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Serial No.....

## Society of Certified Management Accountants of Sri Lanka

### Intermediate Stage March 2007 Examination

Examination Date : 17<sup>th</sup> March 2007  
Examination Time: 9.30a.m.- 12.30p.m.

Number of Pages : 08  
Number of Questions: 05

#### Instructions to candidates:

1. Time allowed is **three (3) hours**.
2. Answer **all** questions.
3. Answers should be entirely in the **English** language.

<b>Subject</b>	<b>Subject Code</b>
<b>Financial Accounting &amp; Reporting</b>	<b>(FAR)</b>

#### Question No. 01 (30 Marks)

Asiri Limited was incorporated in April 2000 with an authorised capital made up of 4,000,000 ordinary shares of Rs. 10/- each and 2,000,000, 10% cumulative preference shares of Rs. 10/- each.

Trial Balance extracted from the books of Asiri Limited as at 31.03.2006 was as follows.

	<b>Dr. (Rs. '000)</b>	<b>Cr. (Rs. '000)</b>
Ordinary share capital		20,000
10% Preference share capital		10,400
Share premium		1,800
Retained profit on 31.03.2005		10,200
Freehold land and buildings at cost	16,000	
Furniture and office equipment at cost	9,000	
Motor vehicles at cost	18,400	
Provision for depreciation on 31.03.2005		
- Buildings		640
- Furniture & office equipment		3,800
- Motor vehicles		6,120
Turnover		154,320
Cost of goods sold	121,000	
Stocks	15,360	
Trade receivables / Trade payables	8,480	7,400
Administration expenses	8,400	
Selling & distribution expenses	8,200	
Provision for bad and doubtful debts		480
12% Redeemable debentures on 01.04.2005		4,000
Debenture redemption account	2,320	
Interest paid	240	
Income tax paid – y/a 2005/2006	3,840	
Cash at bank	5,800	
Cash in hand	2,120	
	219,160	219,160

Following additional information is available.

- (i) (a) Asiri Limited acquired the land & buildings in the year 2000 at a land value of Rs. 11.2 Million.
- (b) A Computer at a cost of Rs. 320,000 was purchased for office use during this year.
- (c) A motor vehicle purchased on 10.05.2003 at a cost of Rs. 3,360,000 was sold for Rs. 1,600,000 during the year and the entire sale proceeds was credited to motor vehicle account. No other entries were made in this respect.
- (d) A motor vehicle at a cost of Rs. 2,000,000 was purchased during this year and properly accounted for.

There was no other addition / disposal during this year.

- (ii) Asiri Ltd's depreciation policy is not to provide for depreciation in the year of purchase but to provide full depreciation in the year of sale, on a straight line method at the following rates.

- Buildings	@ 5% per annum
- Furniture & Office Equipment	@ 20% per annum
- Motor vehicle	@ 25% per annum

- (iii) Closing stocks were valued at cost and included the following.

- (a) 20,000 units of material X at Rs. 50/- per unit. These materials have become obsolete and could be sold as scrap at Rs. 5/- per unit.
- (b) Stock of material Y to the value of Rs. 480,000/- was destroyed by fire on 15.04.2006. These stocks were not insured against any risk.

- (iv) Provision for doubtful debts account balance as on 31.03.2005 had included Rs. 80,000 as a specific provision for the amount due from customer Rajan who was declared bankrupt on 15.09.2005. Balance amount in the account was on account of general provisions.

Customer Silva who owed Rs. 160,000/- as at 31.03.2006 died on 15.04.2006 and hence his amount has become irrecoverable. No adjustments have been made in the books in this respect. Provision for doubtful debts is to be adjusted at 5% on balance outstanding as at the end of the year.

- (v) Asiri Ltd did not provide for gratuity payable in the past. Management has now decided to incorporate this liability as at March 31, 2005 as follows.

Gratuity liability as at 31.03.2005 is Rs. 2,320,000  
Gratuity liability as at 31.03.2006 is Rs. 2,880,000

- (vi) Debenture interest is payable half yearly on September 30, and March 31, each year.
- (vii) Income tax of the company for the year ended 31.03.2006 has been estimated at Rs. 4,240,000.
- (viii) Board of Directors of Asiri Ltd., had decided to redeem 50% of its debentures at 10% premium on 31.03.2006. For this purpose, it issued 200,000 preference shares at a premium of Rs. 2 per share. Total amount paid to the debenture holders on account of redemption was debited to debenture redemption account while total proceeds from issue of preference shares was credited to preference share capital account.

Further, the Board has proposed the following.

- (a) To pay dividend on preference shares held throughout the year.
- (b) To issue bonus shares at the rate of one share for every four ordinary shares held as at 31.03.2006.

**You are required to prepare :**

- (I) Income Statement of Asiri Limited for the year ended March 31, 2006. **(09 Marks)**
- (II) Balance Sheet as at March 31, 2006. **(09 Marks)**
- (III) Statement of Changes in Equity for the year ended March 31, 2006. **(05 Marks)**
- (IV) Following Notes to Financial Statements
- (a) Property, Plant and Equipment **(04 Marks)**
- (b) Operating Profit **(01 Mark)**
- (c) Stocks **(01 Mark)**
- (d) Share Capital **(01 Mark)**
- (Total 30 Marks)**

**Question No. 02 (20 Marks)**

- (i) A factory's normal production capacity was 20,000 units. It produced 19,000 units during the month of December 2006.

Production cost details are as follows:-

	<b>Rs.</b>
Direct material @ 5Kg per unit	100
Direct Labour @ 6 hrs per unit	60
Monthly variable production overheads	400,000
Monthly fixed production overhead	800,000

Find the cost of conversion as per SLAS 5 (revised 2005) **(04 Marks)**

- (ii) (a) What do you mean by a "qualifying asset"? **(01 Mark)**
- (b) B company has constructed an office building for which it has obtained a bank loan of Rs. 2,000,000 on January 01, 2005. Interest is payable at 18% per annum. The repayable period of the loan will commence only after the occupation of the building is completed. You are given the following details.
- Technical and administration work prior to construction commenced on 01.03.2005.
  - Construction work commenced on 01.05.2005.
  - Construction work was completed on 31.05.2006.
  - Office building taken in to the usage of business on 01.07.2006.

**You are required to** compute the amount to be capitalized as borrowing cost of this construction under the Allowed Alternative treatment of SLAS 20 – Borrowing Cost

**(04 Marks)**

- (iii) Prudent Limited, an Investment Company, commenced its business activities during the year 2005/2006. Following is a part of its investment portfolio as at March 31, 2006. According to the nature of these investments, they are to be recognized as current investments.

Company	Sector	Cost	Market Value
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		Rs. '000	Rs. '000
A	Hotel	700	750
B	Hotel	1,300	1,240
C	Tourism	1,220	1,280
D	Tourism	1,500	1,450
E	Plantation	1,600	1,300
F	Plantation	640	960
G	Manufacturing	1,200	1,400

What are the different methods available for valuation of above investments in accordance with SLAS 22 ? Compute the value of investments based on those different methods. **(05 Marks)**

- (iv) You are requested to calculate basic Earning Per Share (EPS) of X Limited based on the information given below for the year ended March 31, 2006.

	Rs.'000
Net Profit before Taxation	8,400
Taxation	(1,680)
Net profit after Taxation	6,720
<b>Deduct</b>	
Preference Share Dividends	(600)
Ordinary Share Dividends	(1,200)
Retained Profit for the year	4,920

Number of Shares on April 01, 2005

Preference 600,000

Ordinary 1,200,000

New Ordinary Shares issued on 01.10.2005 400,000

New Ordinary Shares issued on 01.01.2006 200,000

**(06 Marks)**  
**(Total 20 Marks)**

**Question No. 03 (20 Marks)**

Amal, Wimal and Kamal have been in partnership for several years sharing profits and losses in the ratio 2:1:1 respectively.

The partners have decided to convert the partnership into a limited liability company, Star (Pvt) Ltd. with effect from January 01, 2007, by taking over the assets and liabilities of the partnership excluding cash.

The partnership's financial year commences from April 01, each year.

The summarized balance sheet of the partnership of the partnership as at December 31, 2006 is given below.

Assets	Rs. '000
Office Equipment	900
Furniture & Fittings	520
Motor Vehicles	2,800
Inventories	1,660
Debtors	1,220
Bank Balance	300
	<u>7,400</u>
<b>Capital &amp; Liabilities</b>	

Partners Capital Account – Amal	1,600
Wimal	800
Kamal	600
Partners Current Account – Amal	80
Wimal	40
Kamal	80
Profit available for appropriation	3,220
Creditors	980
	<u>7,400</u>

- The partners are entitled to interest on capital accounts at 10% per annum. Amal, Wimal and Kamal are paid nominal salaries of Rs. 30,000/-, Rs. 24,000/- and Rs. 22,000/- per month respectively.
- The car used by Amal will be taken over by him for Rs. 1,200,000/-, the other vehicles and the other property, plant and equipment will be taken over by Star (Pvt) Ltd on the following revalued amounts.

	<b>Rs.</b>
Other Vehicles	2,500,000
Office Equipment	940,000
Furniture & Fittings	400,000

- A debtor for Rs. 100,000/- was identified as irrecoverable. All other debtors will be taken over by Star (Pvt) Ltd with a 10% provision for doubtful debts. Liabilities will be taken over as well with a provision of Rs. 150,000/- for any unaccounted liabilities.
- Star (Pvt) Ltd will issue 500,000 ordinary shares of Rs. 10 each at a premium of Rs. 2/- on the basis of 40%, 30% and 30% to Amal, Wimal and Kamal respectively.
- The partners have agreed to bring in cash to settle any outstanding obligations.

**You are required to :**

- (a) Prepare the necessary accounts to close the books of the partnership.

**(12 Marks)**

- (b) Prepare the opening balance sheet of Star (Pvt) Ltd. as at January 01, 2007.

**(08 Marks)**

**(Total 20 Marks)**

**Question No. 04 (20 Marks)**

The Summarised Balance Sheet of A Ltd and B Limited as at March 31, 2006 are given below.

	A Ltd (Rs. '000)	B Ltd (Rs. '000)
<b>ASSETS</b>		
<b>NON CURRENT ASSETS</b>		
<b>Property, Plant &amp; Equipment</b>		
Land	600	400
Other Property, Plant & Equipment	2,160	1,260
Accumulated Depreciation	(720)	(360)
	2,040	1,300
<b>Investments</b>		
Investments in B Ltd	1,440	-
Other Investments	120	200
	3,600	1,500
<b>CURRENT ASSETS</b>		
Inventories	1,560	1,350
Receivables	1,120	470
Current Account with A Ltd	-	640
Cash and Cash Equivalents	1,500	150
	4,180	2,610
<b>Total Assets</b>	<b>7,780</b>	<b>4,110</b>
<b>EQUITY AND LIABILITIES</b>		
<b>SHARE CAPITAL AND RESERVES</b>		
<b>SHARE CAPITAL</b>		
Ordinary Share Capital of Rs. 10/- each	2,400	800
12% preference Shares of Rs. 10/- each	800	400
	3,200	1,200
<b>RESERVES</b>		
Share Premium Account	560	120
General Reserves	720	360
Retained Profits	1,100	840
	2,380	1,320
<b>NON CURRENT LIABILITIES</b>		
18% Debentures	520	600
Bank Loans	400	-
<b>CURRENT LIABILITIES</b>		
Payables / Creditors	540	860
Current Accounts with B Ltd	480	-
Income Tax	260	130
	7,780	4,110

The following information is relevant:

- i. A limited has purchased shares of B Limited on April 01, 2003 as stated below.

72,000 Ordinary Shares at Rs. 18/-	1,296,000
12,000 Preference Shares at Rs. 12/-	144,000
	<u>1,440,000</u>

- ii. Balances of Reserve Accounts of B Limited as at April 01, 2003 were as follows.

Share Premium Account	Rs. 120,000
General Reserves	Rs. 140,000
Retained Profits	Rs. 100,000

- iii. During the year B Limited has sold stocks to the value of Rs. 600,000/- to A Limited at cost plus 20% margin of which 50% were still in the inventories as at 31.03.2006.
- iv. At the time of the acquisition, A Limited has considered the fair value of lands of B Limited as Rs. 600,000/-. This valuation is to be adopted in the consolidated financial statements.
- v. Inter company current accounts are not agreeing due to following reasons:
  - a. Inventories from B Ltd to the invoice value of Rs. 120,000/- was received by A Ltd only on 04.04.2006.
  - b. A cash remittance from A Ltd to B Ltd received by B Ltd only on 10.04.2006.
- vi. Goodwill should be accounted for as recommended by SLAS 25 (Revised 2004)

**You are required to prepare consolidated Balance Sheet as at March 31, 2006 of A Ltd and its subsidiary. (Total 16 Marks)**

**Question No: 05 (14 Marks)**

X Ltd's Balance Sheets as at March 31, 2005, and March 31, 2006 together with the income statement for the year ended March 31, 2006 is given below.

**X Limited., Balance Sheet**

	<b>31.03.2006 (Rs. Million)</b>	<b>31.03.2005 (Rs. Million)</b>
<b>NON CURRENT ASSETS</b>		
Property, Plant & Equipment	4,230.6	4,306.8
Investments	1.8	1.8
	<u>4,232.4</u>	<u>4,308.6</u>
<b>CURRENT ASSETS</b>		
Stocks	1,444.2	1,153.8
Debtors	815.4	764.4
Fixed and Call Deposits	112.8	417.6
Cash and Bank	46.8	25.2
	<u>2,419.2</u>	<u>2,361</u>
<b>Total Assets</b>	<b><u>6,651.6</u></b>	<b><u>6,669.6</u></b>
<b>EQUITY &amp; LIABILITIES</b>		
Share Capital	1,662.6	1,662.6
Other Reserves	3,111.6	3,111.6
Accumulated Losses	(307.8)	(449.4)
Shareholders Funds	<u>4,466.4</u>	<u>4,324.8</u>
<b>NON CURRENT LIABILITIES</b>		
Long Term Loans	845.4	1,128.0
Debentures	118.8	118.8
Deferred Liabilities	295.8	208.8
	<u>1,260</u>	<u>1,455.6</u>
<b>CURRENT LIABILITIES</b>		
Trade Creditors	67.8	50.4
Other Creditors	275.4	243.0
Dividends	274.8	176.4
Loans Payable within one year	283.8	309.6
Bank Overdraft	3.6	21.0
Other	19.8	88.8
	<u>925.2</u>	<u>889.2</u>
<b>Total Equity &amp; Liabilities</b>	<b><u>6651.6</u></b>	<b><u>6669.6</u></b>

## Income Statement for the year ended March 31, 2006

	<b>31.03.2006 (Rs. Million)</b>
Sales	3,077.4
Operating Profit	651.6
Other Income	33.0
Profit before Interest	684.6
Interest	(293.4)
Profit before Tax	391.2
Tax	-
Dividends	(249.6)
<b>Retained Profits</b>	<b><u>141.6</u></b>

The following information is also relevant.

- (a) Summary of Property, Plant & Equipment at 31.03. 2006.

	<b>Cost (Rs. Million)</b>	<b>Provision for Depreciation (Rs. Million)</b>
Balance at 01.04.2005	5,335.2	1,028.4
Additions	192.6	266.4
Disposals	(9.6)	(7.2)
Balance at 31.03.2006	5,518.2	1,287.6

- (b) Operating profits include Rs. 3.6 Million profit on sale of property, plant & equipment.
- (c) Deferred Liability Account is maintained for gratuity payment and the provision of Rs. 96 Million was provided during the year as additional provision.
- (d) Other Income account includes Rs. 30.6 Million interest received and the balance in the account is receipt of dividends.
- (e) “Loans payable within one year” account is maintained to show the short term portion of the long term loan. There were no any other additions to long term loans during the year.
- (f) Rs. 30 Million had been taken during the year as other loans.

**You are required to prepare Cash Flow Statement for the year ended 31.03.2006 for X Limited., SLAS (revised 1994) should be followed in presenting your answer.**

**(Total 14 Marks)**

End of Question paper