



UNIVERSITY OF COLOMBO, SRI LANKA
FACULTY OF MANAGEMENT AND FINANCE

Bachelor of Business Administration (Level I - Semester II) Examination 2016

ACT 1200 – Advanced Financial Accounting

Two (02) Hours

Answer Any Four (04) Questions

Instructions to Candidates:

- Use of calculators is permitted
 - Show all your workings clearly
 - Assumptions (if any) should be clearly stated
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Question 01

- i. Explain the 'substance over-form' concept of leases, referring to LKAS 17.

(05 Marks)

- ii. Determine the type of leases for each of the scenario given below with justifications for your answer.

Assume the useful lifetime of the assets in all the cases is 10 years.

- (a) The lease agreement is for 8 years. Present value of minimum lease payment (PV of MLP) is Rs. 624,000 and the fair value of the asset at the inception is Rs. 720,000.
- (b) Lessee has to bear all the maintenance costs and insurance costs of the asset during the lease term of 5 years.
- (c) The lease agreement is for 10 years. However, the lessee has to return the asset to lessor at the end of the lease term.
- (d) Lease term is 9 years. However, as per the agreement, the lessor has the right to waive the agreement in advance by a six month notice.
- (e) Lease term is 4 years. The ownership of the asset is not transferred to the lessee automatically unless s/he is willing to pay the discounted price set by the lessor.

(10 Marks)

- iii. Sisil PLC leases an asset on 01st January 2015 to Nevil Pvt Ltd. In terms of the lease agreement an initial non refundable deposit of Rs.2 Mn, followed by four annual payments of Rs.2 Mn commencing from 31st December 2015 is to be paid. The fair value of the asset is equivalent to the present value of minimum lease payment on 1st of January 2015. The discount rate relevant to this transaction is 10%.

You are required to calculate following in the books of Nevil Pvt Ltd ;

- (a) Present value of minimum lease payment for the above lease transaction.
(04 Marks)
 - (b) Annual interest expense for all four years, using Acturial Method.
(04 Marks)
 - (c) Liability to be shown in the Statement of Financial Position as at the end of each year.
(02 Marks)
- (Total 25 marks)**

Question 02

- i. State the components of Borrowing Cost as per LKAS 23.
(03 Marks)
- ii. ABC construction (Pvt) Ltd starts construction of a qualifying asset on 1st of January 2015. It is anticipated that it will take 5 years to complete. The company borrows Rs. 500 Mn to fund the asset and deposits all excess funds in a bank during the year ended on 31st December 2015.

The company has;

- incurred Rs.25 Mn interest expense on the borrowings,
- received Rs.5 Mn interest income on deposits and,
- incurred Rs.40 Mn of construction costs in relation to the qualifying asset.

How much interest should ABC construction (Pvt) Ltd capitalise in respect of this qualifying asset as at 31 December 2015?

(05 Marks)

- iii. LKAS 11 prescribes the Accounting treatment of revenue and costs of Constructions Contracts. By referring to this standard,
 - (a) Differentiate between two main types of construction contracts.

(04 Marks)

- (b) Explain the decision criterion to recognize the revenue and costs of the construction contract.

(05 Marks)

- iv. N & M constructors undertook a building contract for a individual customer and finished it before the deadline stipulated. The related revenue and costs are given below.

Estimated revenue Rs. 850,000

Additional price for the extra work approved by the customer Rs. 45,000

Site labour cost Rs. 180,000

Material cost Rs. 265,000

Costs of design directly related to the contract Rs. 120,000

General administrative cost not reimbursable Rs. 15,000

Depreciation of Property Plant and Equipment used for the construction Rs. 30,000

Allocated overhead towards cost of construction Rs. 55,000

Environment Levy paid (Reimbursible from the customer) Rs. 20,000

Sales and distribution cost Rs. 10,000

(Incentives for early completion is 10% of the initial contract price.)

Calculate the total revenue and cost of the cotract using the above information.

(08 Marks)

(Total 25 marks)

Question 03

- i. Differentiate between Investment property and Owner-occupied property.
- (03 Marks)
- ii. Explain the 'dual purpose property concept'.
- (03 Marks)
- iii. Tecno (Pvt) limited rented out a property to a third party for Rs.2,000,000 on 1st of January 2015. The property comprises a land and a building. The cost of the land is Rs.800,000 and the buildings is expected to have a useful life of 60 years. At 31st of December 2015, property indices suggest that the fair value of the property has risen to Rs.2,250,000.

Compute the property value presented in the financial statements as at 31st December 2015 if company adopted the following models.

- (a) Cost model
- (b) Fair value model

(06 Marks)

- iv. Taiko (Pvt) limited sold Rs. 140,000 of kitchen appliances on 15th of August 2016 under a six months warranty. The cost of repairing defects during the warranty period is estimated at 6% of the selling price. On 11th of September 2016, company incurred Rs.2000 for part replacement and Rs.3000 for labour cost on repairs under the warranty.

Provide journal entries for;

- (a) The estimated warranty expense as at 31st of August 2016
- (b) The transaction occurred on 11th of September 2016

(04 Marks)

- v. Explain key characteristics of intangible assets.

(05 Marks)

- vi. Define contingent liabilities providing examples.

(04 Marks)

(Total 25 marks)

Question 04

Promo (Pvt) Ltd acquired 70% of the ordinary shares of S & T Ltd on 1st of January 2015. The Statements of Comprehensive Income of two companies for the year ended on 31st December 2015 are given below.

	Promo (Pvt) Ltd	S & T Ltd
Sales	3,400,000	800,000
Cost of Sales	(2,050,000)	(350,000)
Gross Profit	1,350,000	450,000
Other Income	190,000	80,000
Administrative Expense	(448,000)	(86,000)
Finance Expense	(392,000)	(18,000)
Profit Before Tax	700,000	426,000
Tax Expense	(84,000)	(51,120)
Profit for the year	616,000	374,880
Dividends	(195,000)	(140,880)
Retained Profit for the year	421,000	234,000

Additional Information:

1. Total Sales made by S & T Ltd to Promo (Pvt) Ltd during the year was Rs. 900,000. S & T Ltd set the selling price with a markup of 25% on cost. At the end of year, Promo (Pvt) Ltd has 30% of these goods remaining unsold.
2. During the year S & T Ltd has granted a short-term loan to Promo (Pvt) Ltd and has received Rs. 18,000 of interest by 31st December 2015.
3. On 1st of April 2015, Promo (Pvt) Ltd sold a machine to S & T Ltd for Rs.560,000. On this date the carrying amount of the machine was Rs. 500,000. (Assume depreciation rate of the group is 15% p.a.)
4. S & T Ltd has settled an electricity bill of Promo (Pvt) Ltd amounting to Rs 25,000. This is included in administrative expenses of Promo (Pvt) Ltd.
5. Other income of Promo (Pvt) Ltd includes dividends received from S & T Ltd during the year.

You are required to prepare the Consolidated Statement of Comprehensive Income of Promo Group for the year ended 31st December 2015.

(12 Marks)

- ii. Given below are the separate statements of financial position of Duro Ltd and Zonal Ltd as at 31st December 2015.

	Duro Ltd (Rs.)	Zonal Ltd (Rs.)
Non-Current Assets	3,275,000	2,500,000
Investment in Zonal Ltd	5,225,000	-
Current Assets		
Inventory	1,000,000	1,000,000
Receivables	1,500,000	800,000
Prepayments	-	700,000
Cash	800,000	650,000
Total assets	11,800,000	5,650,000
Equity		
Share Capital	8,700,000	3,500,000
Retained Earnings	2,200,000	900,000
Liabilities		
Payables	900,000	600,000
Short term loan	-	650,000
Equity and total liabilities	11,800,000	5,650,000

Additional Information:

1. Duro Ltd has acquired 80% of shares of Zonal Ltd on 1st of January 2015 for Rs.5,225,000. At the date of acquisition, fair value of a land of Zonal Ltd has been increased by Rs.625,000. Non Controlling Interest was valued proportionately to the net assets of Zonal Ltd.
2. During the year 2015, Zonal Ltd made a profit of Rs. 400,000.
3. During the year Duro Ltd sold goods to Zonal Ltd for Rs. 600,000 making a mark-up of 20% on cost. As at 31st December 2015, inventory of Zonal Ltd included 30% of these goods unsold.
4. Zonal Ltd settled a payment to a supplier amonung to Rs. 28,000 on behalf of Duro Ltd. Both companies have shown this in their financial statements under receivables and payables respectively.
5. An impartment test of the goodwill was carried out during the year and found that it has been impaired by Rs.40,000.
6. On 1st of January 2016, Duro Ltd sold a motor vehicle to Zonal Ltd at a price of 800,000. On this date, carrying value of the motor vehicle was 650,000. The group depreciates its motor vehicle at 20% p.a.

You are required to prepare the Consolidated Statement of Financial Position as at 31st December 2015 for Duro Group.

(13 Marks)

(Total 25 marks)

Question 05

- i. Under Corporate Governance, 'UK combine code' works as a major development in principal based corporate governance. Name the sections of 'UK combine code' and explain 3 sections in detail referring to the principles.

(08 Marks)
- ii. Identify the core features of integrated reporting & explain each in detail.

(07 Marks)
- iii. DG Fashion (Pvt) Ltd is engaged in manufacturing garments. The Board of Directors is interested in investing in another industry to diversify their businesses operations. They found a mining company named ABC Mining (Pvt) Ltd, which has not commenced its commercial operations by 31st March 2016. The carrying values of the assets of the company as at 31st March 2016 are as follows.

Mining License	-	Rs. 1,500,000
Mining land	-	Rs. 2,000,000
Working capital	-	Rs. 150,000

On 01st of September 2016, the DG Fashions (Pvt) Ltd acquired 60% of the shares of ABC Mining (Pvt) Ltd for a consideration of Rs. 6,000,000. The share purchase agreement entered into on 01st January 2016 contains the terms and conditions shown below.

- The ABC Mining (Pvt) Ltd will transfer only the mining license and the mining land to DG Fashion (Pvt) Ltd and the remaining assets (working capital) will be distributed among the previous shareholders.
- The ABC Mining (Pvt) Ltd will allow DG Fashions (Pvt) Ltd to appoint 5 out of 6 board members to the Board of Directors of ABC Mining (Pvt) Ltd from 01st April 2016.

The fair values of assets is equal to their carrying value at all the above dates. The fair value of the remaining 40% of shareholding of ABC Mining (Pvt) Ltd was Rs. 2,000,000.

You are required to answer the questions given below.

- What is a business combination as per SLFRS 3?
(02 Marks)
- Can the above transaction constitute a business combination? Explain briefly.
(02 Marks)
- What is the date of the acquisition if the above transaction constitutes a business combination? Explain the reason.
(02 Marks)
- Compute the value of goodwill arising out of the above acquisition assuming it meets the criteria of a business combination
(02 Marks)
- What is the accounting treatment for the goodwill and the bargain purchase?
(02 Marks)

(Total 25 marks)