 Serial No.……………….

Institute of Certified Management Accountants of Sri Lanka
Operational Level
November 2012 Examination

Examination Date :	10th November 2012	**Number of Pages :**	11
Examination Time:	9.30 a:m. – 12.30 p:m.	**Number of Questions:**	07

Instructions to Candidates

1. Time allowed is **three (3) hours.**
2. Total: **100** Marks
3. Answer **all** questions in Part I and **four (4)** questions from Part II selecting **two (2)** question from each of the Sections **A** and **B**.
4. The answers should be in **English Language.**

Subject	Subject Code
Financial Accounting and Reporting	**(FAR / OL 2 – 202)**

PART I

Question No. 01 (20 Marks)

Answer all parts of the Question No.1. Select the most correct answer to each part of the question. Write the number of the part of the question and the selected answer by stating the relevant English letter, in your answer booklet. **E.g. (1) (relevant English letter), (2) (relevant English letter) etc….**

(1) Which of the following statements is false relating to qualitative characteristics of accounting information?
  (1) Information has the quality of relevance when it influences the economic decisions of users.
  (2) Information has the quality of reliability when it is free from material error and bias and can be depended upon by users.
  (3) The relevance of information is not affected by its nature and materiality even though its reliability is affected.
  (4) Qualitative characteristics are the attributes that make the information provided in financial statements useful to users.

(2) The following are few cost items relating to a plant acquired by a business.
  (i) Cost incurred to maintain the operations of plant under good condition.
  (ii) Initial delivery and handling cost of plant.
  (iii) Cost of fixing spare parts while the machinery used for operation.
  (iv) Cost of preparing the site prior to fixing the plant.

  Which items should be capitalized to the cost of the plant?
  (a) (ii), (iii) & (iv) only
  (b) (i), (ii) & (iv) only
  (c) (i) and (iv) only
  (d) (ii) & (iv) only

(3) The value of a construction contract is Rs.6,000 million. Cost incurred up to the 1st year end was Rs.3,600 million. It is estimated that a cost of Rs.3,400 million to be incurred to complete the contract. The percentage of works completed up to the end of the 1st year is 55%. Contract profit/ (loss) for the 1st year would be;

(a) Rs.1,320 million
(b) Rs.(1,000) million
(c) Rs.3,300 million
(d) Rs.(550) million

(4) X PLC purchased a machine for Rs.8,000,000/- on 01st April 2011 and commenced using it on the same day. The machine has an estimated life of 8 years. The compressor of the machine which had a value of Rs.1,600,000/- would need replacement every 4 years. What is the amount to be charged as depreciation for the year ended 31st March 2012?

(a) Rs. 6,000,000
(b) Rs. 2,000,000
(c) Rs. 1,500,000
(d) Rs. 1,200,000

(5) Bank statement of Sampath Ltd. shows a credit balance of Rs.766,000/- as at 31st March 2012. The following were noted by the accountant on his review of cash book and the bank statement for the month of March 2012.

- Cheques not presented to the bank – Rs.474,000/-
- Receipt from a customer amounting to Rs.100,000 has been recorded in the credit side of the cash book.
- Unrealized deposits – Rs.249,500/-.
- The bank has dishonoured a customer’s cheque for Rs. 110,000/- and has charged a bank charge of Rs.2,000/-. However, these entries have not been recorded in the cash book.
- Bank Statement shows a bank charge of Rs.7,000/- which has not been recorded in the cash book.

What is the cash book balance of Sampath Ltd. as at 31 March 2012 prior to making any relevant adjustments relating to the above?

(a) Rs. 1,071,500
(b) Rs. 560,500
(c) Rs. 460,500
(d) Rs. 971,500

(6) The following information is available to you about the receipts and sales of stock item “X” for the month of January 2012.

Date	**Receipts**	**Sales (Units)**
01.01.2012	500 @ Rs. 20 per unit	Nil
05.01.2012	1,200 @ Rs. 22 per unit	Nil
14.01.2012	Nil	600
17.01.2012	980 @ 24/40 per unit	Nil
19.01.2012	Nil	1,000
23.01.2012	570 @ 25/40 per unit	Nil
29.01.2012	Nil	500

If FIFO method of stock valuation was used, the cost of sales in the month of January would be:

(a) Rs. 50,212
(b) Rs. 46,160
(c) Rs. 50,262
(d) Rs. 49,252

(7) In determining the existence of an asset, the legal right of ownership is not essential. Which one of the following gives an example for this?

(a) Patents and copyrights.
(b) Accounts receivable balance.
(c) Freehold property, plant and equipment.
(d) Property held on finance lease.

(8) Which one of the following characteristics are essential to recognize a liability?

(i) Existence of probable future outflow of economic resources.
(ii) Existence of a legally binding debt.
(iii) It must have resulted from a past transaction or event.
(iv) Existence of a present obligation of the entity.

(a) (i), (ii) and (iii) only
(b) (i), (iii) and (iv) only
(c) (ii), (iii) and (iv) only
(a) All of the above

(9) Which one of the following should be excluded from the ascertainment of initial cost of property, plant and equipment as per LKAS 16?

(a) Installation Costs.
(b) Freight Charges of the assets.
(c) Cost of launching of new product through the Property, Plant & Equipment (PPE).
(d) Cost of site preparation.

(10) Which of the following should be considered as a change in the accounting policy?

(a) Depreciation rate of buildings has changed from 10% to 5%s.
(b) Depreciation method was changed from straight line to reducing balance method.
(c) Borrowing cost which was capitalized to assets now consider as expenses.
(d) Provision for doubtful debts made as 10% of the debtors has changed to 5%.

(10 × 2 Marks = Total 20 Marks)

End of Part I

PART II

Section A

Answer <u>any two (2)</u> questions

<u>Question No. 02 (20 Marks)</u>

The following Trial Balance relates to Merchant Ltd. As at 31st March 2012.

	(Rs.000)	**(Rs.000)**
Sales		295,000
Cost of Sales	151,100	
Distribution Cost	12,200	
Administration Cost	29,400	
Closing inventories as at 31/03/2012	6,600	
Finance Cost	2,300	
Property, Plant & Equipment	142,500	
Provision for Depreciation on PPE		30,400
Trade receivables	7,200	
Trade payable		3,600
Cash and bank balances	1,635	
Retained profit 01/04/2011		4,300
Stated Capital		20,000
Debentures interest income received		90
Ordinary share issue		4,550
Share issue expenses	180	
Investments – 12% debentures	1,545	
Other Expenses	1,800	
Taxes paid	2,740	
Provision for Doubtful debts		130
Provision for Income Tax		460
Provision for Trade warranties		350
Provision for Gratuity		320
	359,200	**359,200**

The following information is available.

(1) The company invited applications for 300,000 ordinary shares at Rs.14/- each. As at 31st March 2012 Merchant Ltd. allotted the shares due and no relevant accounting entries have been incorporated. The excess money received was refunded in April 2012.

(2) The company purchased 12% debentures of LB Ltd. on 1st July 2011 from the stock market and received interest income of Rs.90,000/- for the six months period ended 31st March 2012.

(3) Revenue includes an advance of Rs. 4.8 Million received from a customer for delivery of goods in April 2012.

(4) Finance cost includes a interim dividend of Rs.300,000/- paid in October 2011.

(5) Breakup of the property, plant & equipment is as follows (Rs. '000)

	Cost	Accumulated Depreciation as at 01/04/2011
Lands	40,000	-
Buildings	52,000	17,400
Motor Vehicles	20,000	3,400
Office Equipment	18,500	5,600
Furniture & Fittings	12,000	4,000
	142,500	30,400

Company purchased office equipment at a cost of Rs. 3,200,000/- on 01/07/2011. On the same day the company acquired a new vehicle having a fair value of Rs.1,600,000/- by transferring an old vehicle purchased for Rs.2,000,000/- on 01/01/2010 as a full settlement. No relevant entries have been passed for the exchange of vehicle in the Books of Account.

(6) The company policy is to depreciate property, plant & equipment on straight line basis at the following rates:

Building	5%	per annum
Motor Vehicles	25%	per annum
Office Equipment	12.5%	per annum
Furniture & Fittings	15%	per annum

(7) All the lands of the company were revalued on 31.03.2012 by an independent professional value at a value of Rs. 50 Million and no necessary entries were incorporated to show the revalued amount of the lands.

(8) Provision for doubtful debts has to be adjusted as follows:

Specific provision	Rs. 60,000
General provision	5%

(9) Income Tax paid during the year included a payment of Rs.500,000/- for the year of Assessment 2010 / 2011. Income Tax for the current year has been estimated at Rs.3,000,000/-.

(10) The following provisions to be recognized as expenses during the year.

Trade warranties `	Rs. 150,000
General provision at	Rs. 170,000

During the year 2011 / 2012 the company has paid against provision for trade warranties and retiring gratuities Rs.90,000/- and Rs.60,000/- respectively. These payments have been included in the other expenses.

You are required to prepare the following statements for publication purpose:

(a) Statement of comprehensive income for the year ended 31st March 2012. **(08 Marks)**

(b) The statement of Financial Position of the company as at 31st March 2012. **(08 Marks)**

(c) The statement of changes in equity for the year ended 31st March 2012. **(04 Marks)**

(Total 20 Marks)

Question No. 03 (20 Marks)

On April 2011 Major Limited acquired 80% of the equity of Minor Limited for a consideration of Rs. 102 Million. On the date of the acquisition fair value of net assets of Minor Limited was ascertained as Rs. 80 Million. The retained earnings balance of Minor Limited stood at Rs 20 M at the date of acquisition. The stated capital of the Minor Limited is comprised of 3,200,000 numbers of shares. The non controlling interest as at the date of acquisition should be valued at Rs. 40/- per share. The summarized Balance Sheets of Major Limited and Minor Limited as at 31st March 2012 are given below:

	Rs. '000	
	Major Ltd.	**Minor Ltd.**
ASSETS		
Property, Plant & Equipment	147,200	97,400
Investment in 'B' Ltd.	102,000	-
Other Investment		10,000
Current Assets		
Inventories	72,000	38,800
Accounts Receivables	65,200	32,000
Cash & Cash Equivalents	18,400	12,200
Total Assets	**404,800**	**190,400**
EQUITY & LIABILITIES		
Stated Capital	165,200	44,000
Retained Earnings	72,400	29,000
NON CURRENT LIABILITIES		
Debentures	3,000	2,000
Bank Loans	1,200	800
CURRENT LIABILITIES		
Accounts Payables	52,800	23,400
Short-term Borrowings	110,200	91,200
Total Equity & Liabilities	**404,800**	**190,400**

The following information is relevant for the preparation of the Group Consolidated Balance Sheet.

(1) It was decided that any variation of carrying value and fair value of net assets of Minor Limited as at the date of Acquisition is due to increase in PPE which is subject to the depreciation at 20% p.a.

(2) Impairment test carried out on 31st December 2012 revealed that the goodwill on consolidation has impaired by Rs. 5 Million.

(3) Inventories of Minor Limited as at 31st March 2012 includes goods transferred from Major Limited as Rs. 22 Million. Major Limited retained a margin of 25% on cost, when goods are sold to Minor Limited.

(4) Major Limited transferred a plant which had a written down value of Rs. 8 Million to Minor Limited for Rs. 20 Million on 01st October 2011. Minor Limited estimated the plant to have a useful life of 5 years. Minor Limited depreciates its assets on the Straight Line basis.

(5) Minor Limited transferred cash amounting to Rs. 12 Million to Major Limited at the year end, which has not recognized in Major Limited books in the month of April 2012 as it was in transit at the balance sheet date. The inter Company transaction have been recorded in accounts receivable and accounts payable.

(6) A reconciliation of the current accounts which are included in accounts receivables and payables of the two companies showed that Minor Limited owed Major Limited Rs. 19 Million at the year end.

You are required to:

(a) Calculate the Goodwill arising on the acquisition of Minor Limited. **(04 Marks)**

(b) Prepare the Consolidated Statement of Financial Position of Major Limited Group as at 31st March 2012. **(16 Marks)**

(Total 20 Marks)

Question No. 04 (20 Marks)

(a) You are given below the Statement of Comprehensive Income for the year ended 31st March 2012 and the Statement of Financial Position as at 31st March 2012 of Sandalanka Ltd.

Statement of Comprehensive Income for the year ended 31st March 2012.

	(Rs. '000)
Sales	50,000
Cost of Sales	(24,000)
Gross Profit	26,000
Other income	1,000
Distribution Cost	(7,000)
Administrative Expenses	(5,200)
Finance Expenses	(700)
Profit before tax	14,100
Tax	(2,100)
Net Profit for the year	**12,000**
Other Comprehensive Income	
Revaluation of Lands (PPE)	**6,000**
Total Comprehensive Income	**18,000**

Statement of Financial Positions as at 31st March 2012 and 31st March 2011.

	2012 (Rs.'000)	**2011 (Rs.'000)**
Non-current Assets		
Land	45,000	20,000
Buildings	21,600	16,000
Motor Vehicles	14,400	24,000
Current Assets		
Stock	10,250	8,420
Debtors	12,600	10,940
Cash and bank	1,150	640
Total Assets	**105,000**	**80,000**

Equity and Liabilities		
Stated Capital	60,000	40,000
Revaluation Reserve	6,000	-
Retained profit	26,000	31,000
Non-current Liabilities		
Bank Loan	7,000	3,800
Current-Liabilities		
Creditors	5,160	4,700
Income tax payable	640	200
Accrued expenses	200	300
	105,000	**80,000**

The following additional information is also provided.

(1) Administrational expenses for the year included depreciation charges for Buildings – Rs.1,200,000/- and Motor Vehicles – Rs. 4,000,000/- for the year.

(2) The company sold a motor vehicle with a carrying value of Rs. 9,000,000/- for Rs.10,000,000/-.

(3) A bonus issue of shares was made on the basis of one share for every five shares held on 1st April 2011. Further, a new share issue was made to public at the end of the year.

(4) During the year Rs. 9,000,000/- dividend was paid to the shareholders.

(5) A new bank loan of Rs. 5,000,000/- was obtained during the year.

(6) Finance cost consists entirely of interest on loans. The accrued expenses balances in the balance sheets represents interest in accrued as at the year end.

You are required to prepare the cash flow statement for year ended 31st March 2012 using the Direct Method. **(10 Marks)**

(b) Based on the draft financial statement prepared by the accountant of Alpha Limited has shown an accounting profit of Rs. 6,850,000/- for the financial year ended 31st March 2012. The company's Income Tax rate for the year is 28%. During the year Rs. 435,000/- has been charged to the Income Statement as depreciation on PPE. However, as per the provision in the Income Tax law the depreciation amount can be claimed to compute the taxable income for the year is Rs. 1,285,000/-.

Assume that gratuity can be deducted when gratuities are paid to the employees.

	Rs.
Carrying Value of PPE at the end of year	4,450,000
Tax Base of PPE at the end of year	2,360,000
Carrying Value of Intangible Assets at the end of year	800,000
Tax Base of Intangible Assets at the end of year	0
Carrying Value of provision for retiring gratuity	1,450,000
Balance of deferred tax liability as at 01.04.2011	300,000

You are required to compute the tax expense for the year 2011 / 2012. **(10 Marks)**

(Total 20 Marks)

End of Section A

Section B

Answer <u>any two (2)</u> questions

<u>Question No. 05 (20 Marks)</u>

(a) The Balances of stated capital and reserves accounts as at 01st April 2011 of CD Limited were as follows.

	Rs'000
Stated Capital - Ordinary Shares (200,000 shares)	12,000
Stated Capital - Preference Shares (80,000 shares)	4,000
Revaluation Reserve	1,800
General Reserve	3,600
Retained Profit	3,000

The following Additional information is provided.

(1) The company has issued 80,000 new ordinary shares and 50,000 preference shares at Rs.50/- and Rs.35/- respectively during the year under review. Applications were received by the company for 90,000 ordinary shares and 45,000 preference shares. The company has allotted the shares after refunding the excess application money.

(2) The company has made a bonus issue of one (1) share to every ten (10) ordinary shares held as at beginning of the year. The consideration per bonus share was Rs.35/-.

(3) The property, plant and equipment of the company was revalued during the year end resulted a surplus of Rs.2,800,000/- and the revaluation surplus credited to the comprehensive income was Rs,5,400,000/-.

(4) The company has paid following net dividends after deducting 10% dividend tax.

	Rs.
Preference Shares	162,000
Ordinary Shares	360,000

(5) The Board of Directors of the Company has proposed;

a. To transfer Rs.500,000/- to General Reserve.
b. To declare a final dividend to preference share holder Rs.400,000/- and ordinary share holder Rs.500,000/- respectively.

You are required to prepare the Statement of the Changes in Equity for the year ended 31st March 2012 of CD Limited. **(10 Marks)**

(b) Following information has been extracted from the books of Maga Limited for the year ended 31st March 2012.

Interest Cost incurred during the year ended 31st March 2012

	Rs.
Long-term Borrowings	900,000
Short-term Borrowings	480,000
Finance Lease	66,000
Overdraft Interest	34,000
Other Interest	53,000

It has revealed that the long term borrowings have been obtained solely for the purpose of financing the construction of the office complex of the company. Due to shortage of funds the company has utilize 50% of the short term borrowings also for the completion of the above office complex. The total construction cost including the borrowing cost incurred in the previous year has been accumulated to the building work in progress account at the beginning of the year Rs. 7,235,000/-. During the year 2011/2012 the company has incurred a further cost of construction of the office complex amounting to Rs. 950,000/-. The construction works of the office complex completed on 30th November 2011. However, the company commenced the usage of office complex on 01st January 2012. The depreciation rate for the building is 5% per annum.

You are required to:

(i) Interest cost that should be recognized as an expense for the year ended 31st March 2012.

(ii) Interest cost that should be capitalized recognized for the year ended 31st March 2012.

(iii) The carrying value of the office complex as at 31st March 2012. **(10 Marks)**

(Total 20 Marks)

<u>Question No. 06 (20 Marks)</u>

(a) State whether the following items as investment properties as per LKAS 40 (Investment Property)?

(i) Land held for capital appreciation.
(ii) Property intended for sale in the ordinary course of business.
(iii) Building being constructed on behalf of a third party.
(iv) Land held for a currently undetermined future use.
(v) Building being constructed for future use as investment property.

(10 Marks)

(b) A company has spent Rs. 100 M in developing a new product. The company has confirmed based on a comprehensive feasibility study and a market survey carried out by a professional firm that the product could be manufactured on a large scale basis and in the next 5 year period it has a good demand in the market. The company has forecasted the net profits from the product before writing off the development cost are as follows;

Year	Profit before Amortization of Development cost (Rs. M)
1	24
2	16
3	12
4	10
5	08

You are required to explain the accounting treatment for the development cost incurred in the current year. **(10 Marks)**

(Total 20 Marks)

<u>Question No. 07 (20 Marks)</u>

(a) State 3 differences between a finance lease and an operating lease. **(03 Marks)**

(b) An entity that enters into any contingent liability after the year end should be disclosed in the Finance Statements. State (03) three such contingent liabilities. **(03 Marks)**

(c) List (04) four criteria to be considered when development costs are capitalized. **(06 Marks)**

(d) Distinguish the following terms.
   (i) Carrying Value & recoverable Amount. **(04 Marks)**
   (ii) Depreciation & amortization. **(04 Marks)**

(Total 20 Marks)

End of Section B

End of Part II

End of Question Paper