

ASSOCIATION OF ACCOUNTING TECHNICIANS OF SRI LANKA

LEVEL III EXAMINATION - JANUARY 2022

(301) FINANCIAL REPORTING

19-03-2022
Morning
[08.45 – 12.00]

• **Instructions to candidates** (Please Read Carefully):

(1) **Time Allowed:** Reading : 15 minutes

Writing : 03 hours

No. of Pages : 11

No. of Questions : 10

(2) **All questions should be answered.**

(3) **Answers should be in one language, in the medium applied for, in the booklets provided.**

(4) **Submit all workings and calculations. State clearly assumptions made by you, if any.**

(5) **Use of Non-programmable calculators is only permitted.**

(6) **Action Verb Check List with definitions is attached. Each question will begin with an action verb. Candidates should answer the questions based on the definition of the verb given in the Action Verb Check List.**

(7) **100 Marks.**

SECTION A

(Total 20 marks)

Question 01

As per the Conceptual Framework for Financial Reporting, there are qualitative characteristics that enhance the usefulness of information that is relevant and faithfully represented. Further, the framework also sets out the measurement of the elements of financial statements.

You are required to:

(a) **Explain** two(02) qualitative characteristics that enhance the usefulness of financial information. (03 marks)

(b) **State** two(02) different measurement bases used for the measurement of the elements of financial statements. (02 marks)

(Total 05 marks)

Question 02

The adoption of integrated reporting redirects corporate reporting and make beyond excellence in financial and sustainability reporting.

You are required to:

(a) **Explain** the term “Sustainability Reporting”. (03 marks)

(b) **State** two(02) key areas included in the business model of an integrated report. (02 marks)

(Total 05 marks)

Question 03

A financial performance analysis includes analysis and interpretation of financial statements in such a way that it undertakes a full diagnosis of the profitability and financial soundness of the business. Financial ratios analysis is a way to identify the financial performance of a business.

You are required to:

- (a) **State** three(3) reasons as to why the financial ratios analysis is important for an organization. (03 marks)
- (b) **State** two(2) limitations of ratio analysis. (02 marks)
- (Total 05 marks)

Question 04

The followings information was extracted from the books of **Ganesh Ltd.** for the year ended 31st March 2021:

- (1) The company has conducted a market research for the development of a new product in March 2021. An amount of Rs.1,500,000/- was paid to the research company for conducting the market research.
- (2) The company registered the patent right for the new product and cost of registration for patent right was Rs.200,000/-.
- (3) Over the past few years, the company has maintained a good relationship with existing key customers. During the year, the company incurred Rs.2 million on customer entertainment programmes to increase the sale of new product.

You are required to:

Explain whether each of the above costs could be recognized as an intangible asset as per LKAS 38 - Intangible Assets. (05 marks)

End of Section A

SECTION B

(Total 30 marks)

Question 05

The Statements of Financial Position of **Arya (Pvt) Ltd.** as at 31st March 2021 and 31st March 2020 are given below:

Arya (Pvt) Ltd.
Statements of Financial Position *(Rs.'000)*

As at 31 st March	2021	2020
Non-Current Assets:		
Property, Plant and Equipment	10,500	8,200
Accumulated Depreciation	(5,600)	(4,800)
Carrying Value	4,900	3,400
Current Assets:		
Inventory	6,080	5,580
Trade Receivables	1,920	2,330
Cash and Cash Equivalents	1,200	990
	9,200	8,900
Total Assets	14,100	12,300
Equity:		
Stated Capital	5,000	5,000
Retained Earnings	3,050	2,187
	8,050	7,187
Non-Current Liabilities:		
Long Term Loans	3,300	2,700
Employee Benefits (Provision for gratuity)	1,600	1,200
	4,900	3,900
Current Liabilities:		
Short Term Loans	150	50
Trade Payables	750	330
Loan Interest Payable	100	70
Income Tax Payable	150	763
	1,150	1,213
Total Equity and Liabilities	14,100	12,300

The following additional information is also provided:

- (1) Income tax expense was estimated as Rs.105,000/- for the year ended 31st March 2021.
- (2) A machinery was disposed on 01st April 2020. Cost and accumulated depreciation as at 01st April 2020 of the machinery were Rs. 5.1 million and 2.5 million respectively. A loss of Rs.750,000/- was incurred on the disposal of this machinery. A new machinery was purchased during the year to replace the disposed machinery. Other than this, there were no other purchase or disposal of Property, Plant and Equipment during the year.
- (3) Gratuity paid during the year was Rs.360,000/-.
- (4) Interest on loans for the year was Rs.450,000/- and a loan of Rs.2,000,000/- was obtained during the year.
- (5) No dividends were paid during the year to the shareholders.

You are required to:

Prepare the Statement of Cash Flows of **Arya (Pvt) Ltd.** for the year ended 31st March 2021 using indirect method. (10 marks)

Question 06

(A) The following information was extracted from the books of **Ravi Ltd.** for the year ended 31st March 2021:

- (1) Taxable profit for the year ended 31st March 2021 was Rs.600,000/-
- (2) Differed tax assets as at 01st April 2020 was Rs.125,000/-.
- (3) Carrying value and tax base of non-current assets are as follows:

Item	Carrying Value (Accounting Written Down Value) as at 31 st March 2021 (Rs.)	Tax Base (Rs.)
Buildings	10,000,000	12,000,000
Machinery	6,000,000	5,000,000

- (4) Corporate income tax rate is 14%.

You are required to:

Compute the following:

- (a) Deferred tax asset / liability as at 31st March 2021. (03 marks)
- (b) Tax expenses for the year ended 31st March 2021. (02 marks)

(B) The following information was extracted from the books of **X Ltd.** for the year ended 31st March 2021:

- (1) A notice of assessment for the year of assessment 2018/19 was sent by the Department of Inland Revenue (IRD) due to non-payment of income tax and a penalty was imposed on non-payment of tax. As per the assessment, an amount of Rs.2.7 million has been charged by the IRD. The non-payment of income tax was Rs.1.3 million and the management is confident that a balance amount which is a penalty could be waived off.
- (2) One of the ex-employee has filed a case against the company to claim Rs.2 million on his dismissal from the company during the year 2018 due to being accused for a fraud. Due to the availability of valid evidences, the lawyer of the company believes that there is a less probability for the company to pay the compensation.

Decisions were not finalized regarding the above matters as of the date of authorization for issue of financial statements:

You are required to:

Explain how each of the above scenarios could be recognized in the Financial Statements for the year ended 31st March 2021 as per the LKAS 37 - Provisions, Contingent Liabilities and Contingent Assets.

(05 marks)

(Total 10 marks)

Question 07

(a) The following balances were appeared in the Statement of Financial Position of **Sony Ltd.** as at 01st April 2020 relating to its building: (Rs.)

Asset	Cost	Accumulated Depreciation as at 01 st April 2020	Carrying Value as at 01 st April 2020
Building	24,000,000	7,200,000	16,800,000

The estimated useful life of the building was 40 years and the buildings are depreciated on the straight-line basis at cost by the company.

On 01st April 2020, the useful life of the building was reviewed and it was revealed that the remaining useful life of the building has been increased by further 32 years as at 01st April 2020.

You are required to:

Calculate the accumulated depreciation and carrying value of the building as at 31st March 2021.

(04 marks)

- (b) On 01st April 2020, **Sigma Ltd.** (lessee) entered into a lease agreement with **ABC Finance Company** (lessor) to purchase a machinery. You are given the following information with reference to the lease agreement:

Fair value of the machinery	Rs.3,000,000/-
Advance amount paid at the commencement of the lease	Rs.1,000,000/-
Lease term	3 years
Annual lease installment	Rs.832,635/- (to be paid on 31 st March of each year)
Implicit interest rate	12% per annum

The first installment of the lease was paid on 31st March 2021 and as per the lease agreement, the ownership of the machinery is transferred to **Sigma Ltd.** at the end of the lease term. The company depreciates the right to use asset on the straight-line basis over the lease term.

You are required to:

Prepare the extracts of the Statement of Comprehensive Income for the year ended 31st March 2021 and Statement of Financial Position as at 31st March 2021 of **Sigma Ltd.** regarding the lease transaction.

(06 marks)

(Total 10 marks)

End of Section B

SECTION C

(Total 50 marks)

Question 08

The following trial balance was extracted from the books of **Richi PLC** as at 31st March 2021:

Richi PLC	<i>(Rs.'000)</i>	
Trial Balance as at 31st March 2021	Dr.	Cr.
Stated Capital (10,000,000 Ordinary Shares)		100,000
Revaluation Reserve		3,000
Retained Earnings as at 01 st April 2020		22,000
Property, Plant and Equipment at Cost / Revalued Amount:		
Land & Building (Land at revalued value - Rs.44 million)	62,000	
Machinery	14,000	
Computer Software	3,000	
Accumulated Depreciation as at 01st April 2020:		
Building		12,000
Machinery		6,000
Computer Software		1,200
Capital Work-In-Progress	18,000	
Inventory as at 31 st March 2021	28,000	
Trade Receivables / Trade Payables	21,700	15,600
Allowance for Trade Receivables as at 01 st April 2020		3,000
Pre-payments	12,000	
Cash in Hand and at Banks	25,100	
Cost of Sales / Sales	81,000	150,000
Other Income		2,100
Income Tax Payable as at 01 st April 2020		3,500
Income Tax Paid	7,200	
Administration Expenses	34,200	
Distribution Expenses	21,000	
Finance Expenses	6,200	
Bank Loan		15,000
	333,400	333,400

The following additional information is also provided:

- (1) During the year, one of the customers has filed a court case against the company to claim Rs. 1 million compensation for selling bad quality products. On 20th May 2021, the court has ordered the company to pay Rs.750,000/- to the customer as the compensation. No adjustments were made in the books of accounts in this regard.

- (2) Audit fee of Rs.600,000/- for the financial year 2020/2021 has not been accounted. Pre-payment account represents rent payment made for entire calendar year of 2021.
- (3) On 30th April 2020, the company obtained a bank loan of Rs. 15 million at an interest rate of 10% per annum to construct a factory building. Construction of the building was started on 01st May 2020 and it was in progress as at 31st March 2021. Cost incurred during the year on construction was recorded under the Capital Work-in-Progress account and interest on loan for the year was charged to Finance Expenses Account. The bank has given one year grace period to settle the capital repayments and $\frac{1}{4}$ of the loan should be paid in next year.
- (4) It was brought to the notice of the company that a customer who owed Rs.500,000/- to the company was declared bankrupt on 31st March 2021 and a full provision was made in the previous year regarding his dues. Further, it was decided to provide the allowance for receivable at 10% on the remaining trade receivables balance as at 31st March 2021.
- (5) The total income tax liability for the year of assessment 2019/20 was Rs.3,500,000/- which was paid during the year ended 31st March 2021 and the amount paid has been charged to the income tax paid account. The total income tax liability for the year of assessment 2020/21 was estimated as Rs.5,300,000/-.
- (6) Property, Plant and Equipment are to be depreciated on the straight-line basis at cost. The useful life of the assets is as follows:
- | | | |
|-------------------|---|----------|
| Building | : | 20 years |
| Machinery | : | 04 years |
| Computer Software | : | 04 years |
- (7) The company carried out an impairment test for machinery on 31st March 2021 and it was revealed that the fair value less cost of disposal of machinery was Rs.3,000,000/- and value in use of the machinery was Rs.3,400,000/-. No adjustment was made in the books of accounts regarding the impairment.
- (8) Revaluation reserve represents the surplus on land revaluation made 2 years ago.
- (9) The board of directors of the company approved the financial statements for issue on 30th June 2021.

You are required to:

Prepare the following, for **Richi PLC** in a form suitable for publication:

- (a) Statement of Profit or Loss and Other Comprehensive Income (Comprehensive Income Statement) for the year ended 31st March 2021. (10 marks)
- (b) Statement of Financial Position as at 31st March 2021. (09 marks)
- (c) Statement of Changes in Equity for the year ended 31st March 2021. (02 marks)
- (d) Note to the Financial Statements showing movement of Property, Plant and Equipment for the year ended 31st March 2021. (04 marks)
- (Total 25 marks)

Question 09

The following information was extracted from **Beeshma PLC** for the year ended / as at 31st March 2021 and 31st March 2020:

(Rs.'000)

For the year ended 31st March	2021	2020
Sales	372,400	320,300
Cost of Sales	203,500	178,500
Interest Expense	7,220	5,950
Income Tax	4,000	3,800
Profit for the year	22,700	17,800
As at 31st March	2021	2020
Retained Earnings	41,600	18,900
Current Assets	151,400	140,200
Current Liabilities	47,400	33,100
Trade Payables	38,300	25,900
Inventory	95,400	88,400
Stated Capital (5,500,000 Ordinary Shares)	55,000	55,000

All purchases are made on credit.

You are required to:

(a) **Compute** the following ratios based on the above information for the year ended / as at 31st March 2021:

- (i) Gross Profit Ratio.
- (ii) Quick Assets Ratio.
- (iii) Stock Residence Period.
- (iv) Creditors' Settlement Period.
- (v) Earnings Per Share.

(05 marks)

(b) The following industry averages have also been computed for the year 2020/21:

Gross Profit Ratio	52%
Quick Assets Ratio	1.25 : 1
Stock Residence Period	35 days
Creditors' Settlement Period	42 days
Earnings Per Share	Rs.7.50

Analyze the performance of **Beeshma PLC** for the year ended / as at 31st March 2021 with industry averages.

(05 marks)

(Total 10 marks)

Question 10

The following Statements of Financial Position were extracted from **Hiru Ltd.** and **Tharu Ltd.** as at 31st March 2021:

Statements of Financial Position		<i>(Rs.'000)</i>	
As at 31st March	Hiru Ltd.	Tharu Ltd.	
Non-Current Assets:			
Property, Plant and Equipment at Carrying Value	60,000	55,000	
Investment in Tharu Ltd.	40,000	-	
Current Assets:			
Inventory	13,000	18,000	
Trade and Other Receivables	20,000	15,000	
Cash and Cash Equivalents	12,000	15,000	
	45,000	48,000	
Total Assets	145,000	103,000	
Equity:			
Stated Capital	60,000	40,000	
Retained Earnings	14,500	17,200	
	74,500	57,200	
Non-Current Liabilities:			
Bank Loan	16,000	32,000	
Current Liabilities:			
Trade and Other Payables	54,500	13,800	
Total Equity and Liabilities	145,000	103,000	

The following additional information is also provided:

- (1) **Hiru Ltd.** acquired 80% of ordinary share capital of **Tharu Ltd.** on 01st April 2020. Fair value of the non-controlling interest on the date of acquisition was Rs. 20 million. As at the date of acquisition, **Tharu Ltd.**'s retained earnings was Rs.13 million and the fair value of identifiable net assets of **Tharu Ltd.** was equal to its book value.
- (2) On 01st April 2020, **Hiru Ltd.** sold a motor vehicle which was purchased on 01st April 2018 at a cost of Rs. 5 million to **Tharu Ltd.** for Rs. 6 million. Both companies depreciate their motor vehicles over 5 years on the straight-line basis at cost.
- (3) During the month of March 2021, **Tharu Ltd.** sold an inventory costing Rs. 10 million with a 20% profit margin on cost to **Hiru Ltd.** Of that, 50% of the stocks remained unsold at the warehouse of **Hiru Ltd.** as at 31st March 2021. Further, the full amount on this transaction was recorded in trade receivables of **Tharu Ltd.** and trade payables of **Hiru Ltd.**

You are required to:

- (a) **Calculate** the goodwill arising from consolidation. (04 marks)
- (b) **Prepare** Consolidated Statement of Financial Position as at 31st March 2021. (11 marks)

(Total 15 marks)

ACTION VERBS CHECK LIST

Level of Competency	Description	Action Verbs	Verb Definitions
Knowledge (1)	Recall Facts and Basic Concepts.	Draw	Produce a picture or diagram.
		Relate	Establish logical or causal connections.
		State	Express details definitely or clearly.
		Identify	Recognize, establish or select after consideration.
		List	Write the connected items.

Level of Competency	Description	Action Verbs	Verb Definitions
Comprehension (2)	Explain & Elucidates Ideas and Information.	Recognize	Show validity or otherwise, using knowledge or contextual experience.
		Interpret	Translate into understandable or familiar terms.
		Describe	Write and communicate the key features.
		Explain	Make a clear description in detail using relevant facts.
		Define	Give the exact nature, scope or meaning.

Level of Competency	Description	Action Verbs	Verb Definitions
Application (3)	Use and Adapt Knowledge in New Situations.	Reconcile	Make consistent / compatible with another.
		Graph	Represent by graphs.
		Assess	Determine the value, nature, ability or quality.
		Solve	Find solutions through calculations and/or explanation.
		Prepare	Make or get ready for a particular purpose.
		Demonstrate	Prove or exhibit with examples.
		Calculate	Ascertain or reckon with mathematical computation.
		Apply	Put to practical use.

Level of Competency	Description	Action Verbs	Verb Definitions
Analysis (4)	Draw Connections Among Ideas and Solve Problems.	Communicate	Share or exchange information.
		Outline	Make a summary of significant features.
		Contrast	Examine to show differences.
		Compare	Examine to discover similarities.
		Discuss	Examine in detail by arguments.
		Differentiate	Constitute a difference that distinguishes something.
		Analyze	Examine in details to find the solution or outcome.