
  - C. Qualitative and quantitative approaches
  - D. Qualitative approach only
  - E. Quantitative approach only
18. IT Governance structure of relationship does **NOT** include **ONE** of the following
- A. IT Value Delivery
  - B. Strategic alignment
  - C. Performance measurement
  - D. IT Risk Management
  - E. IT Corporate Management
19. IT Assets **CANNOT** be safeguarded through **ONE** of the following strategies
- A. Prevention/detection of fraud
  - B. IT warehouse
  - C. Copyright issues
  - D. Confidentiality
  - E. Privacy
20. The control that protects IT facilities from forced physical entry is known as
- A. Automated control
  - B. Mechanical control
  - C. Electronic control
  - D. Manual control
  - E. System control



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SECTION A: PART II

SHORT-ANSWER QUESTIONS

(20 Marks)

ATTEMPT ALL QUESTIONS IN THIS SECTION

Write the answer that best completes each of the following questions/statements:

1. The part of the computer system that carries out the instructions of a computer program by performing the basic arithmetical, logical and input/output operations of the system is known as .....
2. What is the name of the point used to connect external devices to the computer system unit?
3. Examples of optical storage devices are compact disk (CD) and .....
4. What is the name of the wireless technology standard for exchanging data over a short distance?
5. The act of sharing tasks, and devices such as data storage, complex calculations etc., over multiple computers in Cloud Computing is known as ..... computing.
6. In Computer Forensic investigation, in order to permit multiple Forensic Computer specialists to work on the data or parts of the data at the same time, the evidence has to be .....
7. A computer related crime where a person gains access to and tampers with the system resources is known as .....
8. A particular concern relating to the protection of personal information and knowing who you are doing business with on the internet as well as their business practices is referred to as .....
9. A backup that is performed while the database is running is referred to as .....
10. The acronym HTTP in computer communication means .....
11. Master file update is the process of ..... the contents of a master file with new transaction entries

## PATHFINDER

12. The use of two or more Central Processing Units (CPUs) within a single computer system is referred to as .....
13. A data structure that represents each process in a system is .....
14. A software tool designed to help organisations assess weaknesses in their current IT security environment, reveal a prioritised list of issues and provide specific guidance to minimise those risks is .....
15. The processes a company uses to track and organise its contacts with its current and prospective customers is known as .....
16. Rules to ensure that relationships between coupled database tables remain consistent is known as .....
17. In IT General Control, the acronym COSO stands for .....
18. What is the access control that protects IT systems and data by verifying and validating authorised users?
19. Information processing control that reconciles the input control totals with the totals of items that have updated the file is the .....
20. The user department and individuals that make use of IT facilities in an organisation are known as .....

### SECTION B: ATTEMPT QUESTION 1 AND ANY OTHER THREE QUESTIONS

(60 Marks)

#### QUESTION 1

##### CASE STUDY

##### CHANGING GLOBAL TRANSACTION PATTERN

At a Supply Chain Management Stakeholders' workshop organised by Niger Consulting, the problem experienced by organisations, their suppliers and distributors were extensively discussed.

## PATHFINDER

The Managing Director of Greenland Company who attended the workshop identified the problems in the Supply Chain Management in his own industry to include crippling paper work, delays and wrong order deliveries. The workshop coordinator, who is the Chief Executive of Niger Consulting, proposed adoption of Electronic Data Interchange (EDI) by Stakeholders in the Supply Chain Management industries for greater efficiency.

In an attempt to convince the Board of Greenland Company to adopt EDI, you are required to

- a. Explain the term Electronic Data Interchange (EDI). (2 Marks)
  - b. State **FIVE** benefits derivable by Greenland through the use of EDI. (5 Marks)
  - c. Enumerate **TWO** problems associated with implementing EDI. (3 Marks)
  - d. Explain what is meant by competitive advantage. (2 Marks)
  - e. State **THREE** resources needed for the implementation of EDI. (3 Marks)
- (Total 15 Marks)**

### QUESTION 2

Considering the increasing need for computer literacy, you have been selected by your company to make a presentation to undergraduate Accounting students in your State's University.

In preparation for this, you are required to

- a. State **THREE** features that distinguish the mini-computer from the micro-computer. (3 Marks)
  - b. State **THREE** differences between General Purpose and Special Purpose Computers. (3 Marks)
  - c. Explain with the aid of a diagram, the configuration of a digital computer system. (5 Marks)
  - d. State **TWO** differences between Random Access Memory (RAM) and Read Only Memory (ROM). (4 Marks)
- (Total 15 Marks)**

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### QUESTION 3

The number of SMS messages exchanged every day is enormous. SMS messaging is now one of the most important revenue sources for wireless carriers.

You are required to:

- a.
    - (i) List **THREE** examples of SMS messaging applications. (3 Marks)
    - (ii) State **THREE** reasons why SMS is successful worldwide. (3 Marks)
    - (iii) State **TWO** advantages of email. (2 Marks)
  - b. Digital certificate can be used for a variety of electronic transactions.
    - (i) State **THREE** contents of a digital certificate. (3 Marks)
    - (ii) State who issues and signs a digital certificate? (1 Mark)
    - (iii) State **THREE** reasons for using a digital certificate. (3 Marks)
- (Total 15 Marks)**

### QUESTION 4

Mr. Johnson is the System Administrator in Paddy Nigeria Limited. The Managing Director of the company, Chief Williams, discovered anomalies in the reports generated by the computer system.

You are required to:




- a.
    - (i) State any **FOUR** error detection schemes. (4 Marks)
    - (ii) Explain briefly any **THREE** data processing methods. (6 Marks)
  - b.
    - (i) State **TWO** reasons why Adaptive Maintenance is necessary. (2 Marks)
    - (i) The **TWO** basic technologies employed in storage devices are magnetic and optical. List any **THREE** magnetic data storage media. (3 Marks)
- (Total 15 Marks)**

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### QUESTION 5

Database is a collection of related data and the contents of a database need to be described and presented to show the relationships among data.

**You are required to:**

- a. Explain the E – R Model. (2 Marks)
  - b. Explain with the aid of diagrams the following terms.
    - (i) one-to-one data relationship. (2 Marks)
    - (ii) one-to-many data relationship. (2 Marks)
    - (iii) Many-to-many data relationship. (2 Marks)
  - c. Describe briefly describe the following terms in relation to database.
    - (i) Entity (2 Marks)
    - (ii) Attribute (2 Marks)
  - d. Explain each of the following symbols representation in an E – R diagram.
    - (i) Rectangle  (1 Mark)
    - (ii) Line  (1 Mark)
    - (iii) Diamond  (1 Mark)
- (Total 15 Marks)**

### QUESTION 6

Physical and logical access controls are designed to protect the resources of the computer system.

**You are required to:**

- a. Define Data Integrity (2 Marks)
- b. Identify **FOUR** ways by which Data Integrity can be compromised. (4 Marks)
- c. Explain each of the following types of Data Integrity:
  - (i) Domain Integrity
  - (ii) Entity Integrity
  - (iii) Referential Integrity
  - (iv) User Defined Integrity (8 Marks)

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d. State **ONE** role of flow charting as a System Evaluation Procedure.

(1 Mark)

(Total 15 Marks)

### SOLUTIONS TO SECTION A

#### PART I

#### MULTIPLE-CHOICE QUESTIONS

1. B
2. E
3. D
4. B
5. E
6. C
7. E
8. B
9. A
10. E
11. E
12. D
13. A
14. D
15. C
16. C
17. C
18. E
19. B
20. D

#### EXAMINERS' REPORT

The questions test candidates' knowledge and understanding of various topics of the syllabus.

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The performance was average as over 50% of the candidates scored above 40% of the allocated mark.

Candidates are advised to read widely and prepare well for future examinations.

## **PART II      SHORT-ANSWER QUESTIONS**

1. Central Processing Unit (CPU)
2. Port
3. DVD – (Digital Versatile Disk)/Digital Video Disk
4. Bluetooth
5. Grid
6. Duplicated
7. Modification
8. Webtrust
9. Hot database backup
10. Hyper Text Transfer Protocol
11. Updating
12. Multiprocessing
13. Process Control Block (PCB)
14. Security Assessment Tools
15. Customer Relationship Management (CRM)
16. Referential integrity
17. Committee of Sponsoring Organisations
18. Logical access control/(Identification & Authentication)
19. Run control total
20. End-users (IT-customers)

## **EXAMINERS' REPORT**

The questions test candidates' knowledge and understanding of various topics of the syllabus.

## **PATHFINDER**

Performance was poor as over 70% of the candidates scored below 30% of the allocated mark.

The major pitfall was the inability of most of the candidates to state the appropriate required technical terms.

Candidates are advised to prepare well for future examinations.

### **SOLUTIONS TO SECTION B**

#### **QUESTION 1**

- a. Electronic Data Interchange (EDI) is a direct computer-to-computer transfer of transaction information contained in standard business documents such as invoices and purchase orders in a standard format.
- b. Benefits achievable by Greenland include:
  - ❖ Reduction in paper-work
  - ❖ Competitive advantage
  - ❖ Shortening of handling time
  - ❖ Reduction of errors in data entry
  - ❖ Better customer interaction
  - ❖ Increased suppliers' orders
  - ❖ Availability of up-to-date information to suppliers' as well as the Greenland company
- c. Problems associated with implementing EDI include:
  - ❖ Cost of acquisition of hardware to be used for EDI
  - ❖ Cost of acquisition of software
  - ❖ The company has to conform with standards of EDI
  - ❖ Training of staff
  - ❖ Resistance of employee to change to EDI environment
  - ❖ EDI uses a special EDI software to be manned by an expert or skilled employee and the expert will be paid an enhanced salary
  - ❖ Hacking problem
  - ❖ Virus/worms effects



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- d. Competitive advantage is the provision of a product or service in a way that customers value it better than those of the competitors.
- e. Resources needed for EDI implementation include:
- Workstations
  - Output devices e.g. Monitor, Printer
  - Router/communication processors
  - Telecommunication channel (Physical or wireless)
  - Communication software/operating system
  - EDI software
  - Input devices like keyboard, scanner and Magnetic Character Reader (MCR) e.t.c.
  - Backing storage facilities e.g. hard disk

### EXAMINERS' REPORT

The question tests candidates' understanding of the proper implementation of Electronic Data Interchange (EDI) in a Supply Chain Management System.

The performance was above average as over 60% of the candidates scored over 40% of the allocated mark.

The commonest pitfall was the inability of candidates to relate the implementation of EDI to the organization.

Candidates are encouraged to read widely and in particular ICAN Study Pack and Pathfinder.

### QUESTION 2

- a. Differences in features of Mini computers and Micro computers:

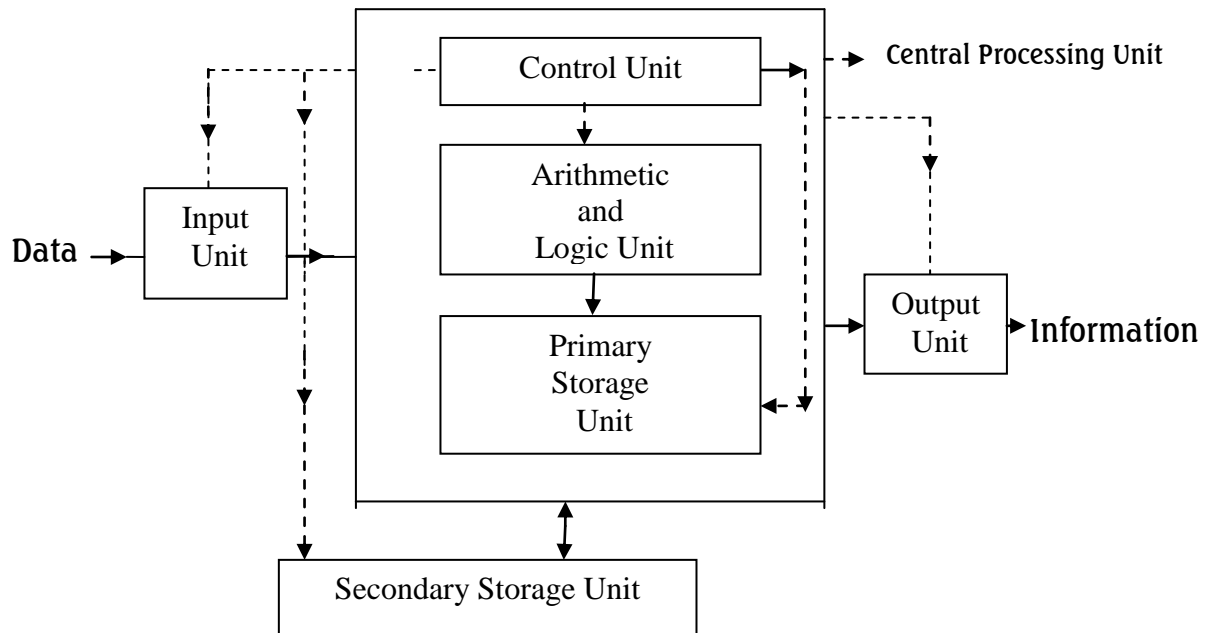
Mini-computer	Micro-computer
Uses Medium Scale Integration (MSI)	Uses Small Scale Integration (SSI)
Cost of acquisition is high	Cost of acquisition is low
Can access up to 500 terminals or workstations on a network	Can access up to 250 terminals or workstations on a network
Operates under Air-conditioners	Operates under normal room temperature
Large in size	Small In Size

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(b) Differences between General Purpose and Special Purpose computers:

General purpose computer	Special purpose computer
Designed to solve a wide range of problems	Designed to solve special problems or jobs
Relating problems on science, technology, education, business are solved using General purpose computers	Use for monitoring war situations, monitoring space launching and controlling robots
Examples include: mainframe, mini/midi and microcomputers	Examples include slaves

(c) Computer Hardware Configuration



Key  Data flow  
 Signal flow

**Input Unit:** This is the unit through which data and programs enter into the computer. It uses devices called input devices e.g. keyboard.

**Output Unit:** This is the unit through which information goes out from the computer. e.g. Printer.

**Secondary Storage Unit:** This is an external storage of the computer. It holds data and information permanently.

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**Central Processing Unit:** This is the power house of an electronic computer. It is the actual processor of the computer and it consists of three components: control unit, Arithmetic and Logic unit and Primary storage unit. The CPU transforms data by performing arithmetic and logical operations on them.

d. Differences between RAM and ROM include:

Random Access Memory (RAM)	Read Only Memory (ROM)
Provides temporary storage and loses all its contents as soon as computer is turned off i.e. it is a volatile storage	Provides permanent storage. Data and programs can be retained after the computer is turned off i.e. it is a non-volatile storage
It is random access and also it is READ and WRITE	Its content cannot be changed by the users i.e. it is READ-ONLY.
It stores data ready for processing and information from the CPU	It stores booting programs

### EXAMINERS' REPORT

The question tests candidates' knowledge on the features as well as differences between General Purpose and Special Purpose computers on one hand, and that of the mini and micro-computers on the other. The question also demands for the differences between RAM and ROM.

Over 90% of the candidates attempted this question and performance was above average, as over 60% of the candidates scored more than 40% of the allocated mark.

The commonest pitfall was that most candidates could not provide the required differences.

Candidates are advised to read widely particularly the ICAN Study Pack and Pathfinder.

### QUESTION 3

a. (i) Examples of SMS messaging applications include:

- Person-to-person text messaging
- Provision of information
- Downloading
- Alerts and notifications
- SMS marketing

## **PATHFINDER**

(ii) Reasons why SMS is successful worldwide include:

- SMS messages can be sent and read at any time
- SMS messages can be sent to an offline Mobile Phone
- SMS messages are supported by all GSM mobile phones and they can be exchanged between different operators or carriers.

(ii) Advantages of email include:

- It is faster to transmit (almost immediately);
- It is more convenient and ecologically friendly (no paper is required);
- There is automatic record of when the e-mail is received;
- It is possible to re-send the same email

b. (i) Contents of a Digital Certificate:

- Owner's public key
- Owner's name
- Expiration date of the public key
- Name of the Issuer (the CA that issued the Digital Certificate)
- Serial number of the Digital Certificate
- Digital signature of the issuer

(ii) A digital certificate is issued by a Certificate Authority (CA) and signed with the CA's private key.

(iii) Reasons for using a Digital Certificate include:

- It ensures that the user is whom he/she claims to be
- Digital certificates ensure integrity by giving the user peace of mind that the message or transaction has not been accidentally or maliciously altered
- Digital certificates ensure confidentiality and messages can only be read by authorised intended recipients
- Digital certificates also specify date and time, so that senders or recipients cannot dispute if the message was actually sent or received.

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## EXAMINERS' REPORT

The question tests candidates' awareness on SMS application as well as the use of Digital Certificate for a variety of electronic transactions.

Over 90% of the candidates attempted the question and performance was good, as over 60% of the candidates scored above 60% of the allocated mark.

The commonest pitfall was the candidates' interpretation of messaging application to refer to chatting by the use of blackberry, whatsapp etc.

Candidates are encouraged to read more literature on these topics.

## QUESTION 4

(a)(i) Error detection schemes include:

- Repetition Schemes
- Checksum
- Parity Schemes
- Horizontal and vertical redundancy checks
- Cyclic redundancy checks
- Hamming distance based checks

(ii) Data Processing methods include:

- Batch Processing: This is a data processing technique where related transactions are grouped together and transmitted for processing. The transactions are executed to completion without human interaction, so that all input data is pre-selected through scripts or command-line parameters. In Batch processing, a program takes a set of data files as input, processes the data and produces a set of output data files.
- On-line Processing: On-line Transaction Processing (OLTP) refers to transaction processing systems that facilitate and manage transaction-oriental applications, typically for data entry and retrieval transaction processing. On-line processing has also been used to refer to processing in which the system responds immediately to users' requests. An Automatic Teller Machine (ATM) used in Banks is an example of such a commercial transaction processing application.

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- Real-time processing: It is a transaction processing system that is subject to a “real-time constraint” i.e., operational deadlines from event to system response. The needs of real-time software are often addressed in the context of real-time operating systems, and synchronous programming languages, which provide frameworks on which to build real-time application software. A real time system is one where its application can be considered within context which are mission critical.
  - Distributed processing: This is the use of more than one processor to perform the processing of an individual task. It also refers to any of a variety of computer systems that use more than one computer or processor, to run an application. This includes parallel processing, in which a single computer uses more than one CPU to execute programs. More often however, distributed processing refers to Local-Area Networks (LANs) designed so that a single program can run simultaneously at various sites.
- b(i) Adaptive maintenance is necessary for the following reasons:
- User requirements may have changed or have been ill defined when the system was being designed.
  - The system environment may have significantly changed
  - The system may have grown beyond the limits that were originally envisaged for it.
- (ii) Magnetic storage devices include:
- Magnetic tape
  - Floppy disk
  - Hard disk
  - Magnetic cartridge
  - Magnetic stripe

# PATHFINDER

## EXAMINERS' REPORT

The question tests candidates' ability and understanding of the accuracy of presentation of information generated by the computer system for a company's use using some error detection schemes.

Less than 60% of the candidates attempted the question and performance was average, as over 50% of the candidates scored more than 40% of the allocated mark.

The major pitfall was the inability of the candidates to identify various types of error detection techniques.

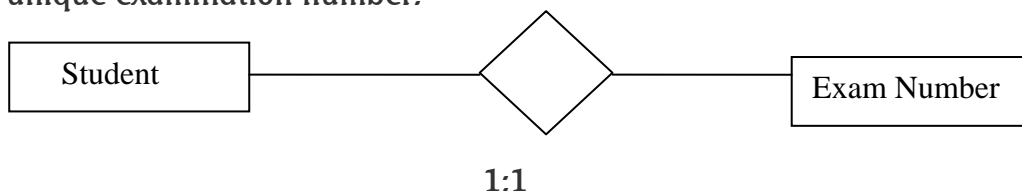
Candidates are advised to improve themselves by reading wide.

## QUESTION 5

a Entity – Relationship model (E-R model) is a logical representation of the data for an organisation or for a business area using entities for categories of data and relationships for association between entities. It is also a graphical depiction of the content of a database.

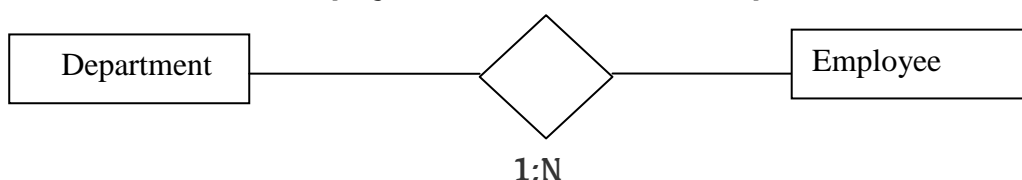
b(i) One-to-one data relationship

In one-to-one data relationship, a single entity instance of one type is related to a single entity instance of another type e.g. in an examination, a unique number is assigned to each candidate and each candidate is assigned a unique examination number.



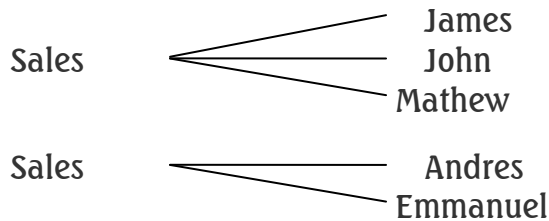
(ii) One-to-many data relationship

In one-to-many data relationship, a single instance of one entity relates to many instances of another entity e.g. Each department has N employees as members and each employee is a member of one department.



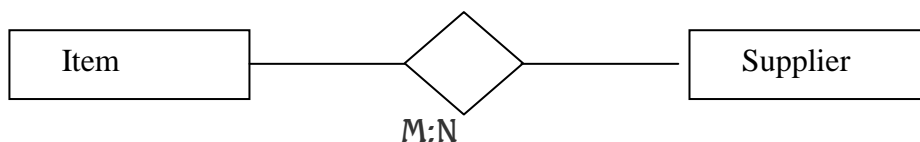
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### Example

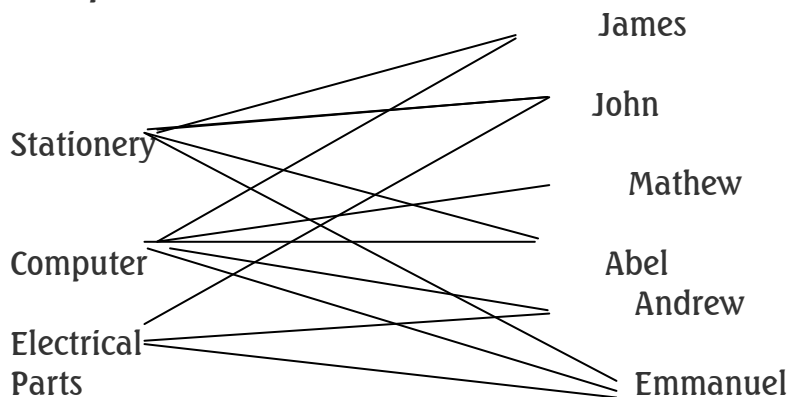


(iii) **Many-to-many data relationship**

Here, many instances of one entity relate to many instances of another entity, and vice versa, e.g. assuming three different items are required for a store and there exists many suppliers and each supplier may supply many different items. This type of relationship is referred to as many-to-many.



### Example



**c.(i) Entity**

Entity is a person, place, object, event or concept which can be identified in the user's work environment about which the organisation wishes to maintain data.

(ii) **Attribute**

Attribute is the property which describes the characteristics of an entity.



## PATHFINDER

- d. (i) Rectangle represents entities  
(ii) Line represents flow of data  
(iii) Diamond represents relationships between entities

### EXAMINERS' REPORT

This question tests candidates understanding of the various types of E-R models in a database structure.

Less than 24% of the candidates attempted the question and the performance was poor as more than 20% of the candidates scored less than 10% of the allocated mark.

Major pitfall was the inability of the candidates to properly use the diagram to represent the required E-R model relationships. They could not also give the correct interpretation of the E-R model.

Candidates are advised to improve on their reading and coverage of the syllabus.

### QUESTION 6

- a. Data integrity is the consistency and accuracy of the data stored in a database i.e. the correctness and consistency of the data.
- b. Ways by which data integrity can be compromised include:
- Human errors when data is entered
  - Errors that occur when data is transmitted
  - Software bugs
  - Hardware malfunctions such as disk crashes
  - Natural disasters such as flood, fire etc
  - Viruses/worms
- c. (i) Domain integrity
- Domain integrity/column integrity specifies the set of data values that are valid for a column and determines whether null values are allowed and enforced by validating checks.

## **PATHFINDER**

(ii) Entity integrity

Entity/table integrity requires that all rows in a table have a unique identifier/primary key

(iii) Referential integrity

This ensures that the relationship between the primary key in a referenced table and the foreign key in each of the referencing tables is always maintained

(iv) User-defined integrity

This allows users to define specific business rules that do not fall into one of the other integrity categories

d. Roles of flow charting include

- It aids system analysis
- It aids system documentation

### **EXAMINERS' REPORT**

The question tests candidates understanding of various types of data integrity. Less than 30% of the candidates attempted the question and performance was very poor as over 20% of the candidates scored less than 10% of the allocated mark.

The major pitfall was the inability of the candidates to understand the basic knowledge of the concept of the various types of data integrity.

Candidates are advised to read widely.

# PATHFINDER

THE INSTITUTE OF CHARTERED ACCOUNTANTS OF NIGERIA

PROFESSIONAL EXAMINATION I - MAY 2014

## MANAGEMENT ACCOUNTING

Time Allowed: 3 hours

### SECTION A: PART I      MULTIPLE-CHOICE QUESTIONS      (20 Marks)

#### ATTEMPT ALL QUESTIONS IN THIS SECTION

Write ONLY the alphabet (A, B, C, D or E) that corresponds to the correct option in each of the following questions/statements.

- The following are roles performed by the Management Accountant **EXCEPT**
  - Planning a profitable future for the business
  - Preparing reports for stewardship purpose
  - Installation and maintenance of accounting system to monitor the performance of the business
  - Identification of potential problems
  - Recording transactions for producing accounting statements
- Adlak Nigeria Limited has a total fixed cost of ₦7,360,000. It produces and sells two products, A and B. You are given the following details:

Product	Selling Price	Variable Cost
A	₦200	₦120
B	₦300	₦200

If the products are sold in constant mix of 40% of A and 60% of B (in units), determine the breakeven point in units.

- 81,776 units
- 80,000 units
- 75,000 units
- 69,500 units
- 49,600 units

## PATHFINDER

- |                |            |
|----------------|------------|
|                | <b>N'M</b> |
| Initial outlay | 40         |
| Cash inflows   | 75         |
| Cash outflows  | 25         |

A. 75.00%  
B. 53.33%  
C. 40.00%  
D. 25.00%  
E. 13.33%

- |                  |           |
|------------------|-----------|
|                  | ₦         |
| Opening payables | 150,000   |
| Closing payables | 75,000    |
| Purchases        | 1,400,000 |

## PATHFINDER

Determine the payment for the year.

- A. ~~₦~~1,250,000
  - B. ~~₦~~1,325,000
  - C. ~~₦~~1,450,000
  - D. ~~₦~~1,475,000
  - E. ~~₦~~1,750,000
7. The stage in corporate planning process that provides an answer to what the business is attempting to achieve is known as
- A. Continuous re-appraisal stage
  - B. Assessment stage
  - C. Objective determination stage
  - D. Appraisal stage
  - E. Implementation stage
8. A product has a marginal revenue of  $\text{₦}200 - 0.0008q$  and unit variable cost of  $\text{₦}70$  ( $q$  = quantity in units).  
What is the optimal output?
- A. 81,250 units
  - B. 160,000 units
  - C. 162,500 units
  - D. 175,000 units
  - E. 325,500 units
9. A new product required 1,000kg of a particular raw material. 600kg of the raw material are in stock at unit price of  $\text{₦}20/\text{kg}$ . If not used for the new product, it will have to be disposed off at a price of  $\text{₦}15/\text{kg}$ . Current replacement cost per kg of the material is  $\text{₦}25$ . What is the relevant cost of the 1,000kg?
- A. ~~₦~~1,000
  - B. ~~₦~~10,000
  - C. ~~₦~~19,000
  - D. ~~₦~~22,000
  - E. ~~₦~~25,000

## PATHFINDER

10. ABC company has a machine with maximum production capacity of 20,000 units. The company expects three possible market demands that are equally likely: 15,000 units, 20,000 units and 24,000 units. Determine the expected demand in units.
- A. 18,000 units
  - B. 18,333 units
  - C. 19,667 units
  - D. 20,333 units
  - E. 21,500 units
11. In a period, 11,280kg of materials were used at a total standard cost of ₦138,744. The material usage variance was ₦1,476 adverse. What is the standard material usage for the period?
- A. 11,060kg
  - B. 11,160kg
  - C. 11,280kg
  - D. 11,290kg
  - E. 11,360kg
12. Which of the following types of capacity level expresses production volume in Standard hours?
- A. Practical capacity
  - B. Budgeted capacity
  - C. Idle capacity
  - D. Full capacity
  - E. Basic capacity
13. Which of the following fully represents methods of determining transfer price?
- A. Variable cost, full cost, market price and negotiated price
  - B. Variable cost, skimming cost, full cost and negotiated cost
  - C. Full cost, negotiated cost, market price and skimming cost
  - D. Negotiated cost, market cost, sunk cost and full cost
  - E. Sunk cost, variable cost, negotiated price and market price

## PATHFINDER

14. Assume labour is paid at a normal hourly rate of ₦200. In a particular period, labour is scarce and the shadow price is computed as ₦75 per hour. What maximum amount should the organisation be willing to pay per hour of overtime?
- A. ₦75
  - B. ₦125
  - C. ₦200
  - D. ₦275
  - E. ₦1,375
15. A project costs ₦250,000 and is payable now. Net cash flow of ₦40,000 per annum will be received from end of year 4 to year 12. What is the payback period?
- A. 6.25 years
  - B. 7.25 years
  - C. 8.00 years
  - D. 9.00 years
  - E. 9.25 years
- 16 Two of the perspectives encompassed in a balanced scorecard are
- A. Investors and shareholders perspective
  - B. Institutional and investment perspective
  - C. Financial and customer perspective
  - D. Customer and distribution perspective
  - E. Customer and supplier perspective
- 17 Which of the following criteria will a decision maker that is risk-neutral use?
- A. Maximax
  - B. Maximin
  - C. Minimax
  - D. Expected value
  - E. Opportunity cost

## PATHFINDER

18. The nature of work in HOPE Plc. is repetitive, with an 85% learning curve effect when a new product is developed. The time taken for the first unit was 18 minutes. The average time required to produce the first four units is

A. 13.01 minutes  
B. 15.30 minutes  
C. 16.20 minutes  
D. 17.30 minutes  
E. 18.00 minutes

19. The following data relate to the inventory costs of Plumo Plc. which uses the EOQ model to establish its re-order quantity for its single raw material:

Ordering costs	₦10 per order
Costs of transportation	₦60 per order
Buying price	₦20 per unit

Storage cost is 20% of the purchase price plus ₦0.30 per unit per annum.  
Annual demand is 5,000 units.

What is the EOQ to the nearest whole unit?

- A. 204 units  
B. 403 units  
C. 404 units  
D. 501 units  
E. 505 units
20. A type of Markov Chain in which there is no movement from one step to another is
- A. Egordic  
B. Regular  
C. Absorbing  
D. Recurrent  
E. Transient



# PATHFINDER

## SECTION A: PART II

## SHORT-ANSWER QUESTIONS

(20 Marks)

### ATTEMPT ALL QUESTIONS IN THIS SECTION

Write the answer that best completes each of the following questions/statements:

1. Any cost that is useful for decision-making is often referred to as.....
2. Risks that are peculiar or unique to each security or company are.....
3. A product or service sold at lower than normal margins in order to attract customers is known as.....
4. The following extract is taken from the production cost budget of Ego Limited:  

Production Units	2,000	3,000
Production Costs	₦111,000	₦129,000

What is the production cost for an activity level of 4,000 units?
5. A control system that is capable of adjustment for external factors is known as.....
6. Decisions that can be clearly defined and tailored through computer – based Management Information System are.....
7. A project is to generate an annual cash inflow of ₦450,000 at current prices for 10 years. Annual inflation rate of 15% is expected to affect the cash flow. If money cost of capital is 15%, what is the total present value of the inflow?
8. The Sales Director of XYZ Ltd. requires 100,000 units of product B to meet customers' demand. The opening inventory is estimated at 30,000 units while the company expects half of this at the year end.  
How many units of product B will be produced to meet the Sales Director's target?
9. What is the main objective of economic order quantity?

## PATHFINDER

Use the following data to answer questions 10 and 11:

K Ltd. has the following budget and actual data:

Budget fixed overhead cost	₦100,000
Budget production (units)	20,000
Actual fixed overhead cost	₦110,000
Actual production (units)	19,500

10. The capacity variance is .....
11. The volume variance is .....
12. The difference between the number of hours that actual production should have taken and the number of hours actually taken multiplied by the standard absorption rate per hour is called.....
13. Two of the objectives of decentralization of an organisation are.....and .....
14. A divisional manager requires a return on an investment of 30%. If total assets is ₦200,000, what operating profit must be generated to meet the target?
15. The transfer pricing objective which ensures the need to select the transfer method that can be used to appraise divisional managers and their division is.....
16. Ak Plc. runs regression between machine hours and total overhead cost. The correlation co-efficient is 0.8. What proportion of the total overhead cost is explained by changes in machine hours?
17. A company's labour cost reduces by 20% each time the output is doubled. What is the learning curve ratio of the company?
18. You are provided with the following data:

Economic Order Quantity = 70,000 pieces

Re-order period 20-28 weeks

Average consumption 6,000 pieces

Minimum consumption 4,400 pieces

Maximum consumption 8,400 pieces

## PATHFINDER

What is the maximum level of inventory?

19. Wakanow Ltd. mixes four raw materials to manufacture a rubber product with Material K costing ₦160 per kg, Material G costing ₦120 per kg, Material Z costing ₦180 per kg and Material U costing ₦320 per kg. Using the least cost mix method, what is the objective cost function, if each material contributes some basic quality to the rubber product?
20. The time available in facility C for products A and B are 2 minutes and 4 minutes respectively. During the week, the actual production was 6,000 units of product A and 700 units of Product B. Actual factory costs were ₦62,600. What is the throughput cost for the week if the cost per factory minute is ₦2?

**SECTION B:                      ATTEMPT QUESTION 1 AND ANY OTHER THREE QUESTIONS**  
**(60 Marks)**

### QUESTION 1

#### CASE STUDY

SAMOBBA Plc. is a group of companies with interest in Manufacturing, Consulting and Oil & Gas. The organisation has been successful in the past, but the market has now become competitive.

The manufacturing section is into baby toys, children bicycles and baby pushchairs. SAMOBBA Plc. has decided to launch a revolutionary new style of sporty pushchairs to compete effectively with the imported ones. The company has commissioned market research to establish possible demand for the sporting pushchairs and the information below has been obtained.

If the price is set at ₦4,250, demand is expected to be 100,000 pushchairs, at ₦5,000 it will be 73,000 pushchairs and at ₦6,000 it will be 42,000 pushchairs. Variable costs are estimated at ₦1,700, ₦2,100 or ₦2,600.

A decision needs to be made on what price to charge.

**You are required to**

- a. Produce a table showing the expected contribution for each of the nine possible outcomes. **(3Marks)**

## PATHFINDER

- ## QUESTION 2

A market research recently carried out at a cost of ₦1,500,000 (payable at the end of year 1) indicates a unit selling price of ₦300 in year 1, rising by 10% per annum. Sales volume for the four-year life of the project has been estimated as follows:

Possible unit variable costs are as follows:

The introduction of the new product is expected to reduce the market demand of an existing product by 5,000 units per annum. The existing product has a unit contribution of ₦75.

	<b>N</b>
Interest on borrowed funds to finance the project	50,000
Depreciation	250,000
Wages, rent, etc.	<u>1,000,000</u>
	1,300,000

## PATHFINDER

**Cost of capital is 12%.**

- a. Advise, with relevant calculations, whether the project should be accepted.  
(12 Marks)
- b. State and explain briefly **THREE** factors influencing pricing decisions.  
(3 Marks)

**(Total 15 Marks)**

Jasper Industries Limited makes up its accounts to 31 December yearly. The company's board of directors is desirous of establishing a new branch office to penetrate a new market. It has directed the Finance Director to prepare a Cash Budget that will assist the board take a decision on the loan required to finance the new branch office. This will supplement the free cash balance for the purpose of funding the branch office estimated to cost ₦7million.

	April	May	June	July	Aug.	Sept.	Oct.	Nov.
	N'000	N'000	N'000	N'000	N'000	N'000	N'000	N'000
Sales	3,600	3,800	4,500	4,800	4,700	4,500	4,900	4,500
Purchases	2,400	2,500	3,000	3,200	3,200	3,200	3,400	3,100
Admin/Selling Expenses	300	200	150	300	200	250	260	270
Wages/Salaries	500	550	600	720	450	480	500	520
Interest income	-	-	-	300	-	-	100	-
Taxation	-	300	-	-	-	350	-	-

(i) The company will purchase a new delivery van at a cost of ₦700,000. The vehicle will be paid for in September 2014 though delivery will take place in November 2014.

## PATHFINDER

- (ii) The company policy on sales is that 30% of sales is for cash while the remaining are credit sales to be collected as follows:
- 50% of the credit sales will be collected in the month of sales.
  - The balance of the credit sales will be collected in the month following sale.
- (iii) The company enjoyed the suppliers' policy of 20% of purchases for cash, while the balance is paid in the following month.
- (iv) The selling and administration expenses are paid for in the month they are incurred.
- (v) Wages and salaries are also paid in the month they are incurred.
- (vi) Interest income is received in the month in which it is due.
- (vii) Taxation is paid a month after it is due.
- (viii) Closing cash balance in June, 2014 is expected to be ₦150,000.

**You are required to**

- a. Prepare a monthly Cash Budget for the first 4 months ending 31 October, 2014. (12 Marks)
- b. Determine the amount of loan that will be required at the end of October, 2014 to pay for the new branch office. (3 Marks)
- (Total 15 Marks)**

### QUESTION 4

- a. Toksas Limited produces two products "Ken and Teks". The standard times for the production of the products are 30 minutes for Ken and 45 minutes for Teks. The budget for January is 60,000 units of Ken and 24,000 units of Teks. During the month, 28,000 labour hours were worked and 40,000 units of Ken and 15,000 units of Teks were produced.

**You are required to compute the following and interpret your result:**

- (i) The activity ratio (3 Marks)
- (ii) The efficiency ratio (3 Marks)
- (iii) The capacity ratio (3 Marks)
- b. State and explain briefly **SIX** objectives of budgetary control. (6 Marks)
- (Total 15 Marks)**

## PATHFINDER

### QUESTION 5

- a. Discuss the **THREE** key objectives of Transfer Pricing. (3 Marks)
- b. Aba Plc. has two divisions: A and B. The company is into the production of bicycles. Division A produces the bicycle frame and Division B assembles the bicycles' components onto the frame. There is a market for both the sub-assembly and the final product. Each division has been designed as a profit centre. The transfer price for the sub-assembly has been set at the long-run average market price. The following data are available for each division:

	₹
Estimated selling price for final product	30,000
Long-run average selling price for intermediate product	20,000
Incremental costs for completion in Division B	15,000
Incremental costs in Division A	12,000

The Manager of Division B has made the following calculations:

	₦	₦
Selling price for final product		30,000
Transferred – in cost (market)	20,000	
Incremental costs for completion	<u>15,000</u>	<u>35,000</u>
Contribution		(5,000)

**You are required to advise Aba Plc if**

- (i) Transfers should be made to Division B, assuming there is no excess capacity in Division A. Is the market price the correct transfer price?  
(7 Marks)
- (ii) Division A's maximum capacity for this product is 1,000 units per month and sales to the intermediate market are now 800 units and assuming that for various reasons, A will maintain the ₦20,000 selling price indefinitely; (that is, A is not considering lowering the price to outsiders even if idle capacity exists); should 200 units be transferred to Division B and at what transfer price?  
(5 Marks)
- (Total 15 Marks)**

## PATHFINDER

### QUESTION 6

BOTISERI Ltd. has the following total factory overhead computed at both the high and low levels of activity for a given month of operation:

Levels of activity	High	Low
Direct labour hours	150,000	100,000
Total factory cost(₦)	352,500	284,000

The total factory overhead above consists of indirect materials, repairs and rent expenses. The company has analysed, at the 100,000 direct labour hours of activity level that costs exist in the following proportions:

	₦
Indirect materials (variable)	100,000
Repairs	64,000
Rent (fixed)	<u>120,000</u>
	<u>284,000</u>

For planning purposes, the company wishes to break the repairs cost into its variable and fixed elements.

You are required to

- Determine how much of the ₦352,500 total factory overhead costs at the high level of activity above that relates to repairs costs. (6 Marks)
  - Determine by means of the high and low method of cost analysis, the cost function for the repairs cost. (5 Marks)
  - State **FOUR** major problems involved in separating mixed costs into fixed and variable elements in practice. (4 Marks)
- (Total 15 Marks)

### SOLUTIONS TO SECTION A

#### PART I MULTIPLE-CHOICE QUESTIONS

- B
- B
- A
- E
- E



## PATHFINDER

- |     |   |
|-----|---|
| 6.  | D |
| 7.  | C |
| 8.  | C |
| 9.  | C |
| 10. | C |
| 11. | B |
| 12. | D |
| 13. | A |
| 14. | D |
| 15. | E |
| 16. | C |
| 17. | C |
| 18. | A |
| 19. | C |
| 20. | B |

## WORKINGS

2. Contribution per unit
- |   |                  |
|---|------------------|
| A | <del>₹</del> 80  |
| B | <del>₹</del> 100 |
- Weighted contribution per unit
- $$= (0.4 \times \text{₹}80) + (0.60 \times \text{₹}100) = \text{₹}92$$
- $$\text{BEP in unit} = \frac{\text{₹}7,360,000}{\text{₹}92}$$
- $$= 80,000 \text{ units}$$

5. **Sensitivity analysis of cash flow**
- NPV**
- 
- PV of inflows  
– 40+75–25
- =**  $\frac{75}{75}$
- =**  $\frac{10}{75}$
- = 13.33%**

## PATHFINDER

- 18.

19.

**PROFESSIONAL EXAMINATION I - MAY 2014**

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# PATHFINDER

## EXAMINERS' REPORT

The question tests a considerable portion of the syllabus. Many candidates did not seem to have a proper grasp of the questions and performance was below average.

Candidates are advised to be conversant with Management Accounting principles, concepts, techniques and tools.

## PART II SHORT-ANSWER QUESTIONS

1. Relevant cost
2. Unsystematic risk/ Diversifiable risk/Idiosyncretic
3. Loss leader
4. ₦147,000
5. Open-loop system
6. Programmed decision or Computer Aided Information or Computer Assisted Decision package
7. ₦4,500,000
8. 85,000 units
9. Minimizes Inventory Cost
10. ₦2,500 Adverse
11. ₦2,500 Adverse
12. Efficiency variance
13. Incentive, Training or Efficiency, Effectiveness or Performance Evaluation, Motivation
14. ₦60,000
15. Performance Evaluation
16. 64%
17. 80%
18. 217,200 pieces
19.  $₦160x_1 + ₦120x_2 + ₦180x_3 + ₦320x_4$
20. ₦29,600

## PATHFINDER

## WORKINGS

4.	Units	Costs
	<del>N</del>	<del>N</del>
High level	3,000	129,000
Low level	(2,000)	(111,000)
	<u>1,000</u>	<u>18,000</u>

$$\text{Variable cost per unit} = \frac{\text{N}18,000}{1,000} = \text{N}18$$

**Total variable cost at high level = 3,000 x £18 = £54,000**

Fixed cost = a

$$a = y - vc$$

$$= \text{N}129,000 - \text{N}54,000 = \text{N}75,000$$

Therefore, cost of 4,000 units = N75,000 + 4,000 (N18)

**= ₦147,000**

7. ~~₦~~450,000 x 10 = ~~₦~~4,500,000

**Note: The inflation rate and cost of capital cancel out.**

	Units
Sales	100,000
Closing stock (1/2 of opening)	<u>15,000</u>
	115,000
Less opening stock	<u>30,000</u>
Production	<u>85,000</u>

10. Absorption Rate =  $\frac{\text{N}100,000}{20,000} = \text{N}5$  per unit

**Volume of variance = ₦5 (19,500 – 20,000)**

**= ~~₹~~2,500 Adverse.**

11.

Budgeted production units	20,000
Less Actual production unit	<u>19,500</u>
Capacity underutilisation =	<u>500</u>
	500 x ₹5

## PATHFINDER

∴ Capacity variance is = ₹2,500 Adverse

Multiply by standard overhead =  
Cost per unit ~~£5~~

18. Maximum level of stock =

**=217,200 pieces**

- $$= 14,800 \times \text{N2 per minute} = \text{N29,600}$$

## EXAMINERS' REPORT

The questions test a sizeable part of the syllabus. Many candidates displayed lack of knowledge of the requirements, hence performance was poor. Candidates are advised to be accustomed to existing and current Management Accounting terminologies, concepts, and principles.

## SOLUTIONS TO SECTION B

## QUESTION 1

## CASE STUDY

	SP	VC	Contribution per unit	Expected demand	Expected Contribution
	<del>N</del>	<del>N</del>	<del>N</del>	<del>N</del> '000	<del>N</del> '000
S <sub>1</sub>	4,250	1,700	2,550	100	255,000
	5,000	1,700	3,300	73	240,900
	6,000	1,700	4,300	42	180,600
	4,250	2,100	2,150	100	215,000
	5,000	2,100	2,900	73	211,700

## PATHFINDER

$S_2$	6,000	2,100	3,900	42	163,800
	4,250	2,600	1,650	100	165,000
$S_3$	5,000	2,600	2,400	73	175,200
	6,000	2,600	3,400	42	142,800

SP is selling price

VC is variable cost

## Summary of Expected Contribution

	₦1,700	₦2,100	₦2,600
Price/VC			
	₦'000	₦'000	₦'000
₦4,250	255,000	215,000	165,000
₦5,000	240,900	211,700	175,200
₦6,000	180,000	163,800	142,800

### ALTERNATIVE SOLUTION

## CASE STUDY SOLUTION

**SAMOBA PLC**

## SUMMARY OF EXPECTED CONTRIBUTION

VC/Price	<del>N</del> 4,250	<del>N</del> 5,000	<del>N</del> 6,000
	<del>N</del> '000	<del>N</del> '000	<del>N</del> '000
<del>N</del> 1,700	255,000	240,900	180,600
<del>N</del> 2,100	215,000	211,700	163,800
<del>N</del> 2,600	165,000	175,200	142,800

### COMPUTATION OF CONTRIBUTION FOR THE POSSIBLE OUTCOMES

	per unit	Units	₹
(i)	(4,250–1,700)	100,000	=255,000,000
(ii)	(4,250– 2,100)	100,000	= 215,000,000
(iii)	(4,250 –2600)	100,000	= 165,000,000
(iv)	(5,000 -1,700)	73,000	= 240,900,000
(v)	(5,000–2,100)	73,000	= 211,700,000
(vi)	(5,000–2,600)	73,000	= 175,200,000
(vii)	(6,000 –1,700)	42,000	= 180,600,000
(viii)	(6,000 –2,600)	42,000	= 142,800,000

## PATHFINDER

- b(i)** Maximax criterion looks at the best possible results. It means 'maximise' the maximum profit. In this case, maximise the maximum contributions.

Demand/ price	Maximum Contribution
	₦'000
100,000/ ₦4,250	255,000
73,000/ ₦5,000	240,900
42,000/ ₦6,000	180,600

**SAMOBA Plc. would therefore set price at ₦4,250**

- (ii) Maximin criterion involves choosing the outcome that offers the least unattractive worst outcome. In this situation, choose the outcome which maximises the minimum contribution.

Demand /Price	Minimum Contribution
	₦'000
100,000/ <del>₦4</del>	165,000
73,000/ <del>₦5</del>	175,200
42,000/ <del>₦6</del>	142,800

**SAMOBA Plc. would set a price of ₦5,000**

- (iii) From setting a price of ₦5,000 and Variable Cost of ₦2,600, the opportunity loss would be ₦175,200,000 – ₦175,200,000 = 0

- (iv) At a price of ₦5,000 and variable Cost of ₦1,700 the opportunity loss would be  $₦255,000,000 - ₦240,900,000 = ₦14,100,000$

- (v) At ₦5,000 and vc of ₦2,100, opportunity loss = ₦215,000,000 – ₦211,700,000 = ₦3,300,000

- (vi) at ₦6,000 and vc of ₦1,700, opportunity loss = ₦255,000,000  
- ₦180,600,000 = ₦74,400,000

- (vii) At ₦6,000 with vc of ₦2,100, opportunity loss = ₦215,000,000 - ₦163,800,000 = ₦51,200,000

- (viii) At 6,000 with vc of ~~₦2,600~~, opportunity loss = ~~₦175,200,000 – ₦142,800,000 = ₦32,400,000~~

- (ix) At ₦4,250 with vc of ₦2,600, opportunity loss = ₦175,200,000 – ₦165,000,000 = ₦10,200,000

## PATHFINDER

- | Price | $S_1$  | $S_2$  | $S_3$  | Maximum Regret |
|-------|--------|--------|--------|----------------|
| 4,250 | -      | -      | 10,200 | 10,200         |
| 5,000 | 14,100 | 3,300  | -      | 14,100         |
| 6,000 | 74,400 | 51,200 | 32,400 | 74,400         |
- Minimax regret strategy (4,250) minimises the minimax regret (10,200.000).

- (c) Expected value is a criterion in which probabilities are assigned to different outcomes in order to evaluate the worth of a decision. When given a number of alternative decisions, each with a range of possible outcomes, an optimum decision is the one which gives the highest expected value. The expected value will never actually occur. They are more of valuable guide to decision making where they refer to outcomes which will occur many times or repeatedly. Information was not given on probabilities of each demand occurring in SAMOBA Plc. baby pushchairs. It is also unlikely that demand will be sufficiently predictable to use this technique successfully.

**(biii) Working Note**

- (i) At a variable cost (vc) of ₦1,700, the best strategy would be a price of ₦4,250 i.e.  $₦255,000,000 - ₦255,000,000 = 0$
- (ii) At variable cost of ₦2,100,  $₦215,000,000 - ₦215,000,000 = 0$  best strategy of ₦4,250

## EXAMINERS' REPORT

The question tests candidates' knowledge of decision making under risk making using maximax, maximin and minimax regret rule. Part 'a' of the question demands the preparation of 'Pay-off' table showing expected contributions for the different levels of demand.

Part 'b' requires a brief explanation of the maximax, maximin and minimax regret rule with reference to the pay-off table constructed in 'a' while part 'c' requests for an explanation of the usefulness of expected values.



## PATHFINDER

Candidates had a challenge in explaining the usefulness of expected values and its application on the scenarios given in the question. Candidates are advised to familiarize themselves with basic analytical tools for decision making in Management Accounting. Candidates should ensure proper presentation of solutions and show their workings.

## QUESTION 2

Year	0	1	2	3	4
	N'000	N'000	N'000	N'000	N'000
Outlay	(14,000)				
Working Capital	750				
Operating Cash flow (w1)		1,505	5,255	8,060	10,409
Scrap value	—	—	—	—	1,000
Net Cash flow	(13,250)	1,505	5,255	8,060	10,659
PVF@12%	<u>1</u>	<u>0.8429</u>	<u>0.7972</u>	<u>0.7118</u>	<u>0.6355</u>
Net Present Value (NPV)	<u>(13,250)</u>	<u>1,343.815</u>	<u>4,189.286</u>	<u>5,737.108</u>	<u>6,773.795</u>
Total NPV		N4794.004			

**RECOMMENDATION:.** The Project is acceptable in view of positive NPV, if other factors remain the same.

## WORKINGS

Year	1	2	3	4
Sales volume (unit)	60,000	85,000	85,000	80,000
Selling price (units)	<del>₦300</del> ₦'000	<del>₦330</del> ₦'000	<del>₦363</del> ₦'000	<del>₦399.3</del> ₦'000
Total sales	18,000	28,050	30,855	31,944
Variable cost (x <del>₦252</del> )	<u>15,120</u>	<u>21,420</u>	<u>21,420</u>	<u>20,160</u>
Total Contribution	2,880	6,630	9,435	11,784
New product Contribution	<u>(375)</u>	<u>(375)</u>	<u>(375)</u>	<u>(375)</u>
Net Contribution	2,505	6,255	9,060	11,409
Net fixed cost (wc)	<u>(1,000)</u>	<u>(1,000)</u>	<u>(1,000)</u>	<u>(1,000)</u>
Net INFLOW	1,505	5,255	8,060	10,409

## PATHFINDER

- (ii) Expected Variable Cost per unit  
 $(240 \times 0.4) + (260 \times 0.6) = \text{N}252$

## EXAMINERS' REPORT

The question tests candidates understanding of Project Appraisal. Candidates were expected to sift the relevant costs from the irrelevant costs and utilize these in evaluation of whether the project should be accepted or not. They are also expected to state three factors influencing pricing decision. Only about 22% of the candidates attempted the question and performance was poor.

The major pitfalls were candidates' inability to differentiate between the relevant and irrelevant costs of the project to arrive at the NPV. Columnar presentation was muddled up by many candidates and they did not add back the working capital saved at the end of the project term.

**Candidates are advised to practise with related questions on Project Appraisal.**

### QUESTION 3

- (a)

**JASPER INDUSTRIES LIMITED**  
**CASH BUDGET FOR JULY –OCT 2014**

	JULY	AUG	SEP	OCT
	N'000	N'000	N'000	N'000
Cash Inflow				
Cash sales	1,440	1,410	1,350	1,470
Debtors receipts (1)	1,680	1,645	1,575	1,715
(2)	1,575	1,680	1,645	1,575
Interest Income	<u>300</u>	<u>—</u>	<u>—</u>	<u>100</u>
Total cash inflow	<u>4,995</u>	<u>4,735</u>	<u>4,570</u>	<u>4,860</u>
Cash outflow ∴				
Cash purchases	640	640	640	680
Creditors payment	2,400	2,560	2,560	2,560
Delivery vans	—	—	700	—
Selling & Admin exp	300	200	250	260
Wages & salaries	720	450	480	500
Taxation	<u>—</u>	<u>—</u>	<u>—</u>	<u>350</u>
Total cash outflow	<u>4,060</u>	<u>3,850</u>	<u>4,630</u>	<u>4,350</u>

## PATHFINDER

Net Inflow	935	885	(60)	510
Opening balance	<u>150</u>	<u>1,085</u>	<u>1,970</u>	<u>1,910</u>
Closing balance	<u>1,085</u>	<u>1,970</u>	<u>1,910</u>	<u>2,420</u>

(b)

	N'000
Closing cash balance	2,420
Required Loan	<u>4,580</u>
Fund Required	<u>7,000</u>

### WORKINGS

Debtors Control Budget								
	April	May	Jun	Jul	Aug	Sept	Oct	Nov
	N'000	N'000	N'000	N'000	N'000	N'000	N'000	N'000
Sales	3,600	3,800	4,500	4,800	4,700	4,500	4,900	4,500
Cash sales	1,080	1,140	1,350	1,440	1,410	1,350	1,470	1,350
30%								
Credit sales	<u>2,250</u>	<u>2,660</u>	<u>3,150</u>	<u>3,360</u>	<u>3,290</u>	<u>3,150</u>	<u>3,430</u>	<u>3,150</u>
7%								
Debtors receipt	1,260	1,330	1,575	1,680	1,645	1,575	1,715	1,575
" "	—	<u>1,260</u>	<u>1,330</u>	<u>1,575</u>	<u>1,680</u>	<u>1,645</u>	<u>1,575</u>	<u>1,715</u>
Total Receipt	<u>1,260</u>	<u>2,590</u>	<u>2,905</u>	<u>3,255</u>	<u>3,325</u>	<u>3,226</u>	<u>3,290</u>	<u>3,290</u>

Credit Control Budget N'000								
	April	May	June	July	Aug.	Sept.	Oct.	Nov.
	N'000	N'000	N'000	N'000	N'000	N'000	N'000	N'000
Purchases	2,400	2,500	3,000	3,200	3,200	3,200	3,400	3,100
Cash purchases 20%	<u>480</u>	<u>500</u>	<u>600</u>	<u>640</u>	<u>640</u>	<u>640</u>	<u>680</u>	<u>620</u>
Credit purchases	1,920	2,000	2,400	2,560	2,560	2,560	2,720	2,480
80%								
Creditors payment	—	1,920	2,000	2,400	2,560	2,560	2,560	2,720

### EXAMINER'S REPORT

The question tests candidates' knowledge on the preparation of Cash Budgets and the determination of amount of loan required at end of period.

About 95% of candidates attempted the question. Candidates are expected to prepare the Cash Budget to show the Inflow, Outflow and Net Cash Flow and determine the amount of loan required.

## PATHFINDER

**Candidates understood the question but performance was just average.**

The commonest pitfalls were candidates' inability to correctly determine the Receivables and the Payables as wrong timings were used. Some candidates also used statements of Profit or Loss format and attempted to obtain gain or loss. Some other formats were used by a few candidates.

Candidates could not correctly determine the Net Cash Flows and Interest received was treated as Outflow. A number of candidates omitted the currency and the thousand on top of the presentation thus losing valuable marks. The budget period was also confused by some candidates.

Candidates are advised to properly digest questions before tackling them. They should not prepare solutions without proper captions and headings. Candidates should ensure adequate coverage of the syllabus and follow standards format in questions of this nature.

### QUESTION 4

Products	Ken	Teks	
Standard time per product	30 min/unit	45 min/unit	
January budget	60,000 units	24,000 units	
Actual production	40,000 units	15,000 units	
Actual labour hours (given)	28,000 hrs		
			Total
Standard hours for production	$40,000 \times 30/60 = 20,000\text{hrs}$	$15,000 \times 45/60 = 11,250\text{ hrs}$	31,250 hrs
Budgeted production hours	$60,000 \times 30/60 = 30,000\text{hrs}$	$24,000 \times 45/60 = 18,000\text{ hrs}$	48,000 hrs

(i) Activity ratio =  $\frac{\text{Standard hours}}{\text{Budgeted hours}} = \frac{31,250}{48,000} \times 100 = 65.10\%$

∴ 65.10% of budgeted activity was achieved or production was 34.90% less than budgeted.

(ii) Efficiency Ratio =  $\frac{\text{Standard hours}}{\text{Actual hours}} = \frac{31,250}{28,000} \times 100 = 111.60\%$

Work was 11.60% above normal level of efficiency. The plant was efficiently run by 11.60% .

(iii) Capacity Ratio =  $\frac{\text{Actual Hours Worked}}{\text{Budgeted hours}} = \frac{28,000}{48,000} \times 100 = 58.33\%$

Toksas operated only 58.33% or operated 41.67% below its installed capacity.

## PATHFINDER

(b) Objectives of budgetary control are to

- Plan and coordinate the various activities of the business
- Provide a yardstick to compare actual results with plan
- Act as a guide for management decision
- Draw attention to where to direct appropriate action for improvement
- Measure each units performance
- Plan and control Income and expenditure so that maximum profitability is achieved
- Create cost awareness.
- Direct capital expenditure in the most profitable way
- To revise the budgeted figures if considered neccessary
- Centralise control

### EXAMINERS' REPORT

The question tests candidates' understanding of computation and interpretation of some control ratios. Part 'b' of the question tests their understanding of the objectives of Budgetary Control. Candidates are expected to compute the Efficiency, Activity and Capacity ratios based on given details.

They are expected to state and explain six objectives of Budgetary Control. Candidates' understanding of the question was superficial as performance was below average. About 40% of them who attempted the question were able to compute the ratios but could not correctly interpret their computations. Many were unable to compute the Total Standard Hours and the Budgeted Production Hours required to compute the ratios. Many were not also able to state the formulas correctly and apply them.

Candidates are advised to sharpen their knowledge of Cost Accounting principles to be able to excel in this stage of the Institute's examinations.

### QUESTION 5

(a) Objectives of Transfer pricing include the following:

- (i) **Goal congruence:** The price should be set so that the divisional management's desire to maximize divisional profit is consistent with the objectives of the company as a whole.

## PATHFINDER

- (b) The company's contribution as a whole

	DIVISION A <del>₦</del>	DIVISION B <del>₦</del>	COMPANY  <del>₦</del>
Selling price	20,000	30,000	30,000
Incremental Cost (A)	(12,000)	(20,000)	(12,000)
Incremental Cost (B)	<u>—</u>	<u>(15,000)</u>	<u>(15,000)</u>
Contribution	<u>8,000</u>	<u>(5,000)</u>	<u>3,000</u>

- |  |                  |
|--|------------------|
| The overall profit would be as follows:                      | ₦                |
| Contribution from excess capacity (200 x <del>₦3,000</del> ) | 600,000          |
| Contribution from 800 units = 800 x <del>₦8,000</del>        | <u>6,400,000</u> |
|  | 7,000,000        |

## EXAMINERS' REPORT

**Candidates are expected to discuss the key objectives of transfer pricing and advise on the appropriateness of making transfers based on given criteria.**

## PATHFINDER

**Candidates are advised to ensure adequate preparation and also wide coverage of the syllabus content.**

(a) Computations of the amount of repairs cost are as follows:

Therefore, the repairs cost  
= ~~₹~~(352,000 - 270,000)

(b) Using the high and low points method, the cost function can be determined thus:

The rate of variability =  $\frac{18,500}{50,000} = 0.371$

$$Y = a + bx$$
$$82,500 = a + 0.37(150,000)$$

Therefore, the cost function for the repairs cost becomes

$$Y = 27,000 + 0.37x$$

## **PATHFINDER**

- (c) The problems that may be involved in separating mixed costs into fixed and variable elements in practice are
- (i) Non-acceptability of technique by the management
  - (ii) Difficulties associated with separating costs when more than two variables are involved.
  - (iii) Some of the costs may not follow the linearity approach as they could be step costs.
  - (iv) Non-availability of competent personnel.
  - (v) Use of judgemental or Subjective classification of costs

### **EXAMINERS' REPORT**

The question tests candidates' knowledge of separating Mixed Cost into its fixed and variable elements. Part 'b' requires candidates' ability to determine the cost function on repairs while part 'c' required candidates to state the problems associated with the separation of mixed costs.

Candidates are to determine the fixed and variable costs, state the cost function and enumerate problems in separating mixed costs into its fixed and variable components.

About 80% of the candidates attempted the questions and performance was below average.

Many candidates mixed up the computations using high level of activity for the low level and vice versa. Many of them commented on the various methods of separating mixed costs instead of stating the problems involved in the separation of mixed costs. Poor presentation was also the bane of many of them.

Candidates are advised to practise extensively and ensure they update their knowledge of Management Accounting Principles. They should also not neglect the Institute's Study Pack.



# **PATHFINDER**

**THE INSTITUTE OF CHARTERED ACCOUNTANTS OF NIGERIA**

**PPROFESSIONAL EXAMINATION I – MAY 2014**

## **FINANCIAL ACCOUNTING**

**Time Allowed: 3 hours**

**SECTION A:            PART I    MULTIPLE-CHOICE QUESTIONS            (20 Marks)**

**ATTEMPT ALL QUESTIONS IN THIS SECTION**

**Write ONLY the alphabet (A, B, C, D or E) that corresponds to the correct option in each of the following questions/statements:**

1. Which of the following is an element of financial statements?
  - i.    Equity
  - ii.   Expenses
  - iii.   Liabilities
  - A.   i only
  - B.   i and ii
  - C.   i, ii and iii
  - D.   i and iii
  - E.   ii and iii
  
2. A document prepared by International Accounting Standards Board which set accepted guidelines on how financial statements are prepared together with requisite contents is known as
  - A.   Accounting standard
  - B.   Conceptual standard
  - C.   Exposure draft
  - D.   Basic going concern concept
  - E.   Conceptual framework

## PATHFINDER

3. In IFRS compliant financial statements, which of the following ratios is disclosed in the Statement of Profit or Loss and other Comprehensive Income?

- A. Quick ratio
- B. Price/Earnings ratio
- C. Debt/Equity ratio
- D. Earnings per share
- E. Dividend cover

4. The ₦16 million disclosed in the following motor vehicle account should be classified in the Statement of Cash Flows as

Motor Vehicle Account			
	₦'000		₦'000
Balance b/d	20,000	Depreciation charge	8,000
Depreciation on Disposal	2,000	Disposal	5,000
Cash/Bank	16,000		
		Balance c/d	<u>25,000</u>
	<u>38,000</u>		<u>38,000</u>

- A. Financing activity cash inflow
  - B. Investing activity cash outflow
  - C. Operating activity cash inflow
  - D. Financing activity cash outflow
  - E. Investing activity cash inflow
5. The landlord of a bankrupt tenant applied his power of distress, in respect of two year-rent of ₦480,000 owed, three months after the commencement of bankruptcy proceedings. How much of the rent owed will rank as preferential debt?
- A. ₦480,000
  - B. ₦360,000
  - C. ₦240,000
  - D. ₦120,000
  - E. ₦60,000

## PATHFINDER

6. Which of the following is **NOT** a characteristic of a finance lease?
- A. It is usually non-cancellable
  - B. The lease term covers all the useful life of the leased asset
  - C. The risks and rewards associated with ownership of the leased assets are transferred to the lessor
  - D. The lessee is responsible for the insurance, repairs and maintenance costs of the leased asset during the lease period
  - E. The assets remain with the lessee during the lease period
7. The additional commission payable to an underwriter for placing blocks of the shares offered by its clients is known as
- A. Overriding commission
  - B. Underriding commission
  - C. Underwriting commission
  - D. Extra underwriting commission
  - E. Additional underwriting commission
8. The following statements are true of biological assets **EXCEPT**
- A. They are living animals and plants
  - B. They are measured at market value including costs of sales
  - C. They can be transformed by a process of management i.e. agricultural activity
  - D. Owners of biological assets may enter into contracts to sell forward the assets or related products
  - E. Determining whether an asset is a biological asset or inventory sometimes depends on the purpose for which the asset is held
9. Which of the following statements is **TRUE** of an Ex-Div loan notes purchase transaction?
- A. The price includes the right of the buyer to receive the immediate next instalment or interest
  - B. The price includes the right of the buyer to receive the immediate past instalment of interest
  - C. The price includes the right of the seller to receive the immediate next instalment of interest

## PATHFINDER

- Use the following information to answer questions 12 and 13.**

	N'Million	N'Million
Profit before taxation	28,650	
Tax expense for the year	<u>(8,590)</u>	
Profit for the year		20,060
Gross premium for the year		102,200
Contingency reserves balance - 1/5/2013		29,605
Issued share capital		31,500

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- PROFESSIONAL EXAMINATION I - MAY 2014

## PATHFINDER

13. Calculate the contingency reserves balance which will appear in the Statement of Financial Position as at 30 April 2014
- A. ~~£~~39,825million
  - B. ~~£~~32,469million
  - C. ~~£~~31,611million
  - D. ~~£~~31,500million
  - E. ~~£~~30,626million

Use the following information to answer questions 14 and 15.

Big Plc acquired 70% and 30% interest in the issued equity of Small Ltd and Tiny Ltd respectively few years ago. Small Ltd had earlier acquired 60% interest in the net assets of Tiny Ltd. During the year ended 31 December 2013, Big Plc sold goods worth ~~£~~840,000 to Small Ltd. The goods were invoiced at cost plus 25% mark-up and a quarter is yet to be sold by Small Ltd by the year end. (Assume control and/or significant influence apply in all cases)

14. In relation to Big Plc group, Tiny Ltd is a/an
- A. Subsidiary
  - B. Associate
  - C. Parent
  - D. Sub-subsidiary
  - E. Mixed Associate
15. Calculate the amount of unrealised profit in inventories to be adjusted for, in the consolidated accounts
- A. ~~£~~210,000
  - B. ~~£~~168,000
  - C. ~~£~~157,500
  - D. ~~£~~52,500
  - E. ~~£~~42,000

## PATHFINDER

- Use the following information to answer questions 17 and 18:**

Parent Plc acquired 150 million shares in Subsidiary Ltd one year ago, which gave Parent Plc control over Subsidiary Ltd. At the date of acquisition, the retained earnings of Subsidiary Limited was ₦60 million and the value of the non-controlling interest in Subsidiary Ltd was ₦65 million.

- 
- PROFESSIONAL EXAMINATION I - MAY 2014**

## PATHFINDER

18. Calculate the Group's Retained Earnings at the end of the year

- A. ₦350 million
- B. ₦280 million
- C. ₦250 million
- D. ₦100 million
- E. ₦96 million

Use the following information to answer questions 19 and 20:

ABC Plc owns 70% of XYZ Plc, a subsidiary and sends goods to XYZ Plc valued at ₦1,044,000 at a mark-up of 20%. 40% of these goods were sold by XYZ Plc to external parties at the end of the year.

19. Calculate the value of the goods sent by ABC Plc to XYZ Plc.

- A. ₦1,253,000
- B. ₦1,044,000
- C. ₦870,000
- D. ₦625,000
- E. ₦418,000

20. Calculate the unrealised profit for the transaction.

- A. ₦835,200
- B. ₦626,400
- C. ₦417,600
- D. ₦104,400
- E. ₦69,600

SECTION A: PART II      SHORT-ANSWER QUESTIONS      (20 Marks)

ATTEMPT ALL QUESTIONS IN THIS SECTION

Write the answer that best completes each of the following questions/statements:

1. TWO of the qualitative characteristics that make the information provided in the financial statements useful to the users include.....and.....

## PATHFINDER

Use the following information to answer questions 2 and 3:

Smart Plc acquired 85% of the 9 million ordinary shares of ₦1.00 each of Dull Plc on 31 March 2013 at a cost of ₦10.8 million. Dull Plc paid a dividend of 10% from a profit of ₦6 million for the year ended 30 September 2013.

2. The effective cost of investment in Dull Plc. is.....
3. The journal entry of dividend received by Smart Plc (without narration) is.....
4. **TWO** of the “one-off costs” associated with the development of a computerised accounting system include.....and.....
5. **TWO** of the requirements an asset must satisfy to be classified as a current asset as stipulated in IAS 1 (Presentation of Financial Statements) include.....and.....
6. The debit balance in a voyage account at the end of the accounting period represents .....
7. A trust created for the benefit of society in general or a large section of it is known as .....
8. IFRS 9 (Financial Instruments), when fully developed will replace International Accounting Standard (IAS) .....
9. The Revenue of a company for a year amounted to ₦400 million. This includes revenue from goods sold on sale or return basis amounting to ₦150 million of which a quarter of the goods return to date will expire after the end of the accounting year. Calculate the amount of revenue which will appear in statement of profit or loss for the year.
10. Banjo Nigeria Limited from 1 January 2013 commenced substantial occupation of the lettable space in its investment property located at Ikeja, Lagos. At year end the property should be reclassified in the statement of financial position as.....



## PATHFINDER

- |  |              |
|--|--------------|
|  | <b>£'000</b> |
| Cost of protecting assets                  | 350          |
| Salaries of official receiver              | 140          |
| PAYE deductions 15 months to 31 March 2014 | <u>800</u>   |
|  | <b>1,290</b> |

12. The following information relates to an insurance company operating in Nigeria.

The margin of solvency is.....

- |                                 | <b>N/M</b> |
|---------------------------------|------------|
| Issue of shares                 | 600        |
| Proceeds from sale of equipment | 730        |
| Interest received               | 260        |
| Taxes paid                      | 180        |

14. An entity with current market value of ₦5 per share has the following information.

The Earnings Yield of the entity will be.....

- 
- PROFESSIONAL EXAMINATION I - MAY 2014

## PATHFINDER

**Use the following information to answer questions 16 and 17:**

Below is the extract from the Statements of Profit or Loss of the underlisted companies.

	Road Plc	Street Ltd	Lane Ltd
	₦'000	₦'000	₦'000
Profit before taxation	960,500	544,600	490,990
Taxation	<u>(288,150)</u>	<u>(163,380)</u>	<u>(147,297)</u>
Profit for the year	672,350	381,220	343,693
Dividend paid	<u>(200,000)</u>	<u>(142,000)</u>	<u>(108,000)</u>
	472,350	239,220	235,693

Road Plc have 75% and 30% interests in the issued equity shares of Street Ltd and Lane Ltd respectively.(Assume control and/or significant influence applies in all cases)

16. The consolidated profit before tax will be.....
17. Non-controlling interest for consolidation purpose will be.....
18. A company indirectly controlled by a parent through its subsidiary is called .....
19. The **TWO** types (classes) of application software are.....and.....
20. State any **TWO** ways of ensuring data security in a computer network environment.

**SECTION B: ATTEMPT QUESTION 1 AND ANY OTHER THREE QUESTIONS**

**(60 Marks)**

## QUESTION 1

**DONGARI GROUP**

Dongari Plc is an enterprise which trades in importation of rice in Nigeria. The company is encountering difficulties in importing rice because of the Federal Government ban on rice importation.

In order to improve the earnings of the company, the Board of Directors decided to:

- (i) Expand the business to include agricultural products, plantation and live stock.

## PATHFINDER

- (ii) Acquire a company which is engaged in agricultural activities.

The company's Financial Controller was directed to implement the board's decision. As a result of this, Dongari Plc acquired 70% of the ordinary shares of Kanga Plc, an agricultural based company for ₦600 million on 1 January 2012, when the reserves of Kanga Plc were ₦300 million. At the date of acquisition the fair value of the non-controlling interest in Kanga Plc was ₦160 million.

The fair values of the net assets of Kanga Plc is the same as their carrying values with the exception of an agricultural land. This land was in the account of Kanga Plc at its cost of ₦300 million. It was estimated at a fair value of ₦360 million.

**Statement of Financial Position of Dongari Plc and Kanga Plc as at 31 December 2013**

	Dongari Plc ₦'000	Kanga Plc ₦'000
Assets		
<b><u>Non-current Assets:</u></b>		
Property, plant and equipment	600,000	450,000
Investments	800,000	-
<b><u>Current assets:</u></b>		
	160,000	150,000
Inventories		
Trade & other receivables	120,000	280,000
Cash and cash equivalent	<u>20,000</u>	<u>50,000</u>
Total assets	<u>1,700,000</u>	<u>930,000</u>
<b><u>Equity and Liabilities:</u></b>		
Ordinary share capital	160,000	120,000
Share premium	40,000	20,000
Reserves	590,000	500,000
<b><u>Non-current Liabilities:</u></b>		
Loan notes	600,000	170,000
<b><u>Current Liabilities</u></b>		
Trade & other payables	<u>310,000</u>	<u>120,000</u>
Total equity & liabilities	<u>1,700,000</u>	<u>930,000</u>

## PATHFINDER

### Additional information:

Immediately after acquisition, the following agricultural products were procured and included in property, plant and equipment and inventories of Kanga Plc as at 31 December 2013:

(i)	Included in property, plant and equipment of Kanga Plc are:	<b>₦'000</b>
	Dairy livestock – immature	40,000
	Dairy livestock – mature	50,000
(ii)	Included in inventories of Kanga Plc is:	
	Cotton plants	20,000

### **You are required to:**

- Prepare the Consolidated Statement of Financial Position for Dongari Plc group as at 31 December 2013 as expected for an agricultural business.  
(12 Marks)
  - State how to measure agricultural products harvested by an entity in line with the requirements of IAS 41 on Agriculture.  
(3 Marks)
- (Total 15 Marks)**

### **QUESTION 2**

The IFRS are generally accepted as accounting standards in the preparation of a general purpose financial statements in many countries of the world.

### **You are required to:**

- Briefly explain the meaning of a general purpose financial statements in accordance with IAS 1 (Presentation of Financial Statements) (2 Marks)
  - Itemise and explain briefly any **FOUR** possible reasons for the prevalence of IFRS in many countries of the world. (8 Marks)
  - Outline any **FIVE** areas of relevance of conceptual framework for financial reporting. (5 Marks)
- (Total 15 Marks)**

# PATHFINDER

## QUESTION 3

Ikotun-Egbe Nigeria Limited decided on 31 December 2013 to place the company into Voluntary Liquidation as a members' voluntary winding-up. The following was the trial balance of the company as at that date:

	N'000	N'000
Ordinary shares of ₦1 each fully paid		400,000
10% cumulative preference shares of ₦1 each fully paid		180,000
Calls in Arrears/Advance	20,000	14,000
Plant and machinery	368,500	
Leasehold properties	242,600	
Investments	75,000	
Inventory and W.I.P	152,340	
Bank overdraft		90,000
Accounts receivables/payables	68,000	141,890
Preference dividend half year to 30/6/2013	9,000	
Trading loss for the year	86,420	
Retained earnings		48,650
Cash in hand	2,680	
8% Loan notes (secured on leasehold)		150,000
	<u>1,024,540</u>	<u>1,024,540</u>
		<u>40</u>

### Additional Information:

	N'000
(i) The Accounts payable consists of:	
Income tax assessment (2012: ₦14,800; 2013: ₦19,400)	34,200
PAYE tax deductions (2012: ₦13,600; 2013: ₦7,700)	21,300
NSITF contribution (28 months)	10,590
Loan for payment of salary	22,000
Local rates (20 months)	8,000
Sundry trade payables	45,800
	<u>141,890</u>

The sundry trade payables accepted a dividend of 90 kobo in naira in full settlement.

- (ii) The Loan notes interest was one year in arrears.
- (iii) The estimated cost and expenses of the liquidation are legal ₦15,500,000 and liquidator's fee ₦9,650,000.

## PATHFINDER

- (iv) The company's assets were estimated to be realised as follows:

	₦'000
Plant and machinery	332,400
Leasehold properties	202,620
Investments	62,900
Inventories and W.I.P	136,200
Accounts receivables	54,350
Calls in arrears	13,900

- (v) The preference capital, plus arrears of dividend to the date of winding-up is stated by the company's regulations to rank pari-passu in the event of liquidation with the ordinary capital.

**You are required to:**

Prepare the Statement of Affairs and Deficiency Account as at 31 December 2013.  
Show calculations to the nearest naira. **(15 Marks)**

### QUESTION 4

'A' Plc is considering acquiring a machine. It has two options; cash purchase at a cost of ₦11,420,000 or a lease.

The terms of the lease are as follows:

- (i) The lease period is for four years from 1 January 2013 with an annual rental of ₦4,000,000 payable on 31 December each year.
- (ii) The lessee is required to pay all repairs, maintenance and other incidental costs.
- (iii) The interest rate implicit in the lease is 15% p.a.

**Note:** Estimated useful economic life span of the machine is four years.

**You are required to:**

- a. State the type of lease arrangement in the above transaction, giving reason(s) **(2 Marks)**
- b. Prepare a schedule of the allocation of the finance charges in the books of 'A' Plc for the entire lease period. **(8 Marks)**
- c. Prepare an extract of the Statement of Financial Position of 'A' Plc for the year ended 31 December 2013. **(5 Marks)**

**(Total 15 Marks)**

### QUESTION 5

	Patrol Plc	Secure Plc
	N'000	N'000
Revenue	200,000	160,000
Cost of sales	<u>(98,000)</u>	<u>(85,000)</u>
Gross profit	102,000	75,000
Administrative expenses	<u>(25,000)</u>	<u>(18,000)</u>
	77,000	57,000
Finance costs	<u>(10,500)</u>	<u>(4,500)</u>
Operating Profit	66,500	52,500
Income tax expense	<u>(20,500)</u>	<u>(16,500)</u>
Profit for the year	46,000	36,000

- (i) Patrol Plc acquired 80% of the ordinary shares in Secure Plc on 1 January 2010.
- (ii) Patrol Plc declared ₦20 million as dividend on ordinary shares while Secure Plc declared ₦16 million.
- (iii) Land, which is non-depreciable is included in the trial balance at a value of ₦38 million. At 31 December 2013, it was re-valued to ₦50 million and this revaluation is to be included in the financial statements.

a. Calculate the following ratios for Patrol Plc and Secure Plc for the year ended 31 December 2013:

- (i) Dividend cover
- (ii) Interest cover
- (iii) Gross profit margin
- (iv) Operating profit margin

(7 Marks)

b. Prepare a consolidated Statement of Profit or Loss and other Comprehensive Income for the year ended 31 December 2013.

(8 Marks)

**(Total 15 Marks)**

# PATHFINDER

## QUESTION 6

The following are the abridged annual financial statements of BUTANE Nigeria Limited.

### Statement of Comprehensive Income for the year end 31 March 2014

	N'000
Revenue	1,275,000
Cost of sales	(956,250)
Gross profit	18,750
Administrative expenses	(42,150)
Operating expenses	(110,400)
	166,200
Finance cost	(23,700)
Operating profit	142,500
Income tax expense	(66,000)
Profit for the year	<u>76,500</u>

### Statement of Changes in Equity for the year ended 31 March 2014

	Share capital N'000	Revaluation reserve N'000	Accumulated profit N'000	Total N'000
Balance b/forward	180,000	-	181,500	361,500
Revaluation of building	-	30,000		30,000
Profit for the year	-	-	76,500	76,500
Dividend paid	-	-	(37,500)	(37,500)
	<u>180,000</u>	<u>30,000</u>	<u>220,500</u>	<u>430,500</u>

### Statement of Financial Position As at 31 March 2014

	2014 N'000	2013 N'000
<b>Non-Current Assets:</b>		
Property plant & equipment – Office building	375,000	330,000
- Plant & machinery	52,500	30,000
- Motor vehicle	9,000	6,000
Long term loans to directors	<u>96,000</u>	<u>90,000</u>
	<u>532,500</u>	<u>456,000</u>
<b>Current Assets:</b>		
Inventories	123,000	63,000
Receivables	94,500	64,500
Prepaid – expenses	31,500	24,000
Bank	<u>30,000</u>	<u>9,000</u>
	<u>279,000</u>	<u>160,500</u>



## PATHFINDER

<b>Total assets</b>	<b><u>811,500</u></b>	<b><u>616,500</u></b>
<b><u>Equity &amp; Liabilities</u></b>		
Share capital	180,000	180,000
Revaluation reserve	30,000	-
Accumulated profits	<u>220,500</u>	<u>181,500</u>
	<u>430,500</u>	<u>361,500</u>
<b><u>Non-current Liability</u></b>		
Borrowings	148,500	187,500
<b><u>Current Liabilities</u></b>		
Trade payables	108,000	52,500
Bank overdraft	64,500	-
Taxation due	<u>60,000</u>	<u>15,000</u>
	<u>232,500</u>	<u>67,500</u>
<b>Total equity &amp; liabilities</b>	<b><u>811,500</u></b>	<b><u>616,500</u></b>

**Additional information:**

- (i) The following depreciation charges were included in operating expenses:
- Plant & machinery ~~N~~37,500,000
  - Motor vehicles ~~N~~ 3,000,000
- (ii) Fully depreciated plant & machinery with an original cost of ~~N~~22,500,000 was sold for ~~N~~7,500,000 during the year, the profit is included in operating expenses.

**You are required to:**

**Prepare a Statement of Cash Flows for the year ended 31 March 2014, using the Direct Method. (Total 15 Marks)**

# PATHFINDER

## SOLUTIONS TO SECTION A

### PART 1 MULTIPLE-CHOICE QUESTIONS

1. C
2. E
3. D
4. B
5. D
6. C
7. A
8. B
9. C
10. B
11. C
12. C
13. D
14. A
15. E
16. C
17. C
18. B
19. C
20. D

### TUTORIALS

$$\text{Q5. 6 Months rents} = \frac{6}{24} \times \frac{\text{N}480,000}{1} = \underline{\underline{\text{N}120,000}}$$

$$\text{Q12. (i) 10\% of profit for the year} = \frac{10}{100} \times \text{N}20,060 = \underline{\underline{\text{N}2,006\text{m}}}$$

## PATHFINDER

$$(ii) \quad 1\% \text{ of gross premium} = \frac{1}{100} \times \frac{102,200}{1} = \text{R}1,022\text{m}$$

(iii) Issued capital less contingency balance = ₦1,895m

The answer is ₦1,895 million

Q13.  $\text{N}29,605\text{m} + (\text{N}31,500 - \text{N}29,605) = \underline{\text{N}31,500 \text{ million}}$

**Q14. Subsidiary = 70% of 60% + 30% = 72% interest**

Q15.  $\frac{25}{125}x \frac{840,000}{1}x \frac{1}{4} = \underline{\underline{\text{N}42,000}}$

**Q17. Net Asset of subsidiary at acquisition**

	N'm
Share capital	200
Retained earnings	<u>60</u>
	<u>260</u>

## PATHFINDER

	N'm
Parent retained earnings	250
Plus post acquisition profit	
In subsidiary	
( <del>N100m</del> – <del>N60m</del> ) x 75%	<u>30</u>
	<u>280</u>

**Q19.**  $\frac{100}{120} \times \frac{1,044,000}{1} = \underline{\underline{\text{N}870,000}}$

**Q20. Unrealised Profit =  $\frac{20}{120} \times \text{N}1,044,000 \times 60\% = \text{N}104,400$**

## EXAMINERS' REPORT

**The questions cover all aspects of the syllabus.**

All the candidates attempted the questions and their performance was below average.

**Candidates are advised to cover all aspects of the syllabus, while preparing for the Institute's examinations.**

## PART II SHORT-ANSWER QUESTIONS

1. Understandability  
Reliability  
Comparability  
Relevance  
Faithful representation

2. ~~₹~~**₹**10.545 million

	Dr	Cr
3. Cash	510,000	
Cost of investment		255,000
Profit or loss		255,000

4.
  - (i) Hardware cost
  - (ii) Networking cost
  - (iii) Software/system cost
  - (iv) Software/system Dev. cost
  - (v) Redundancy cost

- (iii) Installation cost

## PATHFINDER

- 
- PROFESSIONAL EXAMINATION I - MAY 2014

# PATHFINDER

## TUTORIALS

- N'M**
- Q2. Cost of investment 10.8  
 Less:  
 Dividend paid  
 from pre-acquisition profit  
 $(10\% \times 85\% \times 6 \times \frac{6}{12})$  0.255  
10.545
- Q11.  $\text{N}350,000 + \text{N}140,000 + (\frac{12}{15} \times \text{N}800,000) = \underline{\text{N}1,130,000}$
- Q12.  $\text{N}420\text{m} - \text{N}280\text{m} = \underline{\text{N}140\text{million}}$
- Q13.  $\text{N}730\text{million} + \text{N}260\text{million} = \underline{\text{N}990\text{million}}$
- Q14.  $\frac{EPS}{MV} = \frac{2}{5} \times 100 = 40\%$   
 No of shares =  $\frac{750}{1.25} = 600$   
 EPS =  $\frac{1,200}{600} = 2$
- Q16.  $(\text{N}960,500 + \text{N}544,600 + 30\% \times 490,900) = \underline{\text{N}1,652,397,000}$
17.  $25\% \times 381,220,000 = \underline{\text{N}95,305,000}$

## EXAMINERS' REPORT

The questions cover all areas of the syllabus. They test the candidates' knowledge of the fundamental areas of the syllabus.

The performance was below average as most candidates could not answer questions that involve basic knowledge of IFRS (International Financial Reporting Standards).

Candidates are advised to be conversant with basic requirements of IFRS.

# PATHFINDER

## SECTION B

### QUESTION 1

(a)

Dongari Plc

Consolidated Statement of Financial Position as at 31 December, 2013

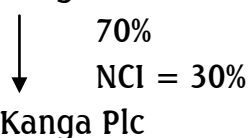
<u>Non Current Assets</u>	<u>₦'000</u>	<u>₦'000</u>
Biological Assets - Dairy livestock: Immature	40,000	
- Dairy livestock: mature	50,000	
- Plantation	<u>20,000</u>	110,000
Property, Plant & Equipment		
(600,000 + 450,000 + 60,000 – 40,000 – 50,000)		1,020,000
Investments (800,000 – 600,000)		200,000
Goodwill (Wk 4)		<u>260,000</u>
		1,590,000
<u>Current Assets</u>		
Inventories (160,000 + 150,000 – 20,000)	290,000	
Trade Receivables (120,000 + 280,000)	400,000	
Cash & Cash Equivalents (20,000 + 50,000)	<u>70,000</u>	<u>760,000</u>
		<u>2,350,000</u>
<u>Equity and Liabilities</u>		
<u>Equity</u>		
Ordinary Shares Capital		160,000
Share Premium		40,000
Group Reserves (W 6)		<u>730,000</u>
Parent Equity		930,000
Non Controlling Interests (W 5)		<u>220,000</u>
Total Equity		1,150,000
<u>Non-current Liabilities</u>		
Loan Notes (600,000 + 170,000)	770,000	
<u>Current liabilities</u>		
Trade Payables (310,000 + 120,000)	<u>430,000</u>	<u>1,200,000</u>
Total Equity and Liabilities		<u>2,350,000</u>

# PATHFINDER

## Workings (W)

### 1. Group Structure

Dongari Plc



### 2.

<u>Workings 'A'</u>			
	N'000	N'000	N'000
<b>Consolidation Schedule</b>			
Detail	COC (70%)	Nci (30%)	Con. Reserves
Ord. Share Capital 120,000	120,000	_____	
Share Premium 20,000	20,000	_____	
Pre acq. Reserve 300,000	300,000	_____	
Post acq. Reserve 200,000	_____	60,000	140,000
Fair adjustment	<u>60,000</u>	_____	_____
Net Assets Acquired	500,000		
Cost	<u>(600,00)</u>		
Fair value of Non Controlling Interest	<u>(160,000)</u>	160,000	
Goodwill	<u>260,000</u>		
Non-Controlling Interest (NCI)		<u>220,000</u>	
Dongari reserves			<u>590,000</u>
Group reserves			<u>730,000</u>

## ALTERNATIVE WORKINGS 'B'

### 3. Net assets of Kanga Plc

	Acquisition Date	Reporting Date	Post acquisition
	N'000	N'000	N'000
Ordinary shares	120,000	120,000	-
Share premium	20,000	20,000	-
Reserves	300,000	500,000	200,000
Fair Value Adj. – Land	<u>60,000</u>	<u>60,000</u>	_____
Fair Value of Net Assets	<u>500,000</u>	<u>700,000</u>	<u>200,000</u>



## PATHFINDER

4. **Goodwill in Kanga Plc**

	N'000
Purchase consideration	600,000
Fair value of NCI at Acquisition	<u>160,000</u>
	760,000
Fair value of Net assets at acquired	<u>(500,000)</u>
Goodwill	<u>260,000</u>

5. **NCI at reporting date**

	N'000
Fair value of NCI at Acquisition	160,000
Share of post acquisition reserves (30% x N200,000)	<u>60,000</u>
	<u>220,000</u>

6. **Group Reserves**

	N'000
Dongari Plc	590,000
Share of post acquisition (70% x N200,000)	<u>140,000</u>
	<u>730,000</u>

- (b) Measurement of harvested agricultural products. Agricultural products harvested from an entity's biological assets shall be measured at its fair value less costs to sell at the point of harvest. Such measurement is the cost at that date when applying it as inventories or another applicable standard.

### EXAMINERS' REPORT

The question tests the ability of the candidates to prepare consolidated financial statements of a group engaged in agricultural activities.

Candidates are required to prepare a consolidated statement of financial position which involves classification and measurement of agricultural products. They are also required to apply their knowledge of IAS 41 on Agriculture.

## PATHFINDER

The question is compulsory and about 95% of the candidates attempted it and their performance was below average. Candidates' commonest pitfall was their inability to classify and present the agricultural products properly in the Statements of Financial Position.

Candidates are advised to study the requirements of IAS 41 on Agriculture and to always prepare adequately for ICAN examinations.

### QUESTION 2

- (a) A general purpose financial statement is a statement that is intended to meet the need of users who are not in a position to demand information that are tailored to their needs. Such information is useful to existing and potential investors.
- (b) **REASONS FOR THE PREVALENCE OF IFRS IN MANY COUNTRIES**
- (i) **Production of High quality financial statements**  
It involves the preparation of financial statements that have qualitative features, that is, faithful representation, error free, neutrality, understandability etc.
  - (ii) **Preparation of User-friendly financial statements**  
Production of financial statements that contains necessary information that will assist users of financial statements to make crucial economic decisions.
  - (iii) **Uniformity of financial statements prepared**  
Financial accounting is a language of business. This language must not be different across countries of the world for it to assist international investors.
  - (iv) **Access to international finances**  
With a General Purpose Financial Statements, it would be easier for multi-national entities to have more access to international funds.
  - (v) **Enhancement of major economic decisions**  
High quality financial statements will assist users of the statements to make informed and important financial decisions.

## **PATHFINDER**

(vi) **Comparability of financial statements**

A general purpose financial statements enhance a better comparability of financial information among similar industries.

(vii) **Globalisation and integration**

With IFRS, Chartered Accountants become more mobile, since the standards are the same across the countries.

(viii) **Job Creation**

Jobs are created across countries and a Chartered Accountant in Nigeria can practice in other countries with convenience.

(ix) **Others**

- ❖ Saving of time and money
- ❖ Promotion of Regional trade
- ❖ Easier accounting and auditing practices

**(c) AREAS OF RELEVANCE OF CONCEPTUAL FRAMEWORK FOR FINANCIAL REPORTING**

- (i) Assists accounting standards and General Accepted practice to develop
- (ii) Create a situation where accounting standards are developed piecemeal in response to specific problems or abuses.
- (iii) Provides solutions to certain critical accounting issues e.g. what is an asset.
- (iv) Assists preparers and auditors to deal with complex situations that are not the subject of accounting standards
- (v) Strengthens the credibility of financial reporting and the accounting profession
- (vi) Makes it difficult for the process of setting standards to be manipulated
- (vii) Facilitates the review of the existing accounting standards
- (viii) Assists countries in setting their local GAAP
- (ix) Help users to comprehend information that are contained in the financial statements
- (x) Assists the standard setting processes of the IASB

## PATHFINDER

- (xi) Promotes harmonization and convergence of accounting standards
- (xii) Enables auditors to form reliable opinion on financial statements
- (xiii) Educate the public on the due process followed by the standard setters in developing accounting standards.

## EXAMINERS' REPORT

The question tests candidates' knowledge of the requirements of International Financial Reporting Standards (IFRS) with special focus on the Presentation of Financial Statements (IAS 1) and the use of Conceptual Framework issued by IASB. Candidates are required to explain the meaning of general purpose financial statements, proffer some possible reasons for the prevalence of IFRS in many countries of the world and to outline some areas of relevance of the conceptual framework on financial reporting.

**A good number of the candidates attempted the question, but their performance was below average. Candidates' commonest pitfall was lack of in-depth knowledge of the conceptual framework, IAS 1 and poor communication skill.**

**Candidates are advised to prepare adequately for the examinations in future.**

### QUESTION 3

**Ikotun-Egbe Nigeria Limited**  
**Statement of Affairs as at 31 December, 2013**

		Estimated to realise
	N'000	N'000
<b><u>Assets:</u></b>		
Plant and machinery		332,400
Leasehold properties		202,620
Investments		62,900
Inventories and W.I.P		136,200
Accounts receivables		54,350
Calls in arrears		13,900
Cash in hand		<u>2,680</u>
		805,050
<b><u>Liabilities</u></b>		
Secured payables – 8% Loan Note Principal	150,000	
Accrued interest	12,000	

## PATHFINDER

Liquidation cost and expenses - Legal cost	15,500	
Liquidator's fee	9,650	
Preferential payables	70,390	
Unsecured – Accounts payables	66,920	
Bank overdraft	<u>90,000</u>	<u>(414,460)</u>
Estimated surplus assets after full settlement of debts		390,590
<b>Contributors:</b>		
10% cumulative preference shares	180,000	
Accrued preference dividend	9,000	
Ordinary shares	400,000	
Calls in advance	<u>14,000</u>	<u>(603,000)</u>
Deficiency		<u>212,410</u>

### Deficiency Account

Items increasing deficiency	₦'000	₦'000
Trading loss for the year		86,420
Losses written off assets:		
Plant and machinery	36,100	
Leasehold properties	39,980	
Investments	12,100	
Inventories and W.I.P	16,140	
Accounts receivables	13,650	
Calls in arrears	<u>6,100</u>	124,070
<b>Other costs and expenses:</b>		
Interest on loan notes	12,000	
Legal cost	15,500	
Liquidator's fee	9,650	
Preference dividend	<u>18,000</u>	<u>55,150</u>
		265,640
<b>Items reducing deficiency:</b>		
Retained earnings	48,650	
Discount received	<u>4,580</u>	<u>(53,230)</u>
Deficiency per statement of affairs		<u>212,410</u>
Wk 1: Analysis of accounts payables:	Preferential	Unsecured
	₦'000	₦'000
Income tax assessment	19,400	14,800
PAYE tax deductions	13,600	7,700
NSITF contribution	10,590	-
Loan for payment of salary	22,000	-
Local rates	4,800	3,200

## PATHFINDER

Sundry trade payables (N45,800 x 0.9)		41,220
	70,390	66,920

Wk 2 Interest on loan notes = 8% of N150,000,000 = N12,000,000

Wk 3 Discount received = N45,800,000 x 0.1 = N4,580,000

### EXAMINERS' REPORT

The question tests the candidates' knowledge of preparation of Liquidation Account. Candidates' are expected to prepare Statement of Affairs and Deficiency Account.

Most candidates attempted this question but few candidates performed well. The commonest pitfall were their inability to determine what constitutes the preferential charges and preparation of the deficiency report.

Candidates are advised to pay attention to the salient areas of every aspect of the syllabus.

### QUESTION 4

(a) **Type of Lease:** It is a finance lease due to the following reasons:

- (i) The lease period is for 4 years which is the economic life of the assets
- (ii) The lessee is responsible for repairs and maintenance of the leased assets, which implies that the risks and rewards of ownership rests with the lessee.
- (iii) The present value of the future rentals of N4m at the end of each year for 4 years is equal to the cash price.

(b)

A	B	C	D	E
Period	Opening Balance	Fin. Charge at 15% of B	Rentals	Closing Balance (B – (D - C))
	N'000	N'000	N'000	N'000
2013	11,420	1,713	4,000	9,133
2014	9,133	1,370	4,000	6,503
2015	6,503	975	4,000	3,478
2016	3,478	<u>522</u>	<u>4,000</u>	
		<u>4,580</u>	<u>16,000</u>	

## PATHFINDER

(c)

**Statement of Financial Position (Extract) as at 31 December 2013**

	₦'000
Non-Current assets (₦11,420,000 – ₦2,855,00)	8,565
Non-Current Liabilities (Obligation under finance lease)	6,502
Current Liabilities Obligation under finance lease (₦9,133,000 – ₦6,503,000)	2,630

**Note:** Annual Depreciation

$$= \frac{11,420,000}{4}$$
$$= \text{N}2,855,000$$

## EXAMINERS' REPORT

The question tests candidates' understanding of accounting for lease transactions. Candidates are expected to know how to calculate lease finance charges, identifying types of lease and the treatment of lease charges in the statement of financial position.

Majority of the candidates attempted the question and showed some level of understanding. Performance was average. The commonest pitfalls were the inability of the candidates to calculate the allocation of annual finance charges and making of entries required in the statement of financial position.

**Candidates are advised to pay more attention to treatment of Finance Leases in future examinations.**

# PATHFINDER

## QUESTION 5

### (a) RATIOS OF PATROL PLC AND SECURE PLC

		Patrol Plc ₦'m	Secure Plc ₦'m
i.	<b>Dividend cover</b> $= \frac{\text{Profit for the year}}{\text{Ordinary share dividend}} =$	$\frac{46\text{m}}{20\text{m}}$  2.3 times	$\frac{36\text{m}}{16\text{m}}$  2.25 times
ii.	<b>Interest cover</b> $= \frac{\text{Operating profit}}{\text{Finance cost}} =$	$\frac{77\text{m}}{10.5\text{m}}$  7.33 times	$\frac{57\text{m}}{4.5\text{m}}$  12.67 times
iii.	<b>Gross profit margin</b> $\frac{\text{Gross profit}}{\text{Revenue}} \times 100\% =$	$\frac{102\text{m}}{200\text{m}} \times 100\%$  = 51%	$\frac{75\text{m}}{160\text{m}} \times 100\%$  = 46.88%
iv.	<b>Operating profit margin</b> $\frac{\text{Operating profit}}{\text{Revenue}} \times 100\%$	$\frac{77\text{m}}{200\text{m}} \times 100\%$  = 38.5%	$\frac{57\text{m}}{160\text{m}} \times 100\%$  = 35.63%

(b)

### Patrol Group

#### Consolidated Statement of Profit or Loss & Other Comprehensive Income for the year 31 December 2013

	₦'000	₦'000
Revenue (₦200m + ₦160m)		360,000
Cost of sales (₦98m + ₦85m)		(183,000)
Gross profit		177,000
Administrative expenses (₦25m + ₦18m)		(43,000)
		134,000
Finance Cost		(15,000)
Operating profit		119,000
Taxation (₦20.5m + ₦16.5)		(37,000)
Profit for the year		82,000



## PATHFINDER

Other comprehensive income for the year		
Gain on revaluation of land		<u>12,000</u>
( <del>₦50m</del> – <del>₦38m</del> )		
Total comprehensive income for the year		<u>94,000</u>

### EXAMINERS' REPORT

The question tests the ability of the candidates to calculate accounting ratios and also prepare consolidated profit or loss and other comprehensive income.

Majority of the candidates attempted the question and the performance was average. Although most of the candidates understood the requirements of the questions, but their inability to identify correct figures led to loss of marks.

Similarly, some candidates failed to recognise that the figures in the questions were expressed in millions, but their solutions were stated in thousands. This also led to loss of marks. Other candidates abandoned the question half way and could not complete the solution, thus leading to further loss of marks.

Candidates are advised to pay more attention to the preparation of Consolidated financial statements, calculation of accounting ratios and application of such ratios for the purpose of interpretation of the financial statements.

### QUESTION 6

#### (a) BUTANE NIGERIA LIMITED

##### STATEMENT OF CASH FLOWS FOR THE YEAR ENDED 31 MARCH 2014

<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>	<b>₦'000</b>
Cash receipts from customers (W1)	1,245,000
Cash payment to suppliers & employees (W2)	(1,087,800)
Interest paid	(23,700)
Taxation paid (W3)	(21,000)
Net cash flow for operating activities	112,500
<b>CASH FLOWS FROM INVESTING ACTIVITIES</b>	
Purchase of property plant & equipment (W4)	(81,000)
Proceed; from sales of plant & machinery	7,500
Loans notes to directors	(6,000)
	(79,500)
<b>CASH FLOWS FROM FINANCING ACTIVITIES</b>	
Borrowing repayment	(39,000)

## PATHFINDER

Dividend paid	(37,500)
	(76,500)
Net decrease in cash & cash equivalent	(43,500)
Cash & cash equivalent @ beginning of the year	<u>9,000</u>
Cash & cash equivalent @ the end of the year (W5)	<u>(34,500)</u>

### WORKINGS (A)

<b>W1</b>	<b>Cash received from customers:</b>	<b>₦'000</b>
	Revenue	1,275,000
	Increase in receivables (94,500 – 64,5000)	<u>(30,000)</u>
		<u>1,245,000</u>
<b>W2</b>	<b>Cash payments to suppliers &amp; Employees</b>	<b>₦'000</b>
	Cost of sales	956,250
	Administrative expenses	42,150
	Operating expenses	110,400
	<b><u>Adj for non cash items</u></b>	
	Profit on sale of plant & machinery	7,500
	Depreciation	(40,500)
	Increase in inventories (123,000 – 63,000)	60,000
	Increase in Trade Payables (108,000 – 52,5000)	(55,500)
	Increase in prepaid expenses (31,500 – 24,000)	<u>7,500</u>
		<u>1,087,800</u>
<b>W3</b>	<b><u>Taxation Paid</u></b>	<b>₦'000</b>
	Balance b/fwd	15,000
	Charged to	66,000
	Less: Balance c/fwd	<u>(60,000)</u>
	Tax paid	<u>21,000</u>
<b>W4</b>	<b><u>PURCHASE OF PROPERTY PLANT &amp; EQUIPMENT</u></b>	
	<b>₦'000</b>	<b>₦'000</b>
	(i) Office building	
	Bal b/fwd	330,000
	Revaluation	30,000
	Less Balance c/fwd	<u>(375,000)</u>
	Acquisition	15,000
	(ii) Plant & machinery b/fwd	30,000
	Depreciation	(37,500)
	Bal c/fwd	<u>(52,500)</u>
	(iii) Vehicles	60,000
	Bal b/fwd	6,000
	Depreciation	(3,000)
	Bal c/fwd	<u>(9,000)</u>
		<u>6,000</u>

## PATHFINDER

81,000

₦'000

	Cash & cash equivalent @ the end of the year:
W5	Bank balance
	Overdraft

30,000  
(64,500)  
(34,500)

### EXAMINERS' REPORT

The question tests the preparation of Statement of Cash flows using the Direct method. Only few of the candidates attempted the question and performance was poor.

The commonest pitfalls were that majority of the candidates used indirect method for preparing the cash flow statement despite the fact that the examiner clearly indicated that the direct method should be used. Also, some candidates could not generate correctly the figures under investing & financing activities sections of the Statement of Cash Flows.

Candidates are advised to pay attention to the provisions of IAS 7 on Statement of Cash Flows for better performance on related questions in future.

# **PATHFINDER**

**THE INSTITUTE OF CHARTERED ACCOUNTANTS OF NIGERIA**

**PROFESSIONAL EXAMINATION I-MAY 2014**

**ADVANCED AUDIT AND ASSURANCE**

**Time Allowed: 3 hours**

**SECTION A: PART I      MULTIPLE-CHOICE QUESTIONS      (20 Marks)**

**ATTEMPT ALL QUESTIONS IN THIS SECTION**

**Write ONLY the alphabet (A, B, C, D or E) that corresponds to the correct option in each of the following questions/statements.**

1. As a consequence of unethical behaviour, which of the following is **NOT** a sanction usually imposed by the Institute of Chartered Accountants of Nigeria for misconduct?
  - A. Expulsion from membership
  - B. Withdrawal of practising licence
  - C. Imprisonment
  - D. Reprimand
  - E. Fine
2. The main objective of corporate governance is to ensure that
  - A. The policy of government adequately favours the business community
  - B. The directors' welfare is properly taken care of
  - C. Transparency and accountability in the management of an organisation exist
  - D. Management is aware of its responsibilities
  - E. Management complies with rules and regulations
3. External peer review of audited accounts of a public company is most likely to be performed by
  - A. Registrar-General of Corporate Affairs Commission
  - B. Audit review staff of the Securities and Exchange Commission
  - C. Employees and partners of the firm who are not associated with the audit being reviewed

## PATHFINDER

- D. Employees and partners of another audit firm
  - E. Financial Reporting Council of Nigeria
4. Audit expectation gap is understood as a vacuum created between the role of an auditor as perceived by the auditor and the expectation of the users of financial statements. Communication gap is the result of the following assumptions by the user of financial statements **EXCEPT** that
- A. Unqualified audit opinion is a clean bill of health
  - B. The auditors guarantee the continued existence of firms
  - C. Auditors issue Financial Statements after the audit exercise
  - D. Users of financial statements may expect all fraud to be discovered by the auditor
  - E. Qualified audit opinion is a report indicating that the firm will fold up
5. The audit approach to be adopted for not-for-profit organisations requires the duty of care from the auditor. Therefore, in the audit of not-for-profit organisation, an auditor must consider all relevant matters **EXCEPT**
- A. Sources of fund
  - B. Legal form of organisation
  - C. Share capital
  - D. Letter of engagement
  - E. Relationship with Government
6. Computer usage in audit fieldwork is explained in terms of its efficiency in spreadsheets and word processing. Spreadsheet software would be most useful for which of the following audit activities?
- A. Testing internal controls over computerised accounting applications
  - B. Preparing an audit program
  - C. Preparing a comparison for current year expenses with those of the
  - D. Drafting a planning memo
  - E. Exceptional report

## PATHFINDER

7. Control procedures within the computer system may leave no visible evidence indicating that the procedures were performed. In such instances, the auditor should test these computer controls by
- A. Reviewing transactions submitted for processing and comparing them to related output
  - B. Making corroborative inquiries
  - C. Observing the separation of duties of personnel in the computer department
  - D. Reviewing the run/operating manual
  - E. Observing the batch processing of data
8. The roles of the Audit Committee include the following **EXCEPT**
- A. To review the external audit process and make recommendations to the Board
  - B. To consider the annual accounts together with the attached audit report
  - C. To be involved in the appointment of the internal auditors
  - D. To list companies with market capitalisation
  - E. To ensure that there is an oversight of systems and procedures in compliance with regulations
9. A typical approach to a forensic audit assignment excludes **ONE** of the following
- A. Perform a conflict check
  - B. Perform an initial investigation
  - C. Develop an action plan
  - D. Obtain the relevant evidence
  - E. Review the directors' report
10. Your family member had been appointed as a director of your major audit client. What step will you take concerning the audit?
- A. Request the accounts department to provide a list of related parties transactions of the director
  - B. Inform your family member that you are the auditor to the company
  - C. Resign as auditor to the company
  - D. Request for joint auditor to be appointed
  - E. Inform your client and identify safeguards necessary to minimise independence threats

## PATHFINDER

11. The following factors influence risks in an organisation **EXCEPT**
- A. Likelihood of financial failure
  - B. Susceptibility of assets to misappropriation
  - C. The frequency of related party transactions
  - D. Estimate of the combined mis-statements
  - E. Effectiveness of internal controls
12. During the audit field work on Adlar Ventures Limited, the audit trainee listed some items for possible adjustment of the financial statements by the audit senior. Which of the following items should be adjusted in the financial statements?
- A. The application to Bank of Industry for loan at reduced interest rate
  - B. Management plan to diversify to other areas of operations
  - C. The liquidation of a major customer of the client
  - D. Major law suit against the company with proceedings commencing after the financial year end
  - E. Minutes of board approval to apply for government grant for the new factory
13. The procedures for Due Process Review do **NOT** include **ONE** of the following
- A. Preliminary discussion between Budget Monitoring and Price Intelligence unit and the beneficiary ministries
  - B. Preparation of draft report
  - C. Organisation of 'Right of Reply' meeting final report
  - D. Codification of final report
  - E. Granting or denying due process certificate
14. The ethical principles which govern auditors' responsibilities do **NOT** include **ONE** of the following
- A. Integrity
  - B. Professional competence
  - C. Objectivity
  - D. Independence
  - E. Experience

## PATHFINDER

15. **ONE** of the functions of Independent Corrupt Practices and Other Related Offences Commission (ICPC) is to
- A. Receive petition to probe government officials
  - B. Prosecute both foreigners and Nigerians for money embezzled offshore
  - C. Educate the public on bribery, corruption and other related offences
  - D. Enlist foreign countries to support war against indiscipline
  - E. Confiscate properties of erring individuals
16. It has been observed that the key input for all service operations is human resources. Audit firms should endeavour to provide conducive office space for their staff. Which of the following essential facilities may **NOT** be provided for various grades of professional staff?
- A. Laptops with internet connectivity for all audit seniors and above
  - B. Smart phones for all audit seniors and above
  - C. Local Area Network to aid internet connectivity
  - D. Calculators
  - E. Car loans
17. The confirmation of management's responsibility for the preparation of the financial statements is embedded in
- A. Management letter
  - B. Engagement letter
  - C. Letter of representation
  - D. Letter of confirmation
  - E. Comfort letter
18. Which of the following is **NOT** a duty or function of the Auditor-General for the Federation?
- A. Serving as Chairman for both Audit Alarm Committee and Losses Committee
  - B. Ensuring that authorised maximum cash balances in Ministries and other Departments are not exceeded
  - C. Reporting on the true and fair view of financial statements Examined



## PATHFINDER

- D. Informing the Corporate Affairs Commission of any defect in the financial statements
  - E. Ensuring that proper system of accounts as prescribed by financial regulations are maintained
19. The auditors' report should conform to the following criteria **EXCEPT**
- A. Based on factual information
  - B. Impartial approach
  - C. Clear and unambiguous language
  - D. Effective presentation
  - E. Assertion of the correctness and accuracy of the accounts
20. In accordance with Codes of Best Practices on Corporate Governance, the functions of the Board of Directors include the following, **EXCEPT**
- A. Strategic planning
  - B. Succession planning
  - C. Communication with shareholders
  - D. Ensuring the integrity of financial controls and reports
  - E. Appointment of members of the audit committee from the shareholders

**SECTION A: PART II      SHORT-ANSWER QUESTIONS      (20 Marks)**

**ATTEMPT ALL QUESTIONS IN THIS SECTION**

**Write the answer that best completes each of the following questions/statements:**

1. The state of mind that has regard to all considerations relevant to the task in hand but no other is known as .....
2. Accounting units in the ministries or extra-ministerial departments are classified into self-accounting, non-self accounting and ..... units
3. Where the financial statements of an entity do not give a true and fair view and the matter under consideration is fundamental, the auditor can give an ..... opinion.

## PATHFINDER

4. The Auditor-General of a State is appointed by the Governor of the State on the recommendation of the..... and subject to confirmation by the.....
5. The International Federation of Accountants (IFAC) stipulates that auditors' independence requires both independence of ..... and independence in .....
6. Which partner in an audit firm is responsible for audit assigned to audit staff right from the beginning to the conclusion of the assignment?
7. A process used to investigate and evaluate a merger or an acquisition opportunity emphasising due care is called .....
8. In actuarial valuation, the present value of the company's total liabilities on all the current policies are determined in respect of ..... and bonuses already declared.
9. Firms that carry out transnational audits and operate subject to national laws and professional rules in more than one country are known as .....
10. The recording of sales that never occurred creates a ..... revenue.
11. The organ established by the Institute of Chartered Accountants of Nigeria Act Cap 111 LFN 2004 for the enforcement of ethical standards is .....
12. Threats to objectivity as articulated in ICAN's Professional Code of Conduct and Guide for Members are self-interest, self-review and .....
13. Substantive tests are those designed to substantiate the validity, accuracy and ..... of amounts appearing in the financial statements and related notes.
14. What type of audit is suitable to assess how well an organisation performs in safeguarding the surroundings in which it operates?
15. The accounting basis generally accepted and used in the public sector is known as .....

## PATHFINDER

- SECTION B:            ATTEMPT QUESTION 1 AND ANY OTHER THREE QUESTIONS**  
**(60 Marks)**

## CASE STUDY

Acute Interiors Limited operates a large shop in Garki, Abuja. The company sells expensive furniture and interior decoration accessories. The normal procedure is that customers see the furniture items on the internet, show room, flyers or on television adverts and place orders either directly or online. The company makes delivery in any part of the country from one of their suppliers within three weeks.

On placing an order, the customer either pays by cash, bank transfer, point-of-sale (POS) or enters into a hire purchase agreement. Acute Interiors Limited has four sales assistants, one van driver and a cashier in the show room. The accounting and purchasing functions are done by the manager and a part-time bookkeeper who has just obtained ICAN/ATSWA certificate.

The directors of the company have other businesses and review the company's operations once-in-a-month at an all-day board meeting.

## PATHFINDER

You are required to explain:

- c. The types of internal control measures that will be appropriate for the company's sales activities. (6 Marks)
  - d. The control tests that the auditor should perform on the company sales activities. (9 Marks)
- (Total 15 Marks)

### QUESTION 2

Early warning signs during an audit process should put auditors on alert about business failure.

Required:

- a.
    - (i) Explain the difference between business failure and audit failure. (4 Marks)
    - (ii) Give **TWO** reasons for business failure. (2 Marks)
    - (iii) Give **TWO** reasons for audit failure. (2 Marks)
  - b.
    - (i) Explain the term **Receivership** and outline the steps to be taken by a Receiver/Manager to perfect his appointment. (4 Marks)
    - (ii) Explain the responsibilities and state **THREE** duties of a Receiver/Manager. (3 Marks)
- (Total 15 Marks)

### QUESTION 3

Many multinationals employ more than one auditor for the purpose of carrying out statutory audit

- a. State the advantages and disadvantages of a joint audit. (4 Marks)
- b. What are the factors that influence the division of work in a joint audit? (6 Marks)

## PATHFINDER

- c. State **FIVE** circumstances that may warrant the need for joint auditors appointment (5 Marks)  
(Total 15 Marks)

### QUESTION 4

As a renowned audit firm, you audited the accounts of one of your ailing clients for the year ended 31 December 2013 which the company submitted along with their application to obtain overdraft facility from their bankers.

Shortly after the approval of the facility by the bank, the company was unable to meet its obligation to pay.

The bank instituted an action against the company. The investigation that followed revealed the following:

- (i) That the financial statements the bank relied upon to grant the facility with respect to work-in-progress and debtors balances were overstated.
- (ii) That the financial statements were audited in a hurry within a limited time.
- (iii) That no audit verification took place prior to the expression of the audit opinion.
- (iv) That the firm had been auditors of the client company for over ten years as auditors.
- (v) That the audit firm purportedly relied on the information supplied by the directors.

#### Required:

- a. What are the auditor's liabilities as it relates to each of the findings above? (5 Marks)
- b. What audit steps should the firm have taken to authenticate the correctness of work-in-progress and debtors balances? (10 Marks)  
(Total 15 Mark)

## PATHFINDER

### QUESTION 5

Modern IT governance implies a system where all stakeholders including the board, internal customers and in particular departments such as finance, make necessary input into decision making process as against the traditional system which defers all key decisions to the company's IT Professionals only.

#### Required:

- a. Explain the framework within which IT governance should operate to achieve its goals and objectives (8 Marks)
  - b. Explain IT oversight functions in an organisation (7 Marks)
- (Total 15 Marks)

### QUESTION 6

During the global economic crisis in 2010, one of your multinational clients went ahead to list on the floor of the Nigerian Stock Exchange. The Managing Director explained to you that the main reason for listing their shares was to imbibe "Global Best Practices" and truly uphold good corporate governance. Shortly after being listed, an Audit Committee was set up in addition to the Board of Directors.

Recently, there has been rivalry between the various organs in the company to the extent that almost all decisions are taken at board meetings. There is also the issue of who should be the Chairman of the Audit Committee as the Managing Director intends to appoint a stooge to that office.

#### Required:

- a. Under what circumstances should the board exercise its powers? (3 Marks)
- b. What are the functions of the board, as specified in the Code of Best Practices on Corporate Governance? (4 Marks)
- c. List the **TWO** terms of reference of the corporate governance committee. (3 Marks)
- d. Who, according to Code of Best Practices, should be the Chairman of the audit committee? (2 Marks)

## PATHFINDER

- e. State **THREE** ways a director can be removed from office before the expiration of his tenure. (3 Marks)

(Total 15 Marks)

### SOLUTIONS TO SECTION A

#### PART I MULTIPLE-CHOICE QUESTIONS

1. C
2. C
3. D
4. C
5. C
6. C
7. A
8. D
9. E
10. C
11. D
12. C
13. D
14. E
15. C
16. B
17. C
18. D
19. E
20. E

#### EXAMINERS' REPORT

The questions cover almost all aspects of the syllabus.

All the candidates attempted the questions and performance was good.

# **PATHFINDER**

## **PART II**

## **SHORT-ANSWER QUESTIONS**

1. Objectivity
2. Sub-Accounting
3. Adverse
4. State Civil Service Commission/State House of Assembly
5. Mind/ Appearance
6. Engagement Partner
7. Due diligence
8. Sum Assured
9. International Firms
10. Fictitious
11. Accountants' Disciplinary Tribunal
12. Advocacy Threat
13. Completeness
14. Environmental Audit
15. Cash Basis
16. Not –for- profit
17. Central Bank of Nigeria
18. Deed of appointment
19. Systems Notes or Narrative Notes
20. Responsibility

## **EXAMINERS' REPORT**

The questions cover almost all aspects of the syllabus.

All the candidates attempted the questions and performance was good.



# PATHFINDER

## SOLUTIONS TO SECTION B

### QUESTION 1

(1a) Acute Interior Limited, as a large shop, should put in place the following internal control measures:

- (i) **Organisational controls:** The company should have a plan of the organisation which should define and allocate responsibilities and show clearly identified lines of reporting.
- (ii) **Segregation of duties:** No one person should be responsible for the recording and processing of a complete transaction in order to reduce the risk of errors or fraud. The company should separate the accounting and purchasing functions and ensure that different persons perform those functions independent of each other.
- (iii) **Authorisation and approvals:** All transactions should be authorised and approved by an appropriate person. Sales invoices should be checked prior to payment by customers in the case of cash sales. Approval should be given in case of hire purchase or credit sales and bank statement checked for point- of- sales (POS) transactions.
- (iv) **Arithmetic and Accounting:** These are controls designed to ensure that transactions are correctly recorded and accurately processed. The company's part-time bookkeeper may not be that competent and committed.
- (v) **Personnel:** Procedures should be designed to ensure that personnel operating in the company are competent and motivated to carry out the tasks assigned to them. The four sales assistants and part-time book-keeper are grossly inadequate and may not be competent in carrying out their assigned tasks.
- (vi) **Supervision:** There should be laid down procedures for the work of the juniors to be supervised by their superiors.
- (vii) **Management:** These are overall supervisory controls exercised by management e.g review of management accounts, budgets and variance, internal audit and so on.

## PATHFINDER

(viii) **Acknowledgement of performance:** All activities carried out must be evidenced by signature or other visible evidence of performance. There is no evidence that this company acknowledge any performance.

(1b) The control tests the auditor should perform in this circumstance are:

(i) **Receipt Books:**

- All receipts should be pre-numbered.
- The issue and custody of cash receipts should be under the control of a responsible official
- Originals of all cancelled receipts should be retained and countersigned by a responsible official.
- Unused booklets should be kept under lock and key.

(ii) **Acknowledgment:** Official receipts must be issued for every amount received.

(iii) **Remittances received:** All correspondences received must be opened by a responsible official. All remittances received must be crossed "Accounts Payee only", entered in a daily cash register and handed over to the cashier.

(iv) **Deposits:** All collections must be internally checked and deposited into the bank the next day. Pay-in-slips should be filed and checked daily. The amount should then be traced into bank statements. All outstanding collections should be thoroughly monitored

(v) **Access to ledgers:** The cashier should not be allowed any access to personal or general ledgers.

(vi) **Teeming and lading:** The following steps should be taken to avoid teeming and lading:

- The amount recorded as having been received should be checked with the corresponding amount in the statement of account received from each of the debtors.
-

## **PATHFINDER**

- Debtors should be requested to give crossed cheques marked “Accounts Payee only”
  - All remittances received in the form of cheques, drafts etc must be crossed and marked ‘Accounts Payee only’ after they have been received .
  - Periodic debtors circularisation should be carried out.
  - The pay-in-slips should be carefully checked with the accounts shown on the carbon copy of counterfoil receipts.
- (vii) Prepare print out of some months’ sales activity and carry out the following:
- Analyse sales into, internet, television advert,
  - Trace sales/ orders to payments
  - Review delivery notes against orders
  - Check that hire purchase customers are paying according to terms of agreement.
  - Carry out test count of stock during audit exercise and compare with stock records.
  - Confirm existence of goods-in-transit insurance.
  - Check flow of authorisation over sales activities

### **EXAMINERS’ REPORT**

The question tests candidates’ understanding of internal control on sales. About 95% of the candidates attempted the question, but performance was poor.

Candidates’ commonest pitfall was lack of understanding of control tests on sales activities.

Candidates are advised to cover the syllabus thoroughly and be able to apply their theoretical knowledge to practical questions.

## **PATHFINDER**

### **QUESTION 2**

- (a) (i) Business failure occurs when a business is unable to repay its lenders or meet the expectations of its investors because of economic or business conditions.
- (ii) Audit failure occurs when the auditor issues an incorrect audit opinion because he failed to comply with the requirements of auditing standards.
- (iii) Reasons for business failure include:
- Poor management decision
  - Unhealthy or unexpected competition in the industry
  - Recession
  - Lack of necessary infrastructure e.g power, road, water, etc.
  - Changes in government policies/laws
  - Lack of cooperation from technical partners
  - Loss of major clients
  - Weak/poor internal control
- (iv) Reasons for audit failure include:
- Assigning incompetent staff to perform certain audit tasks
  - Not taking due care during audit process
  - Failure to comply with relevant auditing standards
  - Lack of adequate review of working papers
  - Inappropriate audit procedure
  - Lack of strategic audit plan before commencing an audit assignment.
- (b) **Receivership**
- (i) Receivership is the process by which someone (referred to as a receiver or receiver/manager) is appointed and is vested with the legal right to receive properties belonging to a company which cannot meet its obligation on a debenture trust deed.

## **PATHFINDER**

### **Steps to perfect his appointment:**

A receiver/manager should take steps to ensure that the lender i.e the debenture holder, has complied with all relevant legal requirements. These requirements include:

- Registration of the instrument of charge within 90 days as required by Section 197 of CAMA Cap 20 LFN 2004.
- Adequate and proper final demand notice to debtor companies. Generally a 21-day final notice is required after which the appointment of the receiver or manager is justified.
- Possession of title documents to the assets charged or obtaining such documents from the debtor company.
- Avoidance of hasty appointment under a fixed charge. The appointment shall not be effected within six months of creation of the charge, while in the case of a floating charge, the period is 12 months.
- Upon appointment, the receiver /manager shall ensure that notice is given to the Corporate Affairs Commission within 14 days.
- Advertisement in national dailies should be carried out.

- (ii) The responsibility of the receiver manager is to receive properties belonging to a company which cannot meet its obligation in a debenture trust deed.

### **Duties include:**

- Running the company in a profitable manner
- Paying debts as funds are made available.
- Preparation of accounts
- Collection of his fees
- Handing over the affairs of the company back to management
- Collection of debts due to the company.

### **EXAMINERS' REPORT**

The question tests candidates' knowledge on audit and business failure on the one hand and duties and responsibility of a Receiver/Manager on the other hand.

## PATHFINDER

Almost all the candidates (about 99%) attempted the question and performance was average.

Commonest pitfall was lack of proper marshalling of points to earn marks. Candidates are advised to prepare adequately for future examinations.

### QUESTION 3

- (a) Joint audit arises when more than one firm of accountants report jointly on a client's set of financial statements. The auditors will have to work together to plan the audit, gather the evidence and review the work in order to provide opinion on the financial statements.

Advantages of joint audit include

- Availability of a wider range of resources particularly across national boundaries.
- Sharing of liabilities
- Possible efficiency improvements to the audit generally

Disadvantages include:

- Likely cultural clashes between the audit firms
- Difficulty in setting a joint approach – too many cooks can spoil the broth
- Joint liability of the auditors
- Increase in fees and expenses to the client
- Delay can occur as a result of one firm failing to meet client's reporting deadline.

- (b) Factors that influence division of work include:

- Technical competence of the auditors
- Geographical location of the firms vis- a-vis the client company
- Resources available to the audit firm

- (c) Circumstances that may require the need for joint audit include:

- Size and complexity of organization being audited
- Timing of audit report
- Boardroom politics
- Decision of parent company
- When shareholders feel that their interest will be better protected
- Retention of subsidiary auditor after merger

# PATHFINDER

## EXAMINERS' REPORT

The question tests candidates' knowledge of joint audit.

About 95% of the candidates attempted the question and performance was good.

### QUESTION 4

- (a) The auditors liabilities in relation to the findings will be as follows:
- (i) If the work in progress and debtors balances were truly overstated in the financial statements, the auditor will be liable since standard of care and caution has not been exercised by him in the performance of his duty, (See Re-West Minster Road Construction & Engineering Co. Ltd- 1939).
  - (ii) Where the financial statements were hurriedly audited, there is probability that the standard of care, caution and diligence would not have been exercised and as a result the auditor will be liable for any negligence that may likely occur. However, even though the audit was concluded in a short period, this does not mean that it would not be thorough.
  - (iii) Verification is an important audit procedure, especially in the audit of assets and liabilities of a business entity. Where this is not carried out, it will be obvious that the auditor is professionally incompetent and as a result will be liable for negligence.
  - (iv) If the client is a privately owned company, the auditor is not liable for staying this long. However, there is no law limiting the tenure of an auditor, subject to the provisions of Code of Corporate Governance relevant to the industry sector.
  - (v) Material information must be verified by auditor. He must not rely solely on director's information otherwise he will be held liable for professional negligence. However, where such information cannot be verified, he should obtain letter of representation from the management of the company.
- b. Steps to be taken to authenticate the correctness of the value of work –in-progress include:
- (i) Test the reliability of work-in-progress by examining the costing system in force.  
Ensure that:  
-

## **PATHFINDER**

- Methods of accounting and control over stores issues and labour usage are adequate
  - Method of allocation of overhead is reasonable. Confirm by calculation that the amount added is in line with the actual rate incurred during the year under review unless the factory operated below normal capacity in which case the normal activity rate should be used.
  - Method of valuation of work-in-progress is consistent with previous years and has not been distorted by changes in the level of production.
  - Physical verification of work-in-progress is carried out or followed through
- (ii) Compare the prices of the selected items of Work In Progress (WIP) with the selling price by adding estimate of the cost required to complete. The projected/actual final cost should be compared with selling price and anticipated losses provided for.
- (iii) For long term contracts, determine whether the basis for the calculation of WIP is permissible and in accordance with the relevant accounting standard.
- (iv) Obtain or prepare a schedule summarizing the stock and WIP by general category, showing the comparative figures for the previous year. Reconcile the total with the amount shown in the balance sheet and with the final stock sheets.
- State on the schedule the basis of valuation used and the nature of the evidence obtained to verify the quantity of stock.
  - State on the schedule of stock and work in progress the amount and proportion of value which were subject to observation at a stock count and other audit tests.



## **PATHFINDER**

- (v) Compare the ratios of stock and WIP to sales, raw material to cost of sales, WIP to cost of sales, and finished goods to cost of sales with those for the previous period. Prepare a schedule stating reasons for significant changes in the above ratios and evidence obtained to verify the explanations given.
- (vi) Review the stock valuation on a current cost basis. If materially different, discuss possible disclosure with the directors.

### **Steps to be taken to authenticate the correctness of the value of Debtors**

- (i) Examine sample of ledger accounts and all accounts with balances equal to or over the materiality factor and trace balances to summary lists.
- (ii) Check additions of the lists of balances and cross cast. Trace total to lead schedule.
- (iii) Check that the total balances agree with the balances on the control account.
- (iv) Examine control account for the year and verify unusual items
- (v) Select balances for direct confirmation through debtor's circularisation. Investigate discrepancies and reconcile.
- (vi) If no circularization of debtors has been carried out, select a sample of balances and check receipts thereon after year end date. Trace such receipts to pay-in-slips.
- (vii) Examine accounts with credit balances and ensure that payments in respect of credit balances are authorized by responsible officials.
- (viii) Ensure that credit balances in debtors ledger are transferred to creditors' schedule
- (ix) Verify that provision for doubtful debts and discount are both reasonable and adequate.
- (x) Examine the credit control procedures and consider if any recommendations should be made. Check for compliance with credit policy of the entity with respect to credit limits, credit period, cash discounts, etc.

## **PATHFINDER**

- (xi) Verify that bad debts written off during the period were properly authorized and all reasonable recovery procedures have been taken prior to write-offs.
- (xii) Examine ledger for transfer between accounts throughout the year. Verify reasons for this and check authorization.
- (xiii) Examine credit notes issued after the year end and verify whether they relate to genuine sales.
- (xiv) Test returns during the period and ensure that credit notes are raised and posted accordingly.

### **EXAMINERS' REPORT**

**The question tests candidates understanding of auditor's liability and audit procedures relating to work-in-progress and debtors balances.**

**About 40% of the candidates attempted the question and performance was poor.**

**The commonest pitfall of candidates was that they could not articulate their answers using the right terms.**

**Candidates are advised to note this pitfall and prepare very well for future examinations.**

### **QUESTION 5**

- (a) IT Governance should operate within the following framework to achieve its goals and objectives.
  - (i) The Board, not the IT function, should be the prime driver for IT governance.
  - (ii) As with the corporation as a whole, sustained financial results should be the objective, prime driver for IT decisions and actions.
  - (iii) Governance should include managing the current and propelling toward the future state of the enterprise.
  - (iv) Since governance is behavior driven, emphasis in implementing this framework should be on changing behavior rather than introducing or changing work artifacts.
  - (v) Other IT governance activities and frameworks should be aligned within the corporate governance framework.

## **PATHFINDER**

- (vi) Appointment of a head of IT to coordinate activities.
- (b) IT oversight functions in an organization comprise the evaluation of:
  - (i) IT governance effectiveness: This is to ensure that there is adequate control of the board over the decisions, directions and IT Performance;
  - (ii) Human resource management and the operating organization structure in the IT environment: This is to ensure that they support the organisation's strategic objectives;
  - (iii) The strategies and processes adopted for IT operations to ensure they align with the organisation's overall objectives;
  - (iv) IT operational policies, standards and procedures for their development and implementation, to ensure their congruence with regulatory and legal standards;
  - (v) Management practices to ensure that they comply with the organisation's IT strategy;
  - (vi) The practices of IT resource investment, use and allocation to ensure alignment with the organisation's overall strategies and standards;
  - (vii) The organisation's risk management practices to ensure that they comply with the organisation's IT Strategy.

### **EXAMINERS' REPORT**

**The question tests candidates' understanding of Information Technology oversight functions in an organization.**

**Less than 30% of the candidates attempted the question and performance was generally poor.**

**The commonest pitfall of candidates was that rather than writing on IT governance they were listing the functions of IT professionals.**

**Candidates are advised to study this particular aspect of the syllabus because IT governance is becoming a global trend.**

## **PATHFINDER**

### **QUESTION 6**

- (a) The board should exercise its powers under the following circumstances:-
- (i) Filling a casual vacancy in the board
  - (ii) Recommending payment of dividend.
  - (iii) Appointing directors to fill casual vacancy.
  - (iv) Appointment of first auditors
  - (v) When strategic decisions are to be taken
  - (vi) When setting up the internal control procedures in an entity.
  - (vii) The board can also use its power to make discretionary payments to any staff of the company for welfare purposes or make some sort of donation to the community in which its company operates.
- (b) The functions of the Board of Directors as specified in the Code of Best Practices on Corporate Governance in Nigeria include the following:
- (i) Communication with shareholders
  - (ii) Succession planning
  - (iii) Ensuring that ethical standards are maintained and the company complies with applicable laws in Nigeria relevant to its operations.
  - (iv) Strategic planning.
  - (v) Ensuring the integrity of financial controls and reports and
  - (vi) Selection, performance, appraisal and compensation of senior executives.
- (c) The terms of reference of the corporate governance committee are to:
- (i) Examine practices in other jurisdictions with a view to adoption of international best practices in corporate governance in Nigeria.
  - (ii) Identify weaknesses in the current corporate governance practices in Nigeria with respect to public companies.
- (d) Audit committee should be established in accordance with CAMA Section 359 (3) with not more than one executive director. A non-executive director nominated by members of the audit committee should be the chairman of the audit committee.

## **PATHFINDER**

- (e) Ways through which a director can be removed from office before the expiration of his tenure include:
  - (i) A company may by ordinary resolution remove a director before the expiration of his period of office.
  - (ii) A removal could be effected by special notice
  - (iii) By special resolution.

### **EXAMINERS' REPORT**

The question tests candidates' understanding of Code of Best Practice on Corporate Governance.

About 80% of the candidates attempted the question but performance was poor.

Candidates' commonest pitfall was lack of understanding of the situation under which the board exercises its powers. They were listing the normal functions of the board.

Candidates are advised to read and interpret questions properly before attempting them.