

**Society of Certified Management Accountants of Sri Lanka****Intermediate Stage  
March 2009 Examination**

**Examination Date :** 21<sup>st</sup> March 2009  
**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><u>Subject</u></b>	<b><u>Subject Code</u></b>
<b>Financial Accounting &amp; Reporting</b>	<b>(FAR / 601)</b>

**Question No.1 (18 Marks)**

The summarized Income Statements of Asanga Limited and Bandara Limited for the year ended 31<sup>st</sup> March 2008 were as follows.

	<b>Rs.'000</b>	
	<b><u>Asanga Ltd.</u></b>	<b><u>Bandara Ltd.</u></b>
Sales	62,500	25,470
Cost of Sales	(20,680)	(10,230)
<b>Gross Profit</b>	<b>41,820</b>	<b>15,240</b>
Other Income	2,980	2,070
Distribution Cost	(7,704)	(5,370)
Administrative Cost	(8,014)	(3,924)
Other Expenses	(1,870)	(932)
Financial Costs	(5,780)	(1,530)
<b>Profit Before Taxation</b>	<b>21,432</b>	<b>5,554</b>
Taxation	(6,300)	(1,720)
<b>Net Profit for the year</b>	<b>15,132</b>	<b>3,834</b>

The following were extracted from the Statements of Changes in Equity for the year ended 31/03/2008.

	<b>Rs. '000</b>	
	<b><u>Asanga Ltd.</u></b>	<b><u>Bandara Ltd.</u></b>
Retained Profit as at 01/04/2007	25,500	5,200
Profit for the year	15,132	3,834
Transferred to General Reserve	(1,200)	(600)
<b><u>Interim Dividends</u></b>		
Preference	(2,100)	(400)
Ordinary	(800)	(800)
<b><u>Proposed Dividends</u></b>		
Preference	(700)	(400)
Balance as at 31/03/2008	<b>35,832</b>	<b>6,834</b>

**The following information is relevant**

- (1) During the year Bandara Ltd. has sold goods to Asanga Ltd. at a selling price of Rs.6,400,000/- in which Bandara Ltd. had kept a margin of 20% on cost. Inventories of Asanga Ltd. included part of these stocks at invoiced value of Rs.1,800,000/-
- (2) Asanga Ltd. has acquired 70% of ordinary shares and 40% of preference shares of Bandara Ltd. on 01<sup>st</sup> April 2006 when the retained profit of Bandara Ltd. was Rs.3,600,000/-.
- (3) Bandara Ltd. has granted a loan of Rs.4,000,000/- to Asanga Ltd. on 01<sup>st</sup> October 2007 for an interest rate of 18% per annum. Both Bandara Ltd. and Asanga Ltd. have not accounted for the interest on this loan.
- (4) During the year under review the following transactions have taken place.
  - (a) Bandara Ltd. has paid a monthly rent of Rs.60,000/- for the premises obtained from Asanga Ltd. on rent.
  - (b) Asanga Ltd. has paid a management fees of Rs.200,000/- on quarterly basis to Bandara.
- (5) Asanga Ltd. has accounted their Dividend income on the Accrual Basis.
- (6) An impairment test on goodwill carried out at the year end concluded that goodwill should be written down by Rs.60,000/-

**You are required to;**

- (i) The consolidate income statement for the year ended 31<sup>st</sup> March 2008. **(12 Marks)**
  - (ii) Change in consolidated retained reserve for the year ended 31<sup>st</sup> March 2008. **(6 Marks)**
- (Total 18 Marks)**

**Question No.2 (21 Marks)**

You are required to answer the following questions based on Sri Lanka Accounting Standards (SLAS)

- (a) (i) State five (5) criteria to be consider in capitalizing Development Costs as per SLAS 37. **(2 Marks)**
- (ii) A company has incurred a Research Cost amounting to Rs.300,000/- and Development Cost amounting to Rs.900,000/- during the year 2006 / 2007. The company is of the view that the product improved by incurring development cost can be sold during the next five (5) financial years. The expected sales quantity for the next five year is 270,000 Nos. During the year 2007 / 2008 the company has sold 30,000 Nos. in quantity. How do you show these cost in the Financial Statement for the years 2006 / 2007 and 2007 / 2008. **(2 Marks)**
- (b) (i) What are the assets eligible for capitalization of borrowing cost? Give two (2) examples of such assets. **(2 Marks)**
- (ii) What is the Benchmark treatment in accounting for borrowing costs? **(1 Mark)**
- (iii) If a company capitalizes its borrowing cost under the allowed alternative treatment in SLAS 20 at what point does the cessation of capitalization takes place? **(2 Marks)**

- (c) (i) SLAS 12 identifies two categories of events after the Balance Sheet date. You are required to explain the two categories and give examples for each of them. **(3 Marks)**
- (ii) 'X' Ltd. has prepared their Financial Statements for the year 2007 / 2008 and those Financial Statements have been authorized by the Board of Directors on 05<sup>th</sup> June 2008. What are the correct accounting treatments for the following events in accordance with the SLAS 12? **(5 Marks)**
1. A debtor value of Rs.400,000/- has been declared as bankrupt by a court decision given in the month of May 2008.
  2. A part of the Stocks had been sold by the company for Rs.400,000/- in the first week of May 2008 which had been valued at cost for Rs.500,000/- as at 31<sup>st</sup> March 2008.
  3. The Board of the company has declared a dividend of Rs.1,000,000/- for their Ordinary Shareholders.
  4. Buildings worth Rs.2,000,000/- has been destroyed by a fire occurred in the 16<sup>th</sup> of May 2008 and the relevant insurance claim would be 75% of the loss.
  5. An investment worth of Rs.3,000,000/- as at the Balance Sheet date has been revalued in the month of April 2008. It was revealed that the actual market value is limited to 40% of the costs.
- (d) (i) Plant cost in Rs.1,600,000/- on 01<sup>st</sup> October 2004 was initially estimated to have a useful life of eight (8) years with no residual value and was depreciated accordingly. During the year 2007 / 2008 it is revealed that the useful life time of the plant is only five (5) years. How do you consider this change and calculate the depreciation should be charged in the Financial Statements for the year 2007 / 2008. **(2 Marks)**
- (ii) As per SLAS 10 on what grounds does an entity change their accounting policies adopted through out the previous financial periods. **(2 Marks)**
- (Total 21Marks)**

**Question No.3 (28 Marks)**

The Trial Balance extracted from the Sakura Company books on 31<sup>st</sup> March 2008 is given below.

	<b>Rs. '000</b>	
	<b>Debit</b>	<b>Credit</b>
Ordinary Share Capital (2,000,000 Shares)		20,000
Share Premium (01.04.2007)		1,600
Retained Profit (01.04.2007)		11,800
Preference Share Capital		3,000
<b><u>Property, Plant &amp; Equipments</u></b>		
- Lands & Buildings (Land Rs. 9,600,000/-)	17,600	
- Furniture, Fittings & Equipment	6,400	
- Motor Vehicles	11,200	
<b><u>Provision for depreciation as at 01.04.2007</u></b>		
- Buildings		1,280
- Furniture, Fittings & Equipment		2,160
- Motor Vehicles		4,800
Sales		50,000
Cost of Sales	40,200	
Stocks	7,080	
Receivables/Payables	3,520	2,130
10% Convertible Debentures		4,000
12% Bank Loan		3,200
Administration Costs	5,640	
Distribution Costs	3,280	
Interest Paid	524	
Income Tax	1,600	
Provision for Tax as at 01/04/2007		130
Lease rentals Paid (140,000 x 12)	1,680	
Interim Dividend paid	1,000	
Investment (Costs)	2,000	
Cash & Cash Equivalents	2,376	
	<b>104,100</b>	<b>104,100</b>

**Following information is available.**

- (1) The company has acquired a Motor vehicle on a Finance Lease on 01<sup>st</sup> April 2007. The cost of Vehicle was Rs.4,200,000/-. As per the lease agreement, 36 monthly lease rentals should be paid at Rs.140,000/- each. The rental payments during the period 2007/2008 which includes an interest amounting to Rs.260,000/- has been debited to lease rentals paid account.
- (2) An equipment, purchased for Rs.800,000/- has been depreciated fully by end of the year 2006/2007. However no book entries had been made in this regard. New equipment has been purchased for Rs.400,000/- on 01<sup>st</sup> April 2007. Company depreciates Property, Plant and Equipment on Straight Line Method at following rates.

Buildings	5%
Furniture, Fittings & Equipment	10%
Motor Vehicles	25%

- (3) Analysis of the investments account is as follows;

	<u>Rs.</u>
Trade Investments	600,000
Long Term Investments	800,000
Fixed Deposits 18% (date of maturity 31.12.2009)	<u>600,000</u>
	<u>2,000,000</u>

The market value of the trade investments was Rs.700,000/- as at the Balance Sheet date. Market value of the long term investments is Rs.900,000/-. It is the company policy that to value their Current Investments / Trade Investments at Market Value.

- (4) Income Tax for the year 2006/2007 amounting to Rs.180,000/- was paid during the year 2007/2008. Income Tax liability for the year 2007/2008 has been ascertained as Rs.1,820,000/-.
- (5) Debenture interest is payable bi-annually on 30<sup>th</sup> September and 31<sup>st</sup> March each year. Interest for the 6 month ended 30<sup>th</sup> September 2007 has already been paid. The company has decided to convert 50% of Debenture with interest accrued thereon in to Ordinary Share with a consideration of Rs.12.50 per share as at 31<sup>st</sup> March 2008. Adjusting entries in this respect has not been incorporated in the accounts.
- (6) 12% of Bank Loan of Rs.4,000,000/- payable in 40 monthly equal installments, was obtained on 01<sup>st</sup> of April 2007. The first installment was paid on 31<sup>st</sup> August 2007 and thereafter installments have been paid by the company on regular basis with accrued interest.
- (7) Rs.180,000/- is to be written off as bad debts. Provision for doubtful debts is to be made at 10% on the balance outstanding as at end of the year.
- (8) The company has issued 100,000 new Preference shares at a consideration of Rs.30/- per share on 01<sup>st</sup> of October 2007. Preference Shareholders are entitled to a dividend of a Rs. 1.50 per share per annum. Interim Dividends shown in the trial balance represent the interim dividend paid to ordinary shareholders at Rs. 0.50 per share. The Directors have proposed a final dividend of Rs.1/- per share for their Ordinary Shareholders.
- (9) The company has signed an agreement with outside contractors to a value of Rs.5,000,000/- for their future capital constructions.
- (10) The following expenses are also included in the administration cost;

	Rs.
Auditors Remuneration and Expenses	120,000
Directors Remuneration	160,000
Donation	72,000

- (11) It is required to comply with the requirements of the new companies Act No. 07 of 2007 in the preparation of company's Financial Statements

**You are required to prepare for publication purpose;**

- (a) Income statement for the year ended 31<sup>st</sup> March 2008. **(9 Marks)**
- (b) The Balance Sheet of the Company as at 31<sup>st</sup> March 2008. **(7 Marks)**
- (c) The Statement of Changes in Equity for the year ended 31<sup>st</sup> March 2008. **(4 Marks)**
- (d) The Statement on movement of Property, Plant & Equipment. **(5 Marks)**
- (e) The relevant note. **(3 Marks)**

**(Total 28 Marks)**

**Question No.4 (19 Marks)**

A, B and C were in partnership sharing profits and losses in the ratio of 5:3:2 respectively. The extracted Balance Sheet as at 31<sup>st</sup> March 2008 is given below.

<u>Assets</u>	<u>Rs. '000</u>	
<b><u>Non Current Assets</u></b>		
<b><u>Property, Plant &amp; Equipments</u></b>		
Lands & Buildings	1,400	
Motor Vehicles	4,400	
Other PPE	8,320	
	<u>14,120</u>	
Investments	640	
Goodwill	360	
	<u>15,120</u>	
<b><u>Current Assets</u></b>		
Stocks	4,160	
Receivables	3,840	
Bank & Cash	480	8,480
<b>Total Assets</b>		<b><u>23,600</u></b>
<b><u>Equity &amp; Liabilities</u></b>		
<b><u>Capital Accounts</u></b>		
A	3,360	
B	2,400	
C	1,920	7,680
		<u>7,680</u>
<b><u>Current Accounts</u></b>		
A	720	
B	560	
C	300	1,580
		<u>9,260</u>
Profit for the year 2007/2008		3,360
		<u>12,620</u>
<b><u>Non Current Liabilities</u></b>		
Bank Loans	2,400	
Loan - B	1,600	4,000
		<u>4,000</u>
<b><u>Current Liabilities</u></b>		
Payables	5,280	
Accruals	1,700	6,980
		<u>6,980</u>
<b>Total Equity &amp; Liabilities</b>		<b><u>23,600</u></b>

The partners have decided to convert their partnership in to a Limited Liability Company in order to expand their business. For this purpose they have registered ABC (Pvt.) Ltd., which acquires assets of the partnership excluding investment and Goodwill. The Company acquires all liabilities excluding B's loan account.

**You are given following additional information.**

- (1) A motor vehicle with a carrying value of Rs.800,000/- was disposed for Rs.900,000/-. An amount received by realization of investment was Rs.800,000/-. The partnership paid Rs.1,440,000/- to settle B's Loan account fully. The expenditure incurred in connection with the closing of the partnership was Rs.64,000/-. The partnership had to pay Rs.320,000/- as compensation for their employees, who will be discontinued.
- (2) The partners are entitled to an interest of 5% per annum on their capital balances. All the partners are entitled to a salary of Rs.24,000/- per month per partner.
- (3) Income Tax on the divisible profit of the partnership for the year ended 31<sup>st</sup> March 2008 was ascertained as Rs.412,000/-. The Income Tax paid by the partnership on Self Assessment basis for the year amounting to Rs.160,000/- has been included in the receivables. Partner 'A' agreed to pay the balance tax liability on behalf of the partnership for the year ended 31<sup>st</sup> March 2008.
- (4) The new company agreed to allot 400,000 Ordinary Shares at Rs. 22/- and 120,000 Preference Shares at Rs. 18/- to the partnership to settle the purchase consideration.
- (5) After the incorporation, ABC Limited decided that the assets of the partnership will be taken to books of the company at following values.

	<b>Rs.'000</b>
Land & Buildings	2,000
Other Motor Vehicles	3,200
Other PPE	8,800

Other assets are to be taken to the books of the company at their book values. It is also decided to make a 10% provision for the doubtful debts on receivables. Further it was agreed to make a provision of Rs. 600,000/- as the retiring gratuity in the books of the company.

- (6) In addition to the shares allotted to the partners, ABC Limited issued 200,000 Ordinary Shares of Rs. 24/- and 40,000 Preference Shares at Rs. 20/- in order to enhance their liquidity position. The company has incurred a cost of Rs.132,000/- for the incorporation activities.

**You are required to prepare:**

- (a) Ledger Accounts of ABC partnership **(12 Marks)**
  - (b) Opening Balance Sheet of ABC (Pvt.) Ltd. **(7 Marks)**
- (Total 19 Marks)**

**Question No.5 (14 Marks)**

The summarized Income Statement for the year ended 31/03/2008 and the Balances of Current Assets and Liabilities as at 31/03/2008 of 'X' Limited are given below.

	<b>Rs. '000</b>
Sales	53,000
Cost of Sales	(33,600)
Gross Profit	<u>19,400</u>
Expenses	(10,200)
Profit before Taxation	<u>9,200</u>
Income Tax Expense	(2,400 )
Profit After Tax	<u>6,800</u>
Proposed Dividends	(1,000 )
Retained Profit	<u><u>5,800</u></u>

Expenses shown in the Income Statement include depreciation for PPE of Rs.1,120,000/- and interest expense of Rs.600,000/-.

	<b><u>Rs. '000</u></b>	
<b>Current Assets &amp; Liabilities as at</b>	<b>31.03.2008</b>	<b>31.03.2007</b>
Stocks	2,560	2,240
Trade & other Receivables	1,680	1,820
Cash & Cash Equivalent	1,570	960
Trade & Other Payables	1,040	860
Accrued Expenses	420	560
Income Tax payables	1,040	500
Dividend payables	1,000	-
Accrued Interest	350	400

Using the indirect method as specified in SLAS 09, prepare a segment of Cash Flow Statement to show the Cash Flows of operating activities for the year ended 31<sup>st</sup> March 2008.

**(Total 14 Marks)**

End of Question Paper

---