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

YEAR II SEMESTER I
END SEMESTER EXAMINATION – JANUARY 2016

AFM 20630 Advanced Financial Accounting

Date	:	09th January 2016
Time	:	9.00 a.m. – 12.00 p.m.
Duration	:	Three (03) hours

Instructions to Candidates:

- Answer **ALL** questions
- The total marks for the paper is 100.
- Marks for each question are shown in brackets.
- Use of scientific calculator is allowed.
- Answers should be written neatly and legibly.

Question No. 01

The trial balance of ABC PLC as at 31.03.2015 is given below.

	Debit (Rs.000)	Credit (Rs.000)
Land and buildings at Cost	15,000	
Motor vehicles at Cost	9,500	
Office equipment at cost	4,600	
Cost of sales	2,250	
Sales		8,100
Sales returns	100	
Provision for depreciation as at 01.04.2014		
Buildings		1,000
Motor vehicles		2,500
Office equipment		500
Inventories as at 31.03.2015	450	
Cash at bank and in hand	230	
Trade receivables	2,760	
Trade payables		715
Stated capital-ordinary shares		10,000
Redeemable preference shares		5,000
Retained earnings as at 01.04.2014		4,500
Distribution expenses	850	
Administration expenses	725	
Finance expenses	120	
Other expenses	80	
Other income		910
Bank loan		4,500
Income tax paid	160	
Dividends paid- ordinary shares	600	
Dividends paid- redeemable preference shares	300	
	37,725	**37,725**

The following additional information is also provided.

1. The inventories as at 31.03.2015 were valued at cost. These inventories includes goods costing Rs. 125,000 of which the net realizable value was estimated as Rs. 85,000.
2. Stated ordinary share capital of the company consisted of 1 million shares issued at Rs.10 each. Company capitalized the retained earnings (made a bonus issue) by issuing one share for every five shares held on 31.03.2015 at Rs.12 each. But no accounting entries were made in this regard.
3. Cost of the land is Rs.7 million and it was revalued at Rs.8.5 million on 31.03.2105. But no accounting entries were made in this regard, Board of Directors of the company decided to take revalued amount to the financial statements.
4. During the year following additions were made to property, plant and equipment and properly accounted.

   01.10.2014: Building Rs.2.6 million

   01.01.2015: Office equipment Rs.1.2 million.
5. A motor vehicle belonging to the company was sold for Rs.850,000 on 01.10.2014. This motor vehicle was purchased on 01.10.2009 for Rs.1.5 million. No accounting entries were made in this regards other than debiting the sales proceeds to cash account by crediting other income account.
6. Property, plant and equipment are depreciated at following rates on straight line method.

   Building -5% p.a.

   Motor vehicles-10% p.a.

   Office equipment-20% p.a.
7. Accrued office rent and sales staff commission as at 31.03.2015 were Rs.25,000 and Rs.60,000 respectively.
8. Distribution expenses includes prepaid advertising expenses of Rs.120,000.
9. The income tax liability for the year is estimated as Rs.270,000.
10. 1/3 of the bank loan should be settled during the year ending 31.03.2016.
11. The board of directors have decided to transfer Rs750,000 to general reserve.
12. Board of directors proposed to pay final dividend of Rs.500,000 for ordinary shareholders and the balance dividend of Rs.300,000 to redeemable preference shares.

Prepare the following financial statements for the purpose of publication.

a. Statement of profit or loss and other comprehensive income for year ended 31.03.2015
b. Statement of financial position as at 31.03.2015
c. Statement of changes in equity for year ended 31.03.2015
d. Note on property, plant and equipment

(Other notes to the financial statements are not required)

(Total 30 Marks)

Question No. 02

The summarised draft financial statements of Kandy PLC and Galle PLC are given below.

Statements of profit or loss and other comprehensive income for the year ended 31 March 2015		
	Kandy PLC Rs. '000	**Galle PLC Rs. '000**
Sales revenue	27,500	11,600
Cost of sales	(12,200)	(6,500)
Gross profit	15,300	5,100
Other Income	1,800	900
Operating expenses	(6,100)	(1,850)
Finance expense	(1,450)	(550)
Profit before tax	10,550	3,600
Taxation	(1,550)	(600)
Profit for the year	**9,000**	**3,000**
Other comprehensive income		
Revaluation reserve	3,000	1,000
Total comprehensive income for the year	**12,000**	**4,000**

Statements of financial position as at 31 March 2015		
	Kandy PLC Rs. '000	**Galle PLC Rs. '000**
Non Current Asset		
Property, plant & equipment	35,000	21,250
Investments	26,500	1,200
Current Assets		
Inventories	14,500	7,500
Receivables	11,250	4,750
Cash and Bank	4,750	2,400
	92,000	**37,100**
Equity		
Ordinary shares of Rs.10 each	55,000	20,000
Retained earnings	20,750	8,000
Revaluation reserve	3,000	1,000
Non-current liabilities		
12% Debentures	9,500	2,500
Current liabilities		
Payables	3,750	5,600
	92,000	**37,100**

The following additional information is also provided.

1. Kandy PLC acquired 60% of the ordinary share capital of Galle PLC at a cost of Rs.20 million on 01.04.2014 when the retained earnings of Galle PLC was Rs.6 million.
2. The fair values of net assets of Galle PLC's at the date of acquisition was Rs.28 million and any difference between the fair values of net assets and the carrying amount was due the change in value of land. The market price of a share of Galle PLC on this date was Rs.18.
3. During the year Kandy PLC sold goods to Galle PLC at a price of Rs. 2.5 million with profit margin of 20% on the selling price. Half (1/2) of these goods were remained unsold at Galle PLC at the year end.
4. During the year Galle PLC sold goods to Kandy PLC at a price of Rs. 2 million by adding 20% profit markup to cost. 3/4 of these goods were remained unsold at Galle PLC at the year end.

5. Receivable balance of Galle PLC includes Rs.1.5 million receivable from Kandy PLC. But payable balance of Kandy PLC includes only Rs.900,000 payable to Galle PLC. This difference is due to cash in transit.
6. During the year Galle PLC has paid interim dividends of Rs.1 million and Kandy PLC has properly accounted for the dividend received from Galle PLC.
7. Galle PLC has paid Rs.500,000 rent to Kandy PLC during the year for the use of building owned by Kandy PLC.
8. Galle PLC issued 12%, debentures on 01.04.2014 and Kandy PLC has invested 40% of these debentures on that day. Interest on debentures was paid by the Galle PLC and Kandy PLC has properly accounted for the interest received.
9. Revaluation surplus of Galle PLC represents the surplus arisen from the revaluation of plant and machineries.
10. Use fair value method to measure non-controlling interest.
11. Kandy PLC acquired 30% of the stated ordinary share capital of Colombo PLC on 01.04.2014 for Rs.3 million when retained earnings of Colombo PLC was Rs.800,000
12. Colombo PLC reported a profit of Rs.3 million for the year ending 31.03.2015. Further, Colombo PLC paid interim dividend of Rs.800,000 during the year and Kandy PLC has recorded the dividend received from Colombo PLC under other income.

Prepare the following financial statement of Kandy Group.

a. Consolidated statement of profit or loss for year ended 31.03.2015
b. Consolidated statement of Financial Position as at 31.03.2015.

(Total 30 Marks)

Question No. 03

The following information has been extracted from the financial statement of Sagara PLC.

	For the year ending / as at 31.03.2015 (Rs.000)
Sales revenue	25,000
Cost of sales	15,000
Other income	4,000
Operating expenses	6,000
Other expenses	500
Finance expenses	1,200
Total current assets	10,000
Total current liabilities	4,600
Inventories	3,500
Debtors	5,200
Creditors	4,000
Ordinary share capital	20,000
Retained earnings	10,000
Long term borrowings	12,000

The following additional information is also provided.

1. Inventories, debtors and creditors balances as at 31.03.2014 were Rs.2.25 million, Rs.4.8 million and Rs.5 million respectively.
2. Current ratio and quick assets ratio as at 31.03.2014 were 1.6:1and 0.7:1 respectively.
3. Gross profit ratio and net profit ratio for the year ending 31.03.2014 were 41% and 15% respectively.
4. The ordinary share capital consists of 2 million ordinary shares issued at Rs.10 each.
5. Inventory retention period, debtor's collection period and creditors' payment period for year 2013/14 were 50 days, 55 days and 90 days respectively.
6. The market price of an ordinary share of the company as at 31.03.2015 was Rs.20 per share.

a. **Calculate** the following ratios for the year 2014/15.

   i. Gross profit ratio

   ii. Net profit ratio

   iii. Return on equity

iv. Current ratio
v. Quick asset ratio
vi. Inventory turnover
vii. Inventory retention period
viii. Debtors collection period
ix. Creditors payment period
x. Debt equity ratio
xi. Earnings per share
xii. Earnings yield ratio

b. **Comment** on the profitability, liquidity and working capital management of the Sagara PLC based on your ratio calculations.

(Total 20 Marks)

<u>Question No. 04</u>

a. **Differentiate** ordinary shares and preference shares

(04 Marks)

b. "When a company acquired more than 50% of the ordinary share capital of another business it creates a parent-subsidiary relationship but when company invests less than 50% of ordinary shares it creates only the investor-associate relationship."

Critically evaluate the above statement.

(08 Marks)

c. **Explain** the equity method of accounting with reference to relevant accounting standards.

(03 Marks)

d. **Define** the following terms as per *SLFRS 11: Joint arrangement*
   i. Joint control
   ii. Joint venture
   iii. Joint operation

(05 Marks)

(Total 20 Marks)