UNIVERSITY OF COLOMBO, SRI LANKA
FACULTY OF MANAGEMENT AND FINANCE

Bachelor of Business Administration (Level I - Semester IV) Examination – November, 2018

ACT 2311 – Advanced Financial Accounting

Three (03) Hours

Answer any Five (05) Questions

Use of calculators is permitted
Show all your workings clearly
Assumptions (if any) should be clearly stated

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1. i. Briefly explain the components of short-term employee benefits.

(05 Marks)

ii. Explain the accounting treatment that should be done under Fair Value Model for the following investment property transfers.

a. A transfer from investment property to owner-occupied property
b. A transfer from investment property to inventories
c. A transfer from owner-occupied property to investment property
d. A transfer from inventories to investment property

(08 Marks)

iii. An entity sells goods with a warranty under which customers are covered for the cost of repairs of any manufacturing defects that become apparent within first six months after the purchase. If minor defects were detected in all products sold, repair costs of Rs. 800,000 would result. If major defects were detected in all the products sold, repair costs of Rs. 1,600,000 would result.
The entities past experience and future expectations indicate that for the coming year, 80% of the goods sold will have no defects, 14% will have minor defects and 6% will have major defects.

a. What is the value of provision to be made for the warranty?

(03 Marks)

b. During the year if 75% claimed for minor defects (from the expected value for minor defects) and 20% claimed as major defects (from the expected value for major defects), what are the journal entries to be entered?

(04 Marks)

(Total 20 marks)

2\. i. ABC Ltd leased a heavy machine which has a useful life of 10 years from CDB Finance Co. CDB Finance Co. is willing to transfer the legal ownership of this machine to ABC Ltd at the end of the lease term. The agreement consists of the following terms:

Lease Term	5 years
Annual Rental	Rs. 120,000
Guaranteed Residual Value	Nil
Interest Rate	15%
FV (at Beginning)	Rs. 540,000

You are required to;

a. Determine the type of Lease.

(02 Marks)

b. Calculate the cost to be recognized in ABC Ltd's books.

(02 Marks)

c. Separately identify the interest and capital amounts of the lease in each instalment using the Actuarial Method.

(04 Marks)

d. Record the above transactions in ledger accounts of both ABC Ltd. and CDB Finance Co.

(12 Marks)

(Total 20 marks)

3\. i. State whether each of the following asset can be categorized as an Investment Property. Provide reasons for your answers.

a. Held under a finance lease and to be leased out in future under an operating lease.
b. Held for sale in the ordinary course of business.
c. Properties rent out for employees.
d. Owned by the company and leased out under an operating lease.
e. Held under a finance lease and leased out under a finance lease.

(05 Marks)

ii. Briefly describe the accounting treatment that should be made for Contingent Assets and Contingent Liabilities.

(04 Marks)

iii. Explain the characteristics of Intangible Assets.

(06 Marks)

iv. According to LKAS 19, post-employment benefits can be classified as defined contribution plan and defined benefit plan. Briefly explain the recognition and measurement of each above plans.

(05 Marks)

(Total 20 marks)

4. i. Head office of Serendib PLC is in Colombo and its branch is located in Male Island, the Maldives. Summarized Trial Balance of the Male branch as at 31st March 2018 is given below.

	MR. values	
	Dr	Cr
Plant, Equipment & Furniture	135,000	
Provision for Depreciation 01/04/2017		13,500
Stock 01/04/2017	44,000	
Purchase	254,000	
Goods from Head office	71,000	
Salaries	8,100	
Transport / Carriage inwards	1,900	
Sales		385,300
Rent & Rates	2,800	
Insurance	1,900	
Sales expenses	2,700	
Head office account		147,500
Debtors/ Creditors	30,300	13,500
Cash at bank	4,200	
Cash in hand	3,900	
	559,800	559,800

Additional information:

- The functional currency of Serendib PLC is LKR whereas Male branch currency is MR.
- Male branch stock at 31st March 2018 is valued to MR 38,200.
- Salaries payable of the Male branch at 31st March 2018 is MR 1,900.
- Prepaid insurance of Male branch at 31st March 2018 is MR 500.
- Provision for depreciation on Plant, Equipment & Furniture is 10% per annum on cost.
- The balance of the Male branch current account at the Head office is LKR 437,500.
- Foreign exchange rates are:
  31/03/2018 1 MR = 4.40 LKR
  01/04/2017 1 MR = 3.80 LKR
  Average for the period is 1 MR = 4.10 LKR
  Spot exchange rate at the date of acquisition of Plant, Equipment & Furniture was 1 MR = 4.10 LKR

You are required to convert the Male branch Trial Balance as at 31/03/2018 into Head office reporting currency of LKR.

(10 Marks)

ii. A Telecom Company has acquired a 4G license. The license could be sold or licensed to a third party. However, the management intends to use it to operate a wireless network. Development of the network starts when the license is acquired. Should borrowing costs on the acquisition of the 4G license be capitalized until the network is ready for its intended use? Provide reasons for your answer.

(05 Marks)

iii. A Real Estate Company has incurred expenses for the acquisition of a permit allowing the construction of a building. It has also acquired equipment that will be used for the construction of various buildings. Can borrowing costs on the acquisition of the permit and the equipment be capitalized until the construction of the building is completed? Why?

(05 Marks)

(Total 20 marks)

5. i On 1st January 2017, X Ltd acquired 6,000,000 ordinary shares of Y Ltd where the total number of ordinary shares of Y Ltd was 8,000,000 (Rs.1/- each). As at the date of acquisition, Y Ltd had a Retained Earnings balance of Rs.2,000,000 and there were no other reserves. The consideration was paid by X Ltd in the following means:

- Immediate cash payment of Rs.5,000,000/-
- A share issue at 1:10 rate (The market prices of shares of X Ltd and Y Ltd were Rs.3/- and Rs.1/- respectively)
- A balance cash payment of Rs.1,500,000 on 31st December 2017 (The respective discount rate would be 15%).

The Non-Controlling Interest was measured proportionately to the net assets of Y Ltd at the acquisition date. For the acquisition process X Ltd had to pay a Rs.250,000 legal fee.

Using the above information, you are required to calculate;

a. Purchase consideration, and
b. Goodwill.

(You may round-up the figures to nearest 1,000 rupees)

(05 Marks)

ii. Plato Ltd acquired 80% of the equity of Sun Ltd on 1st April 2017 by paying a consideration of Rs. 55 Mn.

Given below are the Income Statements of Plato Ltd and Sun Ltd for the year ended 31st March 2018.

	Plato Ltd	Sun Ltd
	Rs. '000	**Rs. '000**
Revenue	68,000	52,000
Cost of Sales	(35,000)	(27,500)
Gross Profit	**33,000**	**24,500**
Other Income	5,800	4,300
Administrative Expenses	(11,200)	(8,400)
Finance Expenses	(4,900)	(3,800)
Profit Before Tax	**22,700**	**16,600**
Tax Expense	(6,300)	(4,600)
Profit for the year	**16,400**	**12,000**
Dividend Expenses	(6,000)	(4,400)
Retained Profit for the year	**10,400**	**7,600**

Additional information is given below (all figures are in Rs.'000):

- During the year, Sun Ltd sold goods to Plato Ltd at a value of Rs. 12,000 by keeping a profit margin of 20%. By the year end, Plato Ltd had sold only 70% of these goods.
- On 01st August 2017, Sun Ltd sold office equipment to Plato Ltd by keeping a profit of Rs. 1,200. The group depreciates its office equipment at 25% per annum.
- Plato Ltd has settled a telephone bill of Sun Ltd amounting Rs. 250. Plato Ltd has recorded for this as their expense and Sun Ltd has not recorded for it.
- Plato Ltd and Sun Ltd declared and paid Rs. 6,000 and Rs. 4,400 respectively as the dividends to equity shareholders during the year. Plato Ltd had recognized the dividend received from Sun Ltd in other income.

Prepare the Consolidated Income Statement for the Plato-Sun Group for the year ended 31st March 2018.

(15 Marks)

(Total 20 marks)

6. Extra Ltd acquired Small Ltd on 01st January 2017 by purchasing Rs. 6,000,000 equity share capital of Small Ltd. For this Extra Ltd paid Rs. 10,000,000 cash immediately. On the acquisition date, the fair value of a depreciable fixed asset of Small Ltd had been increased by Rs. 600 which is depreciable at 20% per annum.

Following are the Statements of Financial Positions of two companies as at 31st December 2017.

	Extra Ltd	Small Ltd
	Rs. '000	**Rs. '000**
Assets		
Non-Current Assets		
Property Plant and Equipment	19,500	16,600
Investment in Small Ltd	10,000	-
Current Assets		
Inventory	6,500	4,200
Trade Receivables	3,900	2,700
Other Receivables	2,300	1,850
Cash and equivalents	6,750	4,150
	48,950	**29,500**
Equity and Liability		
Equity		
Share Capital		
- Ordinary shares (Rs.1/- each)	22,000	10,000
Retained Earnings	12,500	7,800
Non-Current Liabilities		
Term Loan	8,700	5,200
Current Liabilities		
Dividend Payable	-	2,000
Trade Payables	4,800	2,400
Other Payables	950	2,100
	48,950	**29,500**

Additional information (all figures in Rs. 000):

- Non-Controlling Interest at the acquisition is valued at its proportion of net assets.
- Retained Earnings of Small Ltd for the year 2017 was Rs. 3,600.
- During the year, Extra Ltd Ltd sold goods to Small Ltd at a value of Rs. 4,000, by keeping a profit mark-up of 30% on selling price. Only half of these goods have been sold by the year end.
- On 01st July 2017, Small Ltd sold office furniture to Extra Ltd at a price of Rs. 2,500 when the carrying amount was Rs. 3,000. The group of companies depreciates its office furniture at 20% per annum.

- Extra Ltd has lent Rs. 800 to Small Ltd during the year and charged an interest of Rs. 120. By the year end, Small Ltd had a total payable of Rs. 300 to Extra Ltd. Both the companies have recorded for this transaction (both capital and interest) in their books.
- Small Ltd declared Rs. 2,000 of dividends to all of its' ordinary shareholders in this year and it is not yet paid out though it is recorded in its' books as an expense and dividends payables. Extra Ltd has not accounted this yet.
- At the year-end, goodwill has been impaired by Rs. 700.

You are required to prepare Consolidated Statement of Financial Position of the above group as at 31st December, 2017.

(20 marks)