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SCHOOL OF ACCOUNTING AND BUSINESS
BSc. (APPLIED ACCOUNTING) GENERAL / SPECIAL DEGREE
PROGRAMME

END SEMESTER EXAMINATION – JULY 2015

AFM 30930 Financial Reporting Framework

Date : 19th July 2015
Time : 9.00 a.m. – 12.00 p.m.
Duration : Three (03) hours

Instructions to Candidates:

- Answer **ALL** questions.
- This paper consists of two sections (A and B)
Section A: Please submit answers to **Section A** separately in the sheet given
Section B: Answer **ALL** questions.
- The total marks for the paper is 100.
- The marks for each question are shown in brackets.
- Non programmable calculators are allowed.
- Answers should be written neatly and legibly.

Section A

Select most appropriate answer for following questions.

1. Which of the following statement is **true** in relation to the characteristics of a liability as per conceptual framework of financial reporting?
 - A. There should be a present obligation as a result of past event.
 - B. There should be a legal obligation as a result of past vent.
 - C. There should be a possible obligation as a result of future event.
 - D. There should be a future obligation as a result of present event.

2. Dimuthu PLC had 20,000 units of product A which are only 70% completed as at 31.03.2015. Cost incurred as of that date was Rs.650,000. These items can be sold at Rs.55 each once the product is completed after incurring cost of another Rs.250,000. Further, 10% of selling price should be paid as sales commission to sales staff at the point of sale. The net realizable value of these inventories as at 31.03.2015 is:
 - A. Rs.690,000
 - B. Rs.740,000
 - C. Rs.800,000
 - D. Rs.990,000

3. Which of the following statement is **true** in relation to measurement of an item of property, plant at equipment at recognition?
 - A. It should be measured at cost.
 - B. It should be measured at fair value.
 - C. It should be measured at cost or fair value whichever is lower.
 - D. It is should be measured using cost model or revaluation model.

4. Which of followings is **not** an example for investment property?
 - A. Land held for long term capital appreciation.
 - B. Land held for currently undetermined future use.
 - C. Land that is being developed for the use of the business.
 - D. Land which is owned by the business and leased out under an operating lease.

5. Global PLC revalued its plants and machinery for Rs.2.8 million on 01.04.2013 for the first time. On this date the cost and accumulated depreciation of plants and machinery were Rs.3 million and Rs.1.2 million respectively. These assets were purchased on 01.04.2010 and have estimated useful life of 10 years. The same assets were revalued again on 01.04.2015 for Rs.2.5 million. The revaluation done on 01.04.2015 resulted in :
- Deficit of Rs.300,000
 - Deficit of Rs.700,000
 - Surplus of Rs.260,000
 - Surplus of Rs.500,000
6. A business purchased a plant for Rs.8 million on 01.04.2010 of which estimated useful life time was 8 years. On 31.03.2014, the fair value less cost to sell of this plant was Rs.3.6 million and present value of expected future cash flows from using the asset in the business was Rs.3.4 million. The amount of impairment loss and depreciation expense to be recognized for year ending 31.03.2015 are:

	Impairment loss (Rs.)	Depreciation expenses (Rs.)
A.	nil	1,000,000
B.	400,000	900,000
C.	400,000	1,000,000
D.	500,000	850,000

7. Which of following statement is **false** as per LKAS41: Agriculture?
- Biological asset is a living animal or plant.
 - Agricultural produce is the harvest of the biological assets.
 - Biological assets are measured at fair value less cost to sell under any circumstances.
 - All biological assets can be classified as bearer biological assets or consumable biological assets.
8. Which of following statement is not an example for a financial asset?
- Cash
 - Trade Receivables
 - Dentures' issued carrying interest at 15%
 - Investment in ordinary shares of XYZ PLC

9. Which of the following statement is false in relation to total comprehensive income
- A. It is the total of profit for the year and income & expenses not recognized in profit or loss
 - B. It is the total of profit or loss for the year and other comprehensive income
 - C. It represent change in the equity during the year other than the transactions with owners in their capacity of owners
 - D. It is the total of profit or loss for the year and any income not recognized in the profit or loss
10. “A professional accountant should be straightforward and honest in all professional and business relationships” Which fundament principle of IFAC code of ethics explains in the above statement?
- A. Objectivity
 - B. Integrity
 - C. Professional confidence and due care
 - D. Professional behavior

(Total 20 Marks)

Section B

Question No. 01

- a. **Distinguish** the provision from contingent liabilities.

(3 Marks)

- b. ABC PLC purchased a land for Rs.4.5 million on 01.04.2005 and it was revalued for the first time on 31.03.2010 for Rs.4.9 million. This land was revalued again on 01.04.2014 for Rs.4.2 million. The profit for the year ending 31.03.2010 and 31.03.2015 before making any adjustments for these revaluations were Rs.2.6 million and Rs.3.5 million respectively. Retained earnings as at 31.03.2009 and 31.03.2104 were Rs.8 million and Rs.12.5 million respectively.

Show the extracts of statements of profit or loss and other comprehensive income and statements of financial position for year 2009/10 and 2014/15.

(6 Marks)

- c. The following information has been extracted from the financial statements of Lanka PLC for year ending 31.03.2015. Lanka PLC was **incorporated** on 01.04.2014.

Statement of profit or loss for year ending 31.03.2015

(Rs.000)

Sales	25,000
Cost of sales	<u>(16,000)</u>
Gross Profit	9,000
Other Income	1,250
Operating expenses	(4,500)
Finance expenses	<u>(900)</u>
Profit before tax	4,850
Income tax expense	<u>(1,350)</u>
Profit for the year	3,500

The following additional information is also available.

- All the sales and purchases were made on credit basis.
- Operating expenses includes depreciation expense of Rs.1.2 million.

- iii. Other income consist of dividend income of Rs.750,000 and profit on disposal of a motor vehicle of Rs.500,000.
- iv. The finance expense was entirely consists of interest expenses.
- v. The following balances were available as at 31.03.2015

	(Rs.000)
Trade receivables	1,500
Trade payables	2,300
Inventories	1,800
Accrued interest	340
Prepaid operating expenses	400
Income tax payable	550

Prepare the cash flows from the operating activities using indirect method as per LKAS7: Statement of Cash Flows.

(7 Marks)

- d. America PLC acquired 70% of the stated ordinary share capital of Africa PLC on 03.03.2015 for Rs.25 million. The fair value of identifiable net assets of Africa PLC on this date was Rs.30 million. The fair value of non-controlling interest of Africa PLC on this date was Rs.10.5 million.

Calculate the goodwill to be recognized in the consolidated statement of financial position as at 31.03.2015 on the basis that non-controlling interest is measured using

- a. Proportionate share of net assets method
- b. Fair value method

(4 Marks)

(Total 20 Marks)

Question No. 02

a. A trainee accountant of Green Planet PLC has suggested the following accounting treatments for some of the accounting issues identified.

- i. Since the company has changed cost formula used in determining cost of inventories from first in first out (FIFO) method to weighted average method based on the industry practices, it should be considered as a change in an accounting policy and should be accounted prospectively.
- ii. Since it generates future economic benefits, the internally generated goodwill should be recognised in the financial statements.
- iii. Since the warranty certificates issued by the business represent only a possible obligation, it should only be disclosed in the notes as a contingent liability.

Critically evaluate the suggested accounting treatment for each scenario with reference to relevant LKASs.

(9 Marks)

b. **Distinguish** the finance lease from operating lease. **Explain** the accounting concept which rationalizes accounting treatment for finance lease in the lessee's book.

(3 Marks)

c. Kurunegala PLC entered in to finance lease agreement to acquire a motor vehicle on finance lease on 01.04.2014. The following information is available in relation to this transaction.

Fair value of the motor vehicle	Rs.4.5 million
Initial deposit paid at the time of agreement	Rs.1 million
Annual lease rental paid on 31.03.2015	Rs.970,934
Lease term	5 years
Useful life	7 years
Interest rate implicit in the lease	12% per annum
Residual value	Rs.300,000
Title of the asset is transferred to lessee at the end of the lease term	

- i. **Prepare** the lease liability account for year ending 31.03.2015 and 31.03.2016

- ii. **Provide** the extracts of statement of profit or loss and other comprehensive income for year ending 31.03.2015
- iii. **Provide** the extracts of statement of financial position as at 31.03.2015

(8 Marks)

(Total 20 Marks)

Question No. 03

- a. The followings information is relevant to borrowings of Colombo PLC as at 01.04.2014.

	Interest rate per annum	Amount (Rs.000)	Investment income earned for year ending 31.03.2015 from temporary investing the fund borrowed
Loan - Alpha Bank	11%	8,000	280
Loan - Beta Bank	12.5%	6,000	170
Rs.100, Debentures	15%	4,000	120
Overdraft - Sigma Bank	14%	2,000	-

Additional information

The Loan obtained from Alpha bank was fully used for construction of a building. The construction works were commenced on 01.02.2014 and completed on 31.05.2015. Rs.6.5 million was utilized for construction of a power plant during the year from the fund raised by issue of debentures and loan obtained from Beta Bank. The construction of this plant was commenced on 01.09.2013 and completed on 30.06.2015. Bank overdraft was used for operating activities of the business.

Identify the amount of borrowing cost to be capitalized to each asset separately and the borrowing cost to be recognised as expense for year 2014/15.

(5 Marks)

- b. The following information is available in relation to items of property, plant and equipments of Suranga PLC as at 31.03.2015. All the assets were purchased on 01.04.2014.

Asset	Cost (in Rs.000)	Depreciation rate for accounting purpose	Depreciation rate for tax purpose
Buildings	8,000	10%	20%
Motor Vehicles	6,000	25%	25%
Office Equipments	4,500	33.33%	20%

The income tax paid based on self assessment during the year ending 31.03.2015 was Rs.1.8 million and total income tax liability for the year ending 31.03.2015 was estimated as Rs.2.4 million. The tax rate applicable to business is 30%.

- Calculate** the taxable temporary difference and deductible temporary difference.
- Calculate** the differed tax liability and deferred tax asset as at as at 31.03.2015.
- Prepare** the income tax expense account for the year ending 31.03.2015.
- Provide** the extracts of statement of financial position as at 31.03.2015

(08 Marks)

- c. The following information is relevant to a construction contract undertaken by Aken PLC.

Date of agreement	01.04.2013
Initial contract price agreed	Rs.500 million
Total estimated cost	Rs.420 million
<u>As at 31.03.2014</u>	
Cost incurred up to date	Rs.178 million
Value of works certified	Rs.200 million
Progress payments received up to date	Rs.125 million
<u>As at 31.03.2015</u>	
Cost incurred up to date	Rs.345 million
Value of works certified	Rs.406 million
Progress payments received up to date	Rs.275 million
Due to change in specification the contract cost and price was increased by Rs.80 million and Rs.50 million respectively on 31.03.2015.	

- Calculate** the stage of completion as at 31.03.2014 and 31.03.2015

- ii. **Provide** the extracts of statements of profit or loss and other comprehensive income for year ending 31.03.2014 and 31.03.2015.
- iii. **Provide** the extracts of statements of financial position as at 31.03.2014 and 31.03.2015

(7 Marks)

(Total 20 Marks)

Question No. 04

- a. **Explain** the two fundamental qualitative characteristics of financial information as per conceptual framework for financial reporting.

(6 Marks)

- b. As per guide lines of LKAS 36, when the carrying amount of an asset exceeds its' recoverable amount the difference should be accounted as an impairment loss and asset is recognized in the statement of the financial position at the recoverable amount.

Explain the rationale of this treatment with reference to definitions and recognition criteria of assets as per conceptual framework for financial reporting.

(5 Marks)

- c. "When a company owns more than 50% of equity shares of another entity it results parent subsidiary relationship. When a company owns less than 50% of equity shares of another entity it result an investment in associates. When an entity owns exactly 50% of equity shares of another entity it results an investment in joint venture". **Critically evaluate the above statement.**

(10 Marks)

(Total 20 Marks)