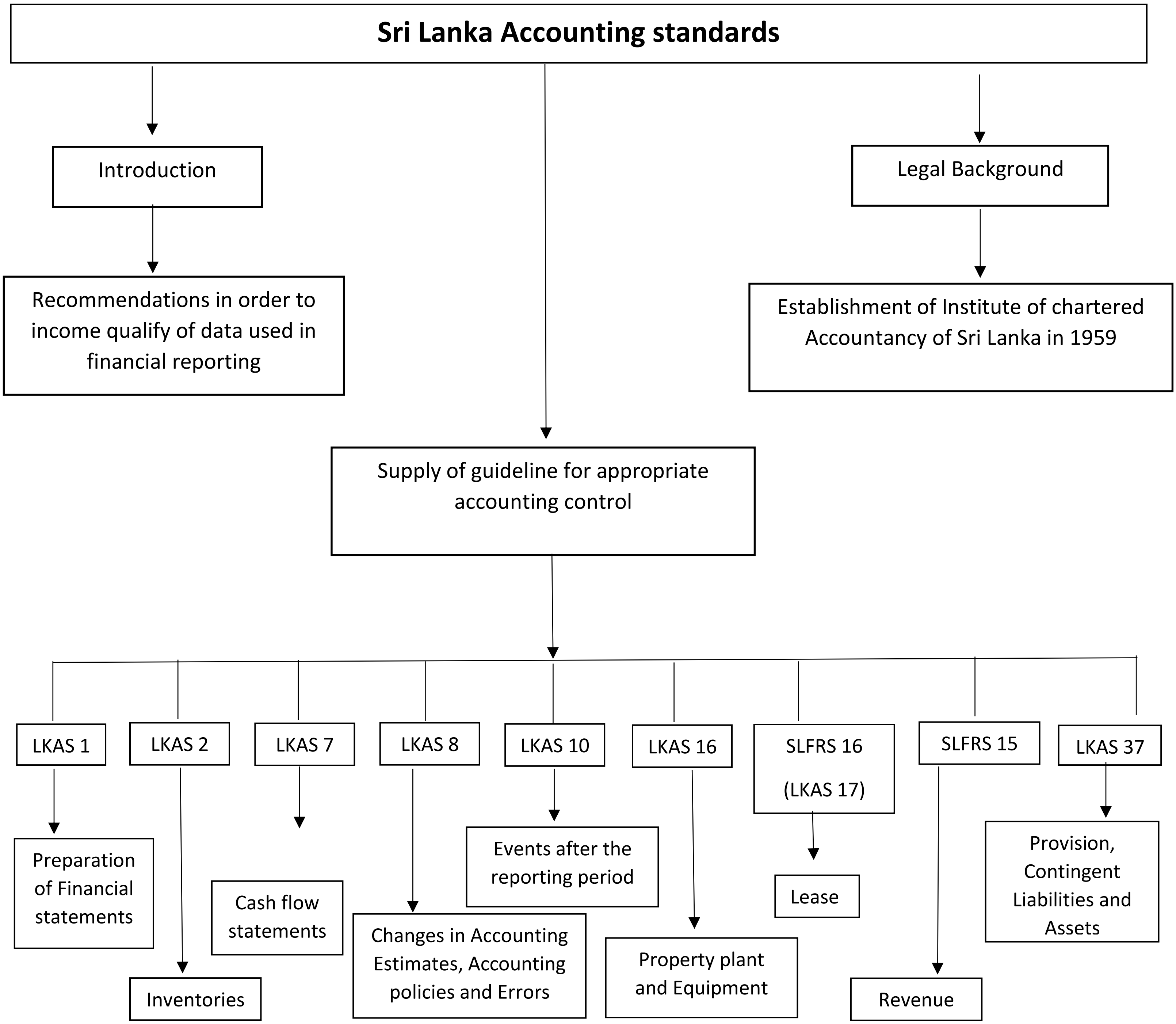
Chapter 10

Accounting standards



Guideline to subject matter:

- Disclose that in preparing and presenting financial statements of specified Business enterprise should follow Sri Lanka Accounting standards recommended by Sri Lanka Accounting and Auditing standards Act No. 15 of 1995
- Incorporation of Sri Lanka Accounting standards Committee according to Sri Lanka Accounting and auditing standards Act No. 15 of 1995
- The Sri Lanka Accounting standards Committee has been established as clearly stipulated in the Sri Lanka Accounting and auditing Standards Act No.15 of 1995.
- The Sri Lanka Accounting and auditing standards Monitoring Board has the power to examine whether the Sri Lanka Accounting standards have been adhered to in preparation of accounting statements of a specified business enterprises, and to take necessary action if the standards have not been adhered to.

Example for functions of Institute of Charted Accountants of Sri Lanka

- Organization exams in order to provide related qualification and relevant educational course.
- Controlling and supervising of student's education and training
- Maintaining and controlling of accounting standards and required methods and limitation in maintaining them.
- Promote resources on accounting and related subjects.

Development maintaining and revising the standards for the clearly specified Business enterprise using legal power vested by the Sri Lanka Accounting and Auditing standards Act No. 15 of 1995.

The need for accounting standards

Accounting standard are a statement which represents how specific transactions and events should be disclosed in the financial statement. Compliance with accounting standards is required for true and fair view of financial statements. Countries like Japan considers as setting up accounting is governments' responsibility.

Reasons for setting accounting standards

There are few reasons to set up accounting standards. Those are:

- Improvement of comparability of financial statements (Intercompany comparison and comparison between two accounting periods of the company
- Accounting standards encourages for reporting disclosures
- Accounting standards are useful for users of financial statements
- Accounting standards are useful to those who prepares the financial statements
- Accounting standards support to find theoretical basis

How Accounting standards are found formed and implemented in Sri Lanka?

Sri Lanka Accounting and auditing Act No 15 of 1995

I. Appointment of a committee for formulation of accounting standards consisting of 12 members
   - Members of institute of chartered Accountants of SL (Including chairman)
   - Members who nominated by CIMA Sri Lanka
   - Registrar of companies
   - Directors General of security and exchange commission
   - Member who is nominated by governor of central Bank of SL
   - Members who are nominated by commercial and industrial board

II. The following things are made by the institute of chartered Accountants of Sri Lanka time to time
   - Formulation of accounting standards from time to time
   - Publishing gazette notification about standards
   - Publishing accounting standards to public

III. Every specified entity requires to prepare the financial statement according to accounting standards. Those entities are as follows.
   - Listed companies
   - Government corporations engaged in sole of goods and services
   - Banks
   - Insurance companies
   - Unit trust
   - Brokering companies registered in stock exchange
   - Non listed companies which exceed specific limits (sales, Equity, Gross assets borrowings from banks and other institutions and no of employees)
     - Having a turnover in excess of 750 million
     - Having an equity capital in exceeds of Rs.450 million
     - Having gross assets of last financial year in excess of Rs.450 million
     - Having a liability to banks and other financial institutions in excess of Rs.150 million
     - Having a staff in excess of 1 000

IV. Accounting and auditing monitoring board was established to ensure that the financial statements have been prepared in compliance with accounting standards

   Powers of the board
   - Obtain a copy of the financial statements of specified entities
   - Request to provide required information during the specified period
   - Summon and question any director, officers or auditor of any specified entities
   - Carry out investigation and inquiries

V. If found guilty and convicted in a court of law with reference to non-compliance with accounting standards, would be liable to one of the following
   - Fine not more than Rs.500,000
   - Imprisonment for a period not exceeded 05 years

LKAS 01- Presentation of financial statements

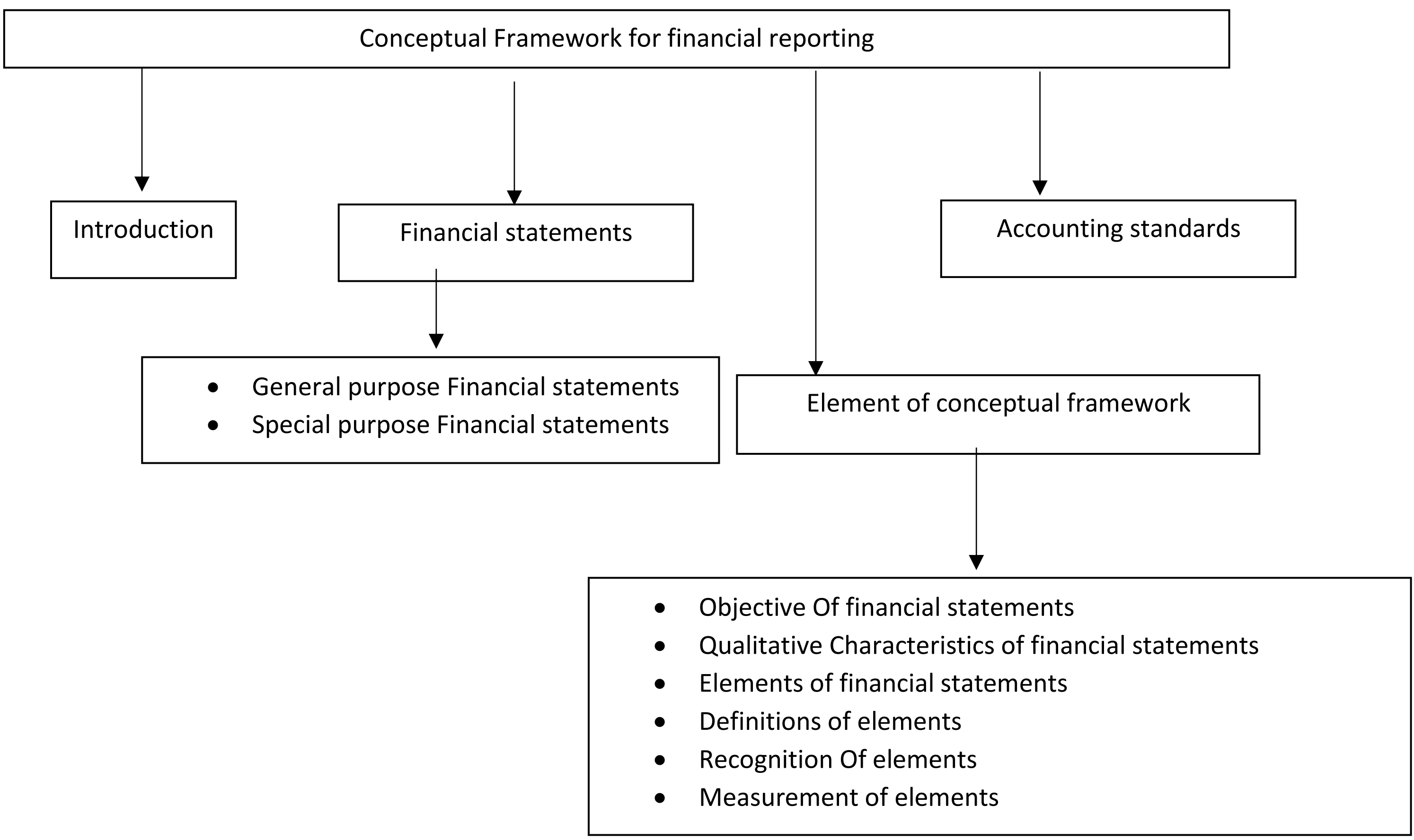
Analyze Conceptual Framework for financial Reporting.

Learning Outcomes:

- Names Types of financial statements
- Explain Conceptual Framework For financial reporting
- Explains elements of conceptual framework for financial reporting

Basic Terms and concepts

Concept Map



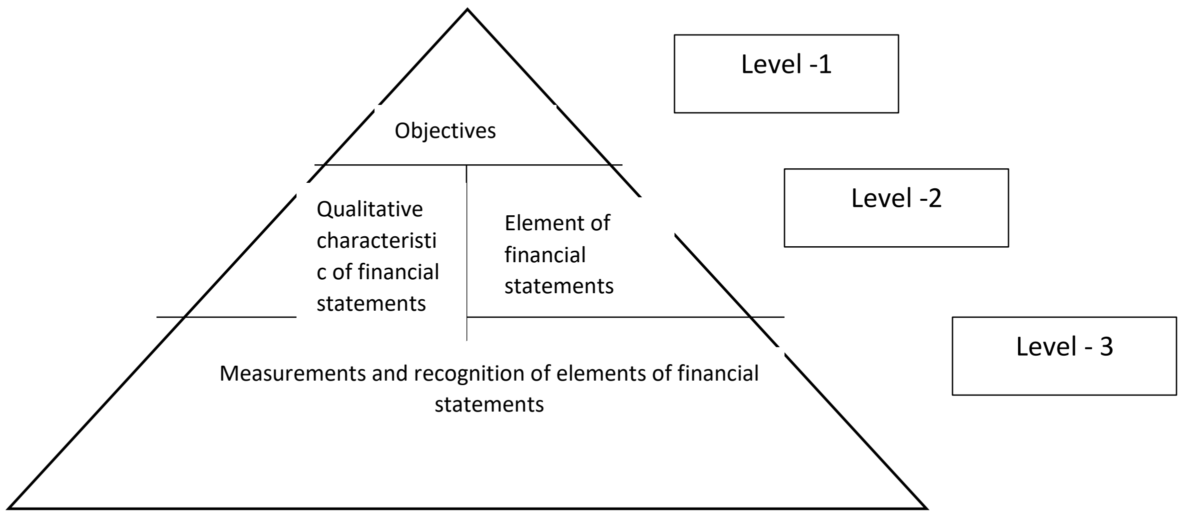
Objective

This standard prescribes the basis for presentation of general-purpose financial statement to ensure comparability both with the business's financial statements of previous years and with financial statements of other business's

Guidelines on subject matter:

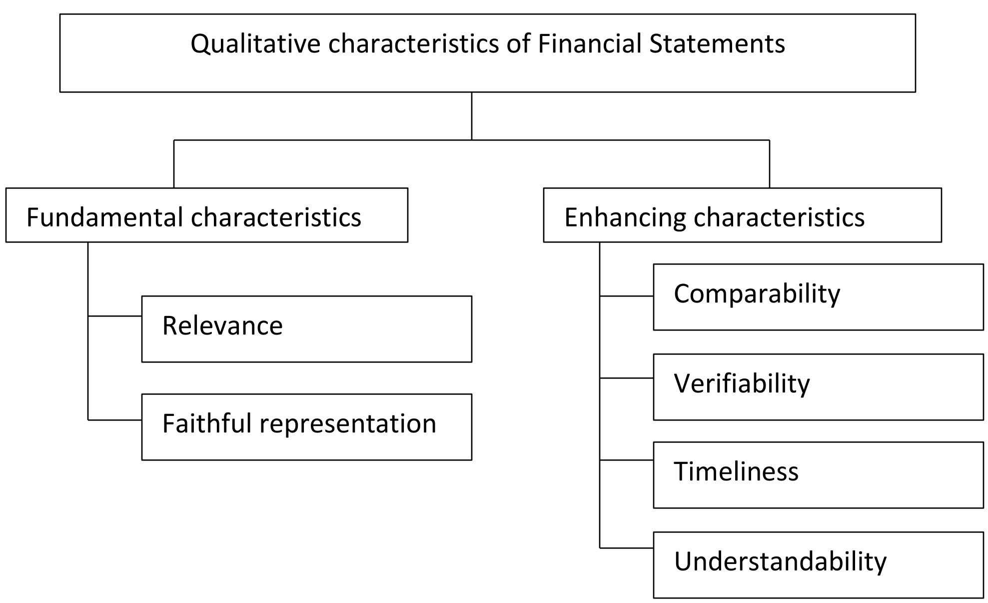
Conceptual framework for financial reporting

A set of rules which helps to make functions and limitations of financial accounting and financial statements are known as conceptual framework.



Objects of financial statements

The objectives of general-purpose financial reporting to provide financial statements reporting is to provide financial information about the reporting entity that is useful to existing and potential investors, lenders and other creditors in making decisions about providing resources of the entity. General purpose financial statements provide financial performance, financial position and changes in financial position of an entity. **Underlying assumption in preparing financial statements is going concern concept.**



Relevance

Relevant financial information is capable of making a difference in the decision made by users. If financial information is to be useful it must consist following sub characteristics.

- Predictive value
- Confirmatory value
- Materiality

Faithful representation

Economic phenomena represented in financial reports should be faithfully presented. To be a perfectly faithful representation a depiction would have following characteristics.

- Completeness
- Neutral
- Free from errors

Comparability

If data of one entity can be compared with similar information about another entities and with similar information about the same entity for another period is known as comparability.

Verifiability

Variability helps assure users that information faithfully represents the economic phenomena it purports to represents.

Timeliness

Timeliness means having information available to decision making in time to be capable of influencing their decisions.

Understandability

Presenting information clearly and concisely makes it understandable to the users.

Five Element and definitions

Contents of financial statements represent the elements. Information provided by the elements helps to achieve objectives of financial reporting. There are five elements.

There are:

- Assets
- Liabilities
- Equity
- Income
- Expenses

➢ Assets

An asset is a resource controlled by the entity as a result of past transactions/events and form which future economic benefits are expected to the entity.

Following **main three characteristics** should be possessed by an asset according to the above definition.

- It has arisen as a result of past transaction or event
- It is expecting to inflow of current economic resources to the business
- That economic resources should be controlled by the business.

➢ Liabilities

A liability is a present obligation of the entity from past transactions/events. The settlements of which is expected to result in an outflow from the entity of resources embodying economic benefits.

Following **main three characteristics** should be possessed by a liability according to the above definition.

- It is probable that an outflow of resources embodying economic benefit will result from the settlement of a present obligation
- There should be a present obligation
- As a result of a past transaction or an event

➢ Equity

Equity is the residual interest in the assets the entity after deducting all its liabilities.

The above equity, assets and liabilities are directly related to the measurement of financial position of an entity.

➢ Income

Income is increased in economic benefits during the accounting period on the form of inflows or increases of assets or decreases of liabilities that result in increases in equity. Other than those relating to equity participants.

➢ Expenses

Expenses are decreases in economic benefits during the accenting period in the form of outflows of assets or incurrence of liabilities that result in decreases in equity. Other than those relating to distribution to equity participants.

Measurements of the elements of financial statements

Measurement of the process of determining the monetary amounts of which the elements of the financial statement. Following methods can be used in measuring elements of financial statements.

- Historical cost
- Current cost
- Realizable value
- Present value

General purpose financial statements

These are the financial statements prepared to meet the information needs of those who are not in a position to require an entity to prepare reports tailored to their particular information need. These are the financial statements prepare to present information mainly to the external parties.

Notes

This contains information in addition to present in statement of comprehensive income, statement of financial position, statement of changes in equity and statement of cash flows.

Total comprehensive income

Is the change in equity during a period resulting from transactions and other events other than those changes resulting from transactions with owners in their capacity as owners.

Total income = Revenue + Profits
Total Expenses = Expenses + Profits
Total comprehensive income = Profit or loss for the year + other comprehensive income

Other comprehensive income

It comprises the item of income and expenses that are not recognized in profits or loss as required by the accounting standards.

<u>Complete set / Components of financial statements</u>

Complete Component of financial statements comprises,

- A statement of financial position as at the end of the period
- A statement of comprehensive income for the period
- A statement of changes in equity for the period
- A statement of cash flow for the period
- Notes comprising summery of accounting policies and other explanatory info

Going concern

When preparing financial statements management shall make an assessment of an entity’s ability to continue as a going concern. When management is aware about an uncertainty of going concern those uncertainties should be disclosed and if financial statements are not prepared on going concern basis the basis on which financial statements are prepared and reasons for that should be disclosed.

Accrual basis of accounting
An entity shall prepare financial statements expect cash flow information using accrual basis.

Frequency of reporting
An entity shall prepare set of financial statements at least annually. If the company change reporting period and when it is shorter or longer than one year following should be disclosed.

- The reasons for this change
- The period covered by financial statements
- The information presented in financial statements are not comparable

Information to be presented in statement of comprehensive income

- Revenue
- financial cost
- Tax expense
- Other comprehensive income
- Total comprehensive income

Classification of expenses
Expenses can be classified based on their **nature** or **functions** in calculation of profits or losses.

Past Paper questions

Activity 01 (2014 a/l)

01)Which of the following are the characteristics of an asset as per the conceptual framework for financial accounting?

A- It is a resource controlled by a firm.
B- Future economic benefits are expected to flow into the firm through it.
C- Its cost or value can be measured reliably.

(1) B only (2) A and B only (3) A and C only
(4)B and C only (5) All A, B and C

02)Categorize the following accounts into assets, liabilities, income, expense and equity.

Account	Classification
A- Provision for doubtful debts	....
B- Rent income received in advance	....
C- Retained earnings	....
D- Bad debts	....

Activity 02 (2015 A/l)

- Use the following information relating to Amal PLC for the year ending 31.03.2015 to answer question No.19 and 20.

Description	Rs.'000
Sales revenue	1 000
Surplus on revaluation of motor vehicles	200
Trade discounts received from the suppliers	100
Gain on the sale of a building	300
Total expense	500

The company has recorded a deficit of Rs.150 000 on the revaluation of motor vehicles for the year ending 31.03.2014 and this has been recognized as an expense.

19. What are the total income and other comprehensive income recognized by the company for the year ending 31.0.2015?

	Total income (Rs.'000)	Other Comprehensive Income (Rs.'000)
1)	1 450	50
2)	1 500	50
3)	1 500	200
4)	1 600	50
5)	1 600	200

(.....)

20. What is the total comprehensive income and retained earnings of the company for the year ending 31.03.2015?

	Total Comprehensive Income (Rs.'000)	Retained Earnings (Rs.'000)
1)	950	950
2)	1 000	800
3)	1 000	950
4)	1 100	900
5)	1 100	1 050

(.....)

Activity 03 (2016 a/l)

Use the following information to answer question No.1, 2, 3

The following information relates to Namal PLC for the year ending 31.03.2016.

Description	Rs.'000
Sales	1 200
Cost of sales	600
Operating expenses	300
Gain on sale of motor vehicle	80
Interim dividends paid to ordinary shareholders	100

Revaluation deficit-office equipment	120
Revaluation surplus- buildings	180

A surplus of Rs.90 000 had been recognized on the revaluation of office equipment for the year ending 31.03.2015. The buildings were revalued for the first time during the year ending 31.03.2016.

1. What was the total income and total expenses recognized for the year ending 31.03.2016 as per Sri Lanka Accounting Standards?

Total income (Rs.'000)	Total expenses (Rs.'000)
1) 1 280	900
2) 1 340	900
3) 1 380	1 020
4) 1 460	1 020
5) 1 460	1 120

(.....)

2. What was the profit and other comprehensive income recognized for the year ending 31.03.2016 as per LKAS 1 (Presentation of Financial Statements)?

Profit (Rs.'000)	other comprehensive income (Rs.'000)
1) 160	180
2) 250	90
3) 260	180
4) 350	90
5) 380	60

(.....)

3. What was the total comprehensive income and retained earnings for the year ending 31.03.2016 as per LKAS 1 (Presentation of Financial Statements)?

Total comprehensive income (Rs.'000)	retained earnings (Rs.'000)
1)340	160
2)340	250
3)440	250
4)440	260
5)440	280

(.....)

04.For each item below, state the element of financial statements in which it is recognized.

Item	Element
A- Retained earnings	....
B- Interest receivable	....
C- Loss on sale of office equipment	....

D- Provision for warranty ……………………………………………..

Activity 03 (2017 a/l)

01)State Weather the following are considered as component of general-purpose financial statement of a firm.

	Yes / No
A- Statement of financial position	……………………..
B- Notes to financial statements	…………………….
C- Directors Report	…………………….
D- Statement of changes in equity	……………………..

02)State the appropriate classification for the following accounts maintained in the general ledger

Account	Classification
A- Depreciation	………………………….
B- Revaluation Reserve	…………………………
C- Trade payables	…………………………
D- Discount received	…………………………

Activity 04 (2018 A/l)

01)Which of the following measurement bases can be used to measure the elements of financial statement as per srilanka Accounting standards ?

A- Historical Cost
B- Fair value
C- Realizable value
D- Present value

1) A and B only 2) A and C only 3) A, B and C only

4) A, B and D Only 5) All A,B,C And D

02)Which of the following are considered as component of financial statement prepared by a Welfare Society

A- Accumulated Fund Account
B- Statement of financial position
C- Statement of cash flows
D- Subscription Account
E- Income and Expenditure

1)A and D only 2) B and C only 3) A,D And E only

4)B, C and E only 5) A,B, and E only

03)Income statement of a retail business reported the following information for the year ending 31.03.2018.

Description	Rs.000
• Sales	2 000
• Interest earned	250
• Gain on sales of motor vehicles	150
• Interest expenses	300
• Operating expenses	500
• Cost of sales	1 200
• Drawings	200

The total income and total expenses to be recognized by this business for the year ending 31.03.2018

	Total income (Rs.000)	Total Expenses (Rs.000)
1)	1 200	800
2)	1 200	1 000
3)	2 250	2 000
4)	2 400	2 000
5)	2 400	2 200

Use the following information to answer question No 01 and 02

The following information was extracted from the financial statements of Ajith PLC for the year ending 31.03.2018.

Description	Rs.
• Turnover	800 000
• Cost of sales	300 000
• Administrative and distributive expenses	80 000
• Surplus/(Deficit) on revaluation:	
o Land	60 000
o Machinery	100 000
o Office equipment	(75 000)

All property, plant and equipment were revalued on 31.03.2018. while lands were revalued for the first time machinery and office equipment were revalued for the second time. The revaluation of machinery and office equipment for the first time on 31.03.2016 had resulted in a deficit of Rs.30 000 and a surplus of Rs.40 000 respectively. The total assets of the company are fully funded by equity and the company is not subject to income tax.

01) The total income and total comprehensive income of this company for the year ending 31.03.2018

	Total income (Rs.)	Total comprehensive income (Rs.)
1)	900 000	160 000
2)	930 000	505 000
3)	960 000	505 000
4)	960 000	580 000

5) 1 000 000 160 000

02) The profit and other comprehensive income of this company for the year ending 31.03.2018:

	Profit (Rs.)	Other comprehensive income (Rs.)
1)	345 000	90 000
2)	345 000	130 000
3)	385 000	160 000
4)	415 000	90 000
5)	415 000	130 000

State as per LKAS 1 (Presentation of Financial statements) the component of financial statements in which the following items are presented

Item	Component Of Financial statement
A- Cost of sales	……………………………………………………………………………….
B- Retained earnings	……………………………………………………………………………….
C- Income tax paid	……………………………………………………………………………….
D- Trade payable	……………………………………………………………………………….

<u>Activity 05(2019 A/L)</u>

- Use the following information to answer questions No. 1 and 2.

Following information was extracted from the draft financial statements of Chathurika Traders for the year ending 31.03.2020.

	Rs.'000
Gross profit	850
Administrative expenses	275
Distribution expenses	200
Finance and other expenses	100

However, following were revealed after the preparation of draft financial statements.

- Office – staff salaries Rs.30,000 and sales commission Rs.20,000 payable as at 31.03.2020 have not been accounted.
- Prepaid building rent of Rs.40,000 has been included as administrative expenses.
- Depreciation on motor vehicle of Rs.50,000 has been included in distribution expenses. However, these vehicles are used to provide transport facilities to the office staff.

01. The **correct** administrative and distribution expenses for the year ending 31.03.2020, after making the relevant adjustments:

	Administrative expenses (Rs.'000)	Distribution expenses (Rs.'000)
(1)	265	170
(2)	265	220
(3)	285	170
(4)	315	170
(5)	315	220

02. Profit for the year ending 31.03.2020 after making the relevant adjustments:

(1) Rs.215,000 (2) Rs.225,000 (3) Rs.265,000 (4) Rs.275,000 (5) Rs.285,000

- Use the following information to answer questions No. 01 and 02.

Following information relates to Saranga PLC for the year ending 31.03.2020.

Description	Rs.'000
Turnover	950
Gross profit	450
Administrative and distribution expenses	250
Revaluation surplus of land	150
Revaluation surplus of motor vehicles	75

Land was revalued for the first time and motor vehicles for the second time during the year. First time revaluation of motor vehicles on 31.03.2018 resulted in a deficit of Rs.35,000. The company is fully financed by equity and is exempted from income tax.

01.Total income and total expenses recognized by the company for the year ending 31.03.2020.

	Total Income (Rs.'000)	Total Expenses (Rs.'000)
(1)	1,140	700
(2)	1,140	750
(3)	1,175	700
(4)	1,175	750
(5)	1,175	785

02.The profit and other comprehensive income of the company for the year ending 31.03.2020:

	Profit for the year (Rs.'000)	Other Comprehensive Income (Rs.'000)
(1)	165	225
(2)	200	225
(3)	200	190
(4)	235	190
(5)	235	225

<u>Activity 06(2020 A/L)</u>

01.) Namal traders commenced its operation on 01.04.2020. The following information is provided for the month of April 2020

Total of prime entry books:	Rs.000
• Sales journal	220
• Purchase journal	200
• Sales return journal	20
• Purchase return journal	10

Other information:	Rs.000
• Cost of sales	110
• Operating expenses (excluding discounts)	60
• Trade discount received	20
• Trade discount allowed	8

- Cash discount received 5
- Cash discount allowed 10

The total income and total expenses recognized for the month of April 2020:

Total Income (Rs.'000)	Total Expenses (Rs.'000)
(1) 200	170
(2) 205	170
(3) 205	180
(4) 220	180
(5) 225	188

02.) The profit and other comprehensive income for the year ending 31.03.2020 of Damitha PLC Were Rs.1 500 000 and Rs.800 000 respectively. The other comprehensive income represents the surplus of Rs.800 000 resulted from the revaluation of land and building for the second time during the current year. The revaluation of land and building for the first time on 31.03.2016 had resulted a deficit of Rs.350 000

The correct profit and total comprehensive income for the year ending 31.03.2020

Profit for the year (Rs.000)	Total comprehensive income (Rs.000)
(1) 1 150	1 950
(2) 1 500	1 950
(3) 1 500	2 300
(4) 1 850	1 950
(5) 1 850	2 300

03.) state whether the following statements as to general – purpose financial statements prepared by a business are **True (T)** or **False (F)**

Statement	True/False
A- These statements are prepared in compliance with accounting standards	....
B- These statements are prepared primarily for the use of resource providers of the business	....
C- These statements provide information relating to a past period of the business	....
D- These statements provide information of the business measured only at historical Cost basis	....

04.) State the appropriate classifications for the following Accounts maintained by a business in the general ledger

Account	Classification
A- Bad debts	....
B- Drawings	....
C- Provision for gratuity	....
D- Accumulated depreciation on office equipment	....

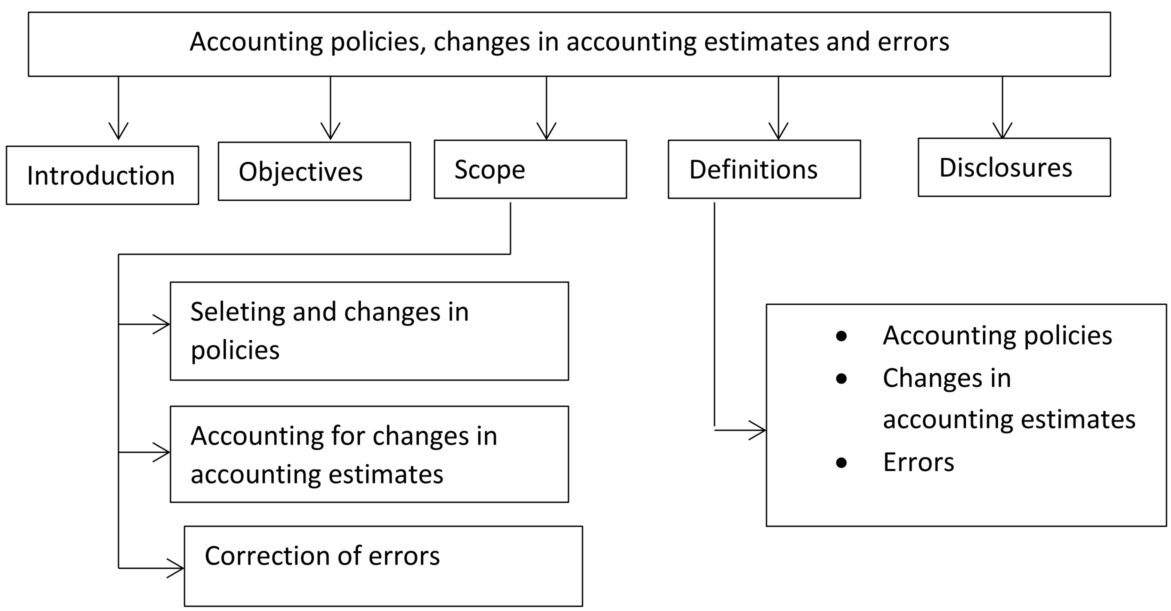
LKAS 08 "Accounting policies, changes in Accounting estimates and Prior period errors"

Leaning outcomes:

- Defines "Accounting policies, changes in Accounting estimates and errors" according to the standards.
- Presents two main points to be considered in selecting accountings policies.
- States the situations where Accounting Policies could be changed.
- Explains the way of recording changes in accounting estimates.
- States that it should recognize and correct current year errors before approving the financial statements.
- Disclosure requirements according to the standard.

Basic terms and concepts

Concept Map



Guidance on subject matter

- **Definitions**
  - **Accounting policies**
    Accounting policies are the specific principals, bases, conventions, rules and practices adopted by an enterprise in preparing and presenting financial statements.
  - **Changes in accounting estimates**
    Is an adjustment of the carrying amount of an assets or a lability or the amount of the periodic consumption of an asset. That result from the assessment of the present status of and expected future benefits and obligations associations with assets and liabilities.

- **Prior period Errors**
  Are omissions from and misstatements in the entity's periods arising from a failure to user or misuse of reliable information that was available when financial estimates for those periods were authorized for issue.
  Example: mathematical errors, errors in use of accounting policies, oversight misinterpretation and frauds.

➢ **Selecting Accounting Policies**
There are two ways of selecting an accounting policy.
- If an accounting standard clearly applies to transitions or event. The accounting policy should adhere to the standard.
- If not, management shall use to judgement in developing and applying an accounting policy.

➢ **Changes in Accounting Policies**
An entity change is accounting policy only if the change
a) Is required by a standard
b) Required to changes in entity's financial position, performance or cash follows to be presented in more reliable and more relevant manner.

Accounting for changes in accounting estimates

- If the change affects only the period in which the change occurred. Then adjust the profit or loss of the period.
  Examples: - impairment loss on trade receivables
  -allowance for expected loss on trade receivables
- If the change affects both the period in which the changes occurred and the future periods. The adjust the profit/losses of each period affected.
  Examples: - changes in depreciation values due to the changes in useful
  -Economic life of property plant and equipment
- If the change affects assets, liabilities or equity. The adjust the related period assets, liabilities, equity and their fair values.

(Important: Accounting of Changes in accounting policies and errors are not discussed for advances level)

Examples of disclosures

Changes in accounting policies	**Changes in accounting Estimates**	**Prior period errors**
• Nature of the change accounting policy.	Reasons for changing the estimates	Nature of the prior period errors
• The effect on present and future periods	Effect on the financial statements due to the change n the estimate	The correction at the beginning of the earliest period presented.

		A description of how and in which period the errors has been occurred

Past Paper questions

Activity 01(2012 A/l)

How would the resulting change in the amount of annual depreciation of an asset be recorded in the financial statements when the expected useful life of a building is revised?

(1) Consider as a change in accounting estimates and adjust the profit or loss of the current and future periods.
(2) Consider as a change in accounting estimates and revise the opening balance of retained earnings.
(3) Consider as an error and revise the opening balance of retained earnings.
(4) Consider as an error and adjust the profit or loss of the current period.
(5) Consider as a change in accounting policy and revise the opening balance of retained earnings.

Activity 02(2013 A/l)

State the two circumstances under which a firm could change its accounting policies as per LKAS 8 (accounting policies, changes in accounting estimates and errors).

……
……

Activity 03(2015 A/l)

The following information relates to a machine owned by a company.

Cost (Rs'000)	6 000
Accumulated depreciation as at 31.03.2014 (Rs'000)	2 400
Expected residual value (Rs'000)	400
Expected useful life (years)	14

On 01.03.2014, the company incurred Rs.1 800 000 for a major improvement of the machine. As a result, its remaining useful life was increased to 10 years. However, its residual value remained unchanged. What is the depreciation of this machine for the year ending 31.03.2015 and its carrying amount as at 31.03.2015?

	Depreciation (Rs.'000)	Carrying Amount (Rs.'000)
1)	100	4 500
2)	100	4 900
3)	320	3 280
4)	500	4 500
5)	500	4 900

Activity 03(2015 A/l)

State whether the following situations of a company would represent a change in accounting estimates per LKAS 8 (Accounting Policies, Changes in Accounting and Errors.)

Situation	Change in Accounting Estimates (Yes/ No)
A- The change in the profit due to the overstatement of opening inventory	…………………………….
B- The change in the rate at which doubtful debts are provided on year-end Debtors' balance.	………………………………
C- The change in the inventory valuation method from first-in first-out (FIFO) to weighted average method.	……………………………
D- The change in expected useful life if buildings from 30 to 35 years	…………………………..

Activity 04(2019 A/l)

Which of the following statements/s is are correct as per LKAS 8 (Accounting policies, changes in accounting estimates and errors)?

A- Accounting policies are the specific principles, bases, conventions, rules and practices used in the preparation and presentation of financial statements.
B- Changes in accounting estimates arise due to the new information or new developments.
C- Prior period errors are corrected retrospectively only if they arise with respect to measurement of elements in financial statements.

(1.) A only (2.)B only (3.)A and B only

(4) B and C only (5) All A,B,C

Activity 05(2020 A/l)

State whether the following statements Statements are True (T) or False (F) as per LKAS 08(Accounting policies, Changes in Accounting Estimates and errors).

Statement	True/False
A- The changes in accounting accounting estimates should be adjusted in financial statements prospectively	………………..
B- Accounting policy changes are always applied retrospectively	………………..
C- The Changes in the depreciation Method of an assets is an accounting policy change	……………….
D- The change in the useful life of an asset is a change in an accounting estimate	……………..

Model questions

01. Which of the following statement/statements is correct in relation to **determine the accounting policies** as per LKAS 08 Accounting policies, changes in accounting estimates and errors.
    A- If an accounting standard directly apply to a transaction or to an event, the accounting policy should be set based on the guidance provided in the relevant accounting standard.
    B- If the effects of transactions and events on the institution's financial position, performance and cash flows can be shown in a more reliable and trustworthy manner by use of a new accounting Policy.

C- A requirement of some other accounting standard.
D- If an accounting standard does not directly apply to a transaction or to an event the accounting policy should be set according to decision of the management.

(1) B and C only (2) A and B only (3) A and D only
(4) B and D only (5) All A, B, C and D

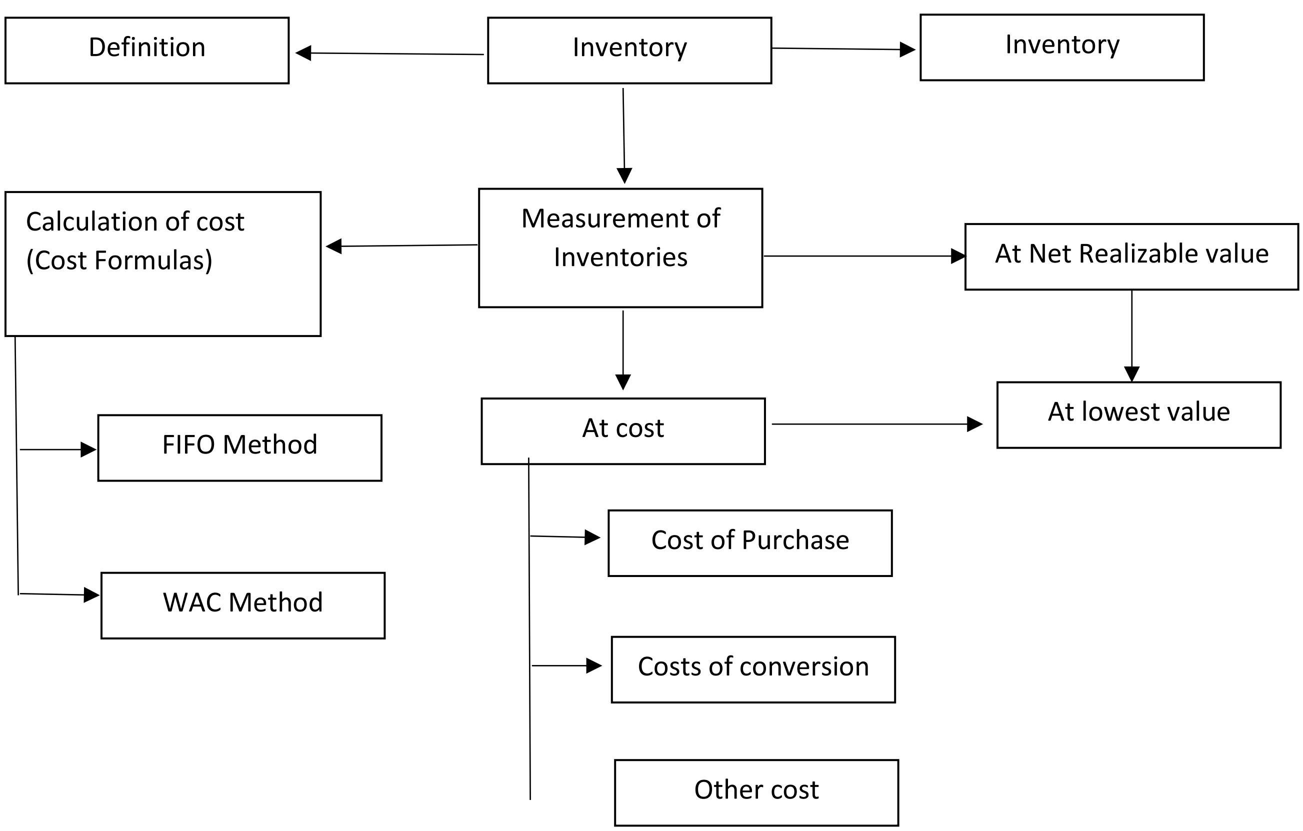
LKAS 02 (Inventory)

Learning outcome:

- Defines "inventory" as per inventory stand
- Explains the inventory cost
- Explains Net realizable value
- Calculation Cost of closing stocks based on first in first out method (FIFO) and weighted average cost methods (WAC)
- Records the value of inventory which is recognized as an expense in the financial statements.

Basic Terms and concepts

Concept Map



Assignment 01

Following are the details of inventories of a company at the year end.

As per LKAS 02, Calculate the value of inventories based on lower of cost and net realizable value using item by item method and group method separately. Show the journal entries and extract of financial statements.

Group	Item	Cost	NRV
Soup	A	100	90
	B	80	110
Shampoo	P	200	220
	Q	200	150
Toothpaste	X	50	60
	Y	70	80

Assignment 02

Following are the receipts and issues details of Wansan's business for the year ended 31.03.2016.

Date		Description	Quantity	Unit price (Rs.)
01.03.2016		Opening Inventory	100	45
02.03.2016		Purchases	300	45
05.03.2016		Issues	200	-
10.03.2016		Purchases	800	60
15.03.2016		Issues	400	-
21.03.2016		Issues	400	-
25.03.2016		Purchases	600	75
30.03.2016		Issues	400	-

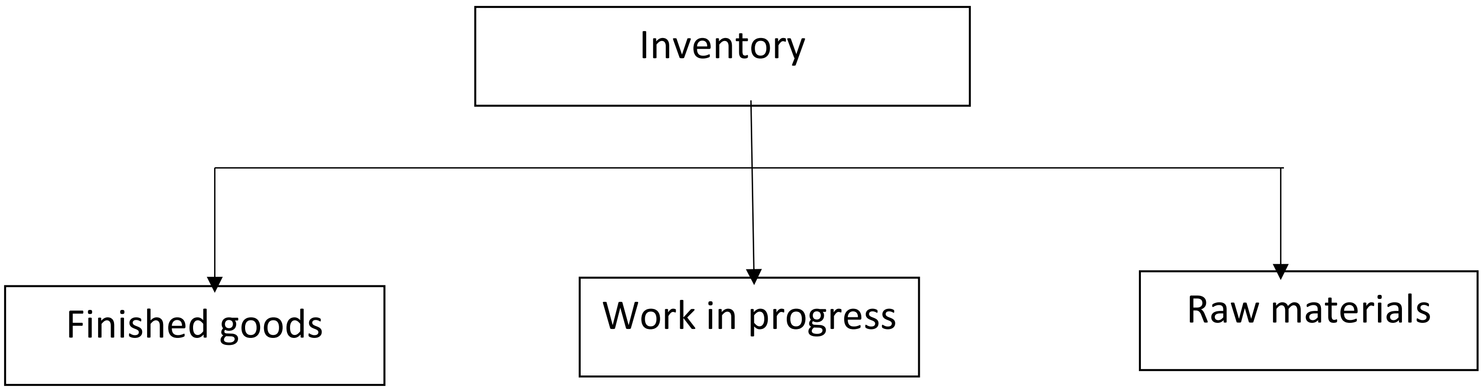
Calculate the following based on First in First out method (FIFO) And Weighted Average cost method?

1. Inventory value as at 31.03.2016
2. Cost of sales
3. Gross profit if all the stocks mentioned above will be sold at Rs.80

Guidelines for subject matters:

Definitions

- Inventories are assets:
  a) Held for sale in the ordinary course of business (Finished goods)
  b) In the process of production for such sale (work in progress)
  c) In the form of materials or supplier to be consumed in the production process or in the rendering of services (Raw materials or supplies)



Elements of cost of inventories

- Cost of purchase
- Costs of conversion
- Other costs incurred in bringing the inventories to their present location and condition

Net Realizable Value

Net realizable value is the estimate selling price in the ordinary course of business leass the estimated cost of completion and the estimated costs necessary to make the sale

Net realizable value = Estimated selling price – (Estimated selling expenses + Expected further completion cost)

As per LKAS 02, Inventories shall be measured at the lower of cost and net realizable value.

- There are the methods of deciding the lower of cost or net realizable value.
    1. Item by Item basis
    2. Group method

Cost Formulas

Before calculating cost or net realizable value of inventories, it should be confirmed that the remaining inventory balance is considered with which purchase / which product. Cost formulas provide a basis to decide on which purchase or which products the remaining inventory is represented. There are few methods.

Following cost formulas are recommended by the standard.

i. First in First out methods (FIFO)
ii. Weighted Average cost method (WAC)

1. **First in First out method (FIFO)**
   The FIFO formulas assumes that the items of inventory that were purchased or produced first are sold first and consequently the items remaining in inventory at the end of the period are those most recently purchase or produced. But in practically It is not needed to sell the items in first out basis only.
2. **Weighted average cost method (WAC)**
   Under this method the cost of each item is determined from the weighted average of the cost of similar items at the beginning of a period and the cost of similar items purchased or produce during the period.

   It is calculated as follows.

$$\text{Weighted Average price} = \frac{value\ of\ inventory\ at\ the\ issuing\ date}{Quantity\ of\ inventory\ at\ the\ issuing\ date}$$

Recognition as an expense:

There are two situations here the inventories are recognized as an expense.

i. When inventories are sold, the carrying amount of those inventories shall be recognized as an expense in the period in which the related revenue is recognized. It is identified as cost of sales.
ii. The amount of any written down of inventories to net realizable value and all losses of inventories shall be recognized as an expense in the period the written down or loss occurs.

Past Paper questions

Activity 01(2012 A/l)

A company has provided the following information as at 31.03.2012 for three items of the inventory.

Item	Cost of production (Rs)	Expected Sales (Rs)	Expected selling expenses (Rs)
A	13 000	15 000	5 000
B	10 000	16 000	4 000
C	17 000	19 000	7 000

According to 'item-by-item' basis, what is the value of the inventory as at 31.03.2012?

(1) Rs.32 000 (3) Rs.40 000 (5) Rs.50 000
(2) Rs.34 000 (4) Rs.42 000 (....)

Activity 02(2012 A/l)

Use the following information to answer questions

A company buys and sells a single product. The selling price per unit is Rs.250. the opening inventory on 01.07.2012 was 100 units at Rs.150 per unit. The company purchases 150 units on 10.07.2012 at Rs.200 per unit. It sold 200 units on 31.07.2012.

State the following if First-in-First0out (FIFO) pricing method is used issuing inventory.

(a) Cost of Sales for the month of July 2012 : ……………………………………………………
(b) Value of inventory as at 31.07.2012 : …………………………………………………….

What is the gross profit for the month of July 2012 if weighted Average pricing method is used in issuing inventory?

…….

<u>Activity 03</u> (2013 a/l)

The following information relates to a company for the month ending 31.03.2013.

Description	Units	Unit Price (Rs.)
Inventory as at 01.03.2013	1 000	100
Purchases on 07.03.2013	5 000	120
Purchases on 15.03.2013	3 000	140
Sales on 20.03.2013	8 000	-

The company uses 'first-in first-out' method to price the inventory issues. The net realizable value of yearend inventory was Rs.120 per unit.
What is the cost of sales for the month ending 31.03.2013 and inventory values as at 31.03.2013 to be shown in the financial statements of the company?

	Cost of Sales for the month Ending 31.03.2013 (Rs.)	**Inventory as at 31.03.2013 (Rs.)**
(1)	960 000	120 000
(2)	980 000	140 000
(3)	980 000	120 000
(4)	1 020 000	100 000
(5)	1 020 000	120 000

<u>Activity 05</u> (2014 a/l)

The following information pertains to a product of a company for the month of March 2014.

Date	Description	units	Units Cost (Rs.)
01.03.2014	Inventory	3 000	80
10.03.2014	Purchases	5 000	90
15.03.2014	Returns (from goods purchased on 10.03.2014)	1 000	?
20.03.2014	Purchases	3 000	70
22.03.2014	Sales	?	?
31.03.2014	Inventory	4 000	?

The company uses the 'First-in First-out' (FIFO) method to price the inventory issues.
The cost of sales for the month ending 31.03.2014 and value of inventory as at 31.03.2014.

	Cost of sales	Inventory (Rs.)
(1)	420 000	300 000
(2)	480 000	330 000
(3)	480 000	320 000
(4)	510 000	300 000
(5)	540 000	360 000

<u>Activity 07</u> (2015 a/l)

The following information relates to an inventory item of a company for the month of March 2015.

Date	Description	Quantity (units)	Unit cost (Rs)
01.03.2105	Balance	1 000	60
20.03.2015	Purchases	3 000	80
31.03.2015	sales	2 000	

The company uses the 'First-in-First-out' (FIFO) method to price the inventory issues. The net realizable value per unit of inventory as at 31.03.2015 as Rs.70.

What are the cost of the inventory as its carrying amount shown in the Statement of Financial Position as at 31.03.2015 as per LKAS 2 (inventory)?

	Cost (Rs'000)	**Carrying amount (Rs'000)**
1)	140	140
2)	140	160
3)	150	140
4)	160	140
5)	160	160

<u>Activity 08</u> (2016 a/l)

Which of the following can be identified as inventory as per the definition of LKAS 2 (Inventory).

A. Goods held for sale in the ordinary course of business.
B. Items in the process of production to be sold in the ordinary course of business.
C. Materials and supplies to be consumed in the production process or in rendering services.

1) A only 2) A and B only 3) A and C only
4) B and C only 5) All A, B and C (....)

<u>Activity 09</u> (2016 a/l)

A trading company uses the weighted average to price the issue of inventory. Information relating to an inventory item for march 2016 is given below

Date	Description	Quantity	Price (Rs.)
01.03.2016	Balance	1 000	10
07.03.2016	Purchase	2 000	15
14.03.2016	Purchase	4 000	11
20.03.2016	sales	4 000	?

Calculate the following:

(a) Cost of sales - March 2016 Rs…………………………………………………………….
(b) Inventory as at 31.03.2016 Rs…………………………………………………………….

<u>Activity 09</u> (2017 a/l)

The following information relates to an inventory item of a company for the month of march 2017

Date	Description	Quantity	Per unit Cost (Rs.)
01.03.2017	Balance	100	200
20.03.2017	Purchases	400	400
27.03.2017	Sales	200	?

The company which currently follows FIFO method to price the inventory issues, is considering to use the weighted average method in the future

What is the cost of inventory as at 31.03.2017 under each of these methods?

	FIFO(Rs.000)	WAC(Rs.000)
(1)	100	90
(2)	100	108
(3)	120	90
(4)	120	108
(5)	120	180

<u>Activity 09</u> (2019 a/l)

Which of the following cost item/s is/are not included in the determination of cost of inventory as per LKAS 2 (Inventories)?

A. Abnormal amounts of wasted materials, Labour or other production costs
B. Storage costs of finished goods till they are delivered to customers
C. Administrative overhead of the showrooms

(1)A only (2) B only (3) A and B Only

(4) B and C only (5) All A,B and C

Activity 10 (2019 a/l)

The following information relates to a product by a company

Date	Description
01.07.2019	Inventory balance (1 000 units at Rs.3 per unit)
05.07.2019	Purchases (1 500 units at Rs.4 per unit)
12.07.2019	Purchases (500 units at Rs.6 per unit)
28.07.2019	Sold (2 000 units at Rs.10 per unit)

Compute the following under each of the pricing method given below:

Pricing method	Cost of goods sold for month of July 2019	Closing Inventory as at 31.07.2019
(a) FIFO	…………………………………………………..	……………………………………………
(b) WAC	…………………………………………………..	……………………………………………

Model Questions

01. Following information relevant for conversion cost of inventory

	(Rs.)
Direct labor cost	20,000,000
Direct other expenses	8,000,000
Fixed production overheads	1,200,000
Variable production overhead	1,600,000
Actual production (capacity)	40 000
Normal production (capacity)	60 000

You are required to calculate conversion cost per unit and if the closing inventory units are 4 000, what is the total conversion cost

Conversion cost per unit	Total conversion cost (when inventory quantity 4 000)

(1)	Rs. 3,040,000	Rs. 760
(2)	Rs. 770	Rs. 3,080,000
(3)	Rs. 760	Rs. 3,040,000
(4)	Rs. 3,080,000	Rs. 770
(5)	Rs. 740	Rs. 2,960,000

Use the following information of an entity relating to an item of inventory to answer questions No. 02 and 05

Date	Description	Units	Units cost (Rs.)
01.01.2020	Balance	20 000	300
14.01.2020	Purchase	50 000	400
20.01.2020	Purchase	30 000	500
31.01.2020	Balance	25000	-

75000 units have been sold between 21st and 31st January.

02. What is the **cost** of inventory as at 31.01.2020 if weighted average mothered is used for issuing inventories.?

(1) Rs. 12,500,000 (2) Rs. 10,250,000 (3) Rs. 12,500,000
(4) Rs. 28,500,000 (5) Rs. 30,750,000

03. What is the **cost of sales** for month ending 31.01.2020 if weighted average mothered is used for issuing inventories.?

(1) Rs. 12,500,000 (2) Rs. 10,250,000 (3) Rs. 10,000,000
(4) Rs. 28,500,000 (5) Rs. 30,750,000

04. What is the **cost** of inventory as at 31.01.2020. if the first in first out (FIFO) method there is used for issuing inventories.?

(1) Rs. 12,500,000 (2) Rs. 10,250,000 (3) Rs. 7,500,000
(4) Rs. 28,500,000 (5) Rs. 30,750,000

05. What is the **cost of sales** for the month ending 31.01.2020. if the first in first out (FIFO) method is used for issuing inventories?

(1) Rs. 12,500,000 (2) Rs. 10,250,000 (3) Rs. 15,000,000
(4) Rs. 28,500,000 (5) Rs. 30,750,000

06. The following information pertains to a product of a company for the month of March 2020.

Date	Description	Units	Unit cost (Rs.)
01.03.2020	Inventory	60 000	100
10.03.2020	Purchases	95 000	130
15.03.2020	Returns (from goods purchased on 10.03.2020)	5 000	?
20.03.2020	Purchases	50 000	150
22.03.2020	Sales	?	?
31.03.2020	Inventory	70 000	?

The company uses the (FIFO) method to price the inventory issue

	Cost of sales (Rs.000)	Inventory (Rs.000)
(1)	15,100	10,500
(2)	17,700	10,100
(3)	15,100	10,100
(4)	10,100	15,100

(5) 18,350 7,000

07. Which of the following cost item/s is/are not included in the determination of cost of inventory as per LKAS 2(Inventories)?

A. Abnormal amounts of wasted material, labour or other production costs
B. Storage costs, unless those cost are necessary in the production process before further production stage
C. Administrative overheads that do not contribute to bringing inventories to their present location and condition
D. Selling cost

(1)	A, B and C only	(2)	B and D only	(3)	A, C and D only
(4)	B, C and D only	(5)	All A, B, C and D only		

08. Which of the following things included in the cost of inventory as per LKAS 2 (Inventories)?

A - Cost of purchase
B - Cost of conversion
C - Other cost incurred in bringing the inventories to their present location and condition.

(1)	A only	(2)	B only	(3)	A and B only
(4)	B and C only	(5)	All A,B and C only		

09. Which of the following things included in the inventory as per LKAS 2 (Inventories)?

A. Inventories are assets held for sales in the ordinary course of business:
B. Inventories are assets, in the process of production for such sales.
C. Inventories are assets, in the form of materials or supplies to be consumed in the production process or in the rendering of services.

(1)	A only	(2)	B only	(3)	A and B only
(4)	B and C only	(5)	All A,B and C only		

10. Which of the following statement is correct that inventories recognition as an expense as per LKAS 2 (Inventories)?

A. When inventories are sold, the carrying amount of theses inventories shall be recognized as an expenses in the period in which the related revenue is recognized.
B. The amount of any written down of inventories to net realizable value
C. All losses of inventories shall be recognized as an expens

(1) A only	(2) B only	(3) A and B only
(4) A and C only	(5) All A,B,C	

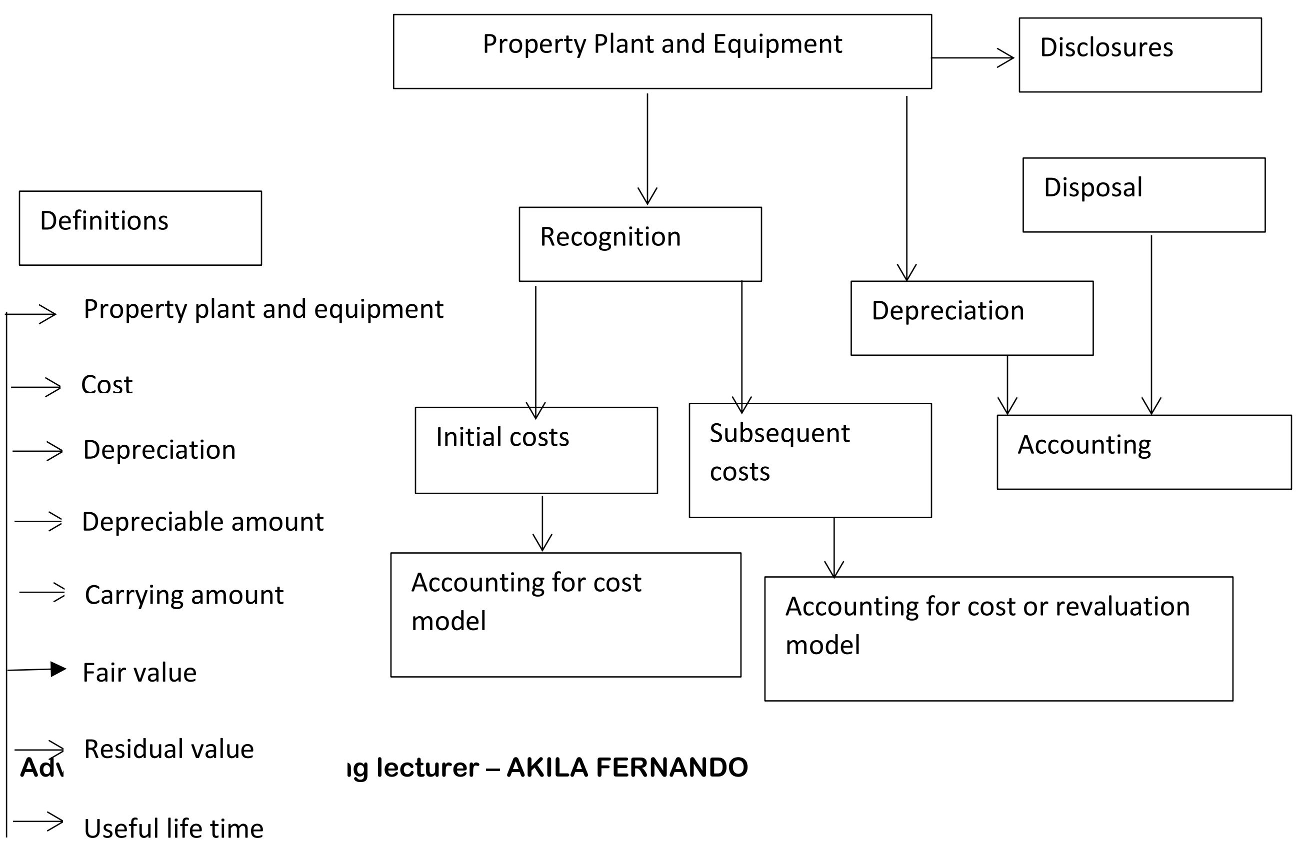
LKAS 16 Property Plant and Equipment

Learning outcomes:

- Defining Property Plant and Equipment as per Sri Lanka Accounting Standard.
- Defining the following terms as per Sri Lanka Accounting Standard.
    - Cost
    - Depreciation
    - Depreciation amount
    - Carrying amount
    - Fair value
    - Residual value
    - Useful life time
- States the need of consideration towards initial costs and subsequent costs when recognizing.
- Names elements of costs
- Explain that it should be necessary to measure at cost for the first time and then cost model or revaluation model could be used for measurement of property plant and equipment.
- Accounting at revaluation model
- Name depreciation methods and accounting for depreciation
- Accounting for disposal of Property Plant and Equipment
- Make necessary disclosures regarding Property Plant and Equipment

Basic terms and concepts

Concept map



- Property Plant and Equipment are tangible items that: are held for uses in the production or supply of goods or services, for rental to others or for administrative purposes and are expected to be used during more than one period.
- Following items should be defined as per LKAS 16 Property Plant and Equipment
    - Cost
    - Depreciation
    - Carrying amount
    - Fair value
    - Residual value/scrap value
    - Useful life time

Guidance of subject matter

- **Cost**
  Cost is the amount of cash equivalent paid or the fair value of other consideration given to acquire an asset at the time of its acquisition construction or, where applicable. The amount attributed to that asset when initially recognized in accordance with the specific requirements.

- **Depreciable amount**
  Depreciable amount is the cost of an asset or other amount substituted for cost, less its residual value.

- **Carrying amount**
  Carrying amount is the amount at which an asset is recognized after deducting any.
  Accumulated depreciation and accumulated impairments losses.

  Calculation of impairment losses are not expected here.

- **Fair value**
  Fair value is the amount for which an asset could be exchanged between knowledgeable, willing parties in an arm's length transaction.

- **Residual value**
  The residual value of an asset is the estimated amount that an entity would currently obtain from disposal of the asset, after deducting the estimate cost of disposal, in the condition expected at the end of its useful lie.

- **Useful life**
  Useful life is the period over which an asset is expected to be available for use by an entity or the number of production or similar units expected to be obtained from the asset by an entity.
- **Recognition**
  The cost an item of property, plant and equipment shall be recognized as an asset if.

1. It's probable that future economic benefits associated with the item will flow to the entity and.
2. The cost of the item can be measured reliably.

- An entity evaluates under the recognition principle all its property plant and equipment costs at the time they are incurred those. These costs can be of two types.

- **Initial costs**
  Costs incurred initially to acquire or construct an item of property plant and equipment. These costs should be capitalized.

- **Subsequent costs**
  Costs incurred subsequently to add to replace part of or service it. Could be identified in two types.
  1. Capital expenditure
  2. Revenue expenditure
- **Revenue expenditure**
  The costs incurred in maintain the assets.
  Examples: machine repair expenses

  Building painting expenses

Property, Plant and Equipment measurement at recognition

An item of property, plant and equipment that qualifies for recognition as an asset shall be measured at its cost and it includes following:

a) Its purchase price, including import duties and non-refundable purchase taxes. Shipment charges, insurance changes after deducting trade discounts and rebates.
b) Ant cost directly attributable to bringing the asset to the expected location and conditions.

Example:

- Direct costs of construction or acquisitions of assets.
- Cost of site preparation
- Initial delivery and handling costs
- Installation and assembly costs
- Net costs of testing whether the assets are functioning properly
- Professional fees

c) The estimation of costs of dismantling and removing the assets at the end of the life time.

Measurement after recognition:

- An entity shall choose either the cost model or revolution model foe measurement after recognition at cost.

- Property, plant and equipment are measured at revolution model as follows.
- Method of recording fair value of the asset. Here the carrying amount has been calculated by deducting accumulated depreciation against cost and compare it with the fair value.
- Revaluation of property, plant and equipment

Revaluation of an item of property plant and equipment for the First time

Revaluation for the first time

Revaluation surplus

Relevant asset a/c/ Dr. xx
Revaluation reserves a/c Cr. xx

Revaluation deficit

Other expenses Dr. xx
Relevant asset a/c/ Dr. xx

Revaluation of an item of property plant and equipment for the second time when it was revalued in a previous year.

Example: A profit of 1,000,000 was received by the first-time revaluation of building

The building is revalued again

Ex: if revaluation deficit is Rs.800 000

Revaluation Reserves A/c Dr. 800 000
Building account Cr. 800 000

Ex: if revaluation deficit is Rs.1 300 000

Other expenses Dr. 300 000
Revaluation Reserves A/c Dr. 1 000 000
(Deducted from Revaluation reserves)
Building account Cr. 1 300 000

Example: A deficit is Rs.500 000 by the first-time revaluation of a machine.

The machine is revalued again

Ex: if revaluation surplus is Rs.400 000

Machine account Dr. 400 000
Revaluation reserves Cr. 400 000

Ex: if revaluation surplus is Rs.700 000

Machine account Dr. 700 000
Other expense Cr. 500 000
(Deducted from other expenses)
Revaluation reserved account Cr. 200 000

When revaluation assets, accumulated depreciation should be debited to provision for depreciation account and credited to relevant asset account.

- Calculation of depreciation of property, plant and equipment using straight line method and reducing balance method.
- Calculation of depreciation as per straight line method

$$\text{Annual depreciation} = \frac{\text{Cost of residual value}}{\text{Useful life lime}}$$

Calculation of depreciation as per reducing balance method

$$\text{Annual depreciation} = (\text{Cost} - \text{Accumulated depreciation}) \times \text{Rate of depreciation}$$

Annual depreciation is recorded as follows:

Depreciation account	Dr. xx	
Accumulated depreciation account		Cr. xx

Accounting for disposals of Property, Plant and Equipment

Journal entries relating to disposals of property, plant and equipment are as follows.

- <u>Cost of the disposed PPE</u>

PPE disposal account	Dr.xx	
PPE (Cost) account		Cr.xx

- <u>Accumulated depreciation of the disposal PPE</u>

Accumulated depreciation account	Dr.xx	
PPE disposal account		Cr.xx

- <u>Sales price of the PPE</u>

Cash account	Dr.xx	
PPE disposal account		Cr.xx

- <u>Exchange value of PPE</u>

PPE (Cost) account	Dr.xx	
PPE disposal account		Cr.xx

- <u>Profit arising from disposal</u>

PPE disposal account	Dr.xx	
Profit or loss account (Other income)		Cr.xx

- <u>Loss arising from disposal</u>

Profit or loss account (Other expense)	Dr.xx	
PPE disposal account		Cr.xx

Disclosures relating to property, plant equipment

- The measurement bases used for determining the gross carrying amount
- The depreciation method used
- The useful life or the depreciation rates used
- The gross carrying amount and the accumulated depreciation at the beginning and end of the period.

Revaluation

First time revaluation

First time revaluation surplus (on Opening date)

- Building cost as at 01/04/2020 = Rs.2200
- Accumulated dep on building as at 01/04/2020 = Rs.200
- Building depreciation rate = 10% per annum on cost (straight line method)

Building has been revalued at Rs.2500 on 01/04/2020 by a professional valuer.

First time revaluation surplus (on closing date)

- Building cost as at 01/04/2020 = Rs.2200
- Accumulated dep on building as at 01/04/2020 = Rs.200
- Building depreciation rate = 10% per annum on cost (straight line method)

Building has been revalued at Rs.2500 on 31/03/2021 by a professional valuer.

First time revaluation Deficit (on opening date)

- Building cost as at 01/04/2020 = Rs.2200
- Accumulated dep on building as at 01/04/2020 = Rs.200
- Building depreciation rate = 10% per annum on cost (straight line method)

Building has been revalued at Rs.1500 on 01/04/2020 by a professional valuer.

First time revaluation Deficit (on closing date)

- Building cost as at 01/04/2020 = Rs.2200
- Accumulated dep on building as at 01/04/2020 = Rs.200
- Building depreciation rate = 10% per annum on cost (straight line method)

Building has been revalued at Rs.1500 on 31/03/2021 by a professional valuer.

Second time revaluation

Second time revaluation surplus (on opening date) ***(while previous year has revaluation Deficit)***

The building has been revalued on 01/04/2020 for Rs.19500 for the second time (while first time revaluation results a Deficit of Rs.500)

- Building cost as at 01/04/2020 = Rs.15000
- Accumulated depreciation on building as at 01/04/2020 = Rs.500
- Building depreciation rate = 10% per annuum on cost (straight line method)

Second time revaluation Deficit (on closing date) ***(while previous year has revaluation surplus)***

The building has been revalued on 31/03/2021 for Rs.19500 for the second time (while first time revaluation results a surplus of Rs.500)

- Building cost as at 01/04/2020 = Rs.25000
- Accumulated depreciation on building as at 01/04/2020 = Rs.500
- Building depreciation rate = 10% per annuum on cost (straight line method)

Second time revaluation surplus (on opening date) ***(while previous year has revaluation surplus)***

The building has been revalued on 01/04/2020 for Rs.19500 for the second time (while first time revaluation results a surplus of Rs.500)

- Building cost as at 01/04/2020 = Rs.15000
- Accumulated depreciation on building as at 01/04/2020 = Rs.500
- Building depreciation rate = 10% per annuum on cost (straight line method)

Second time revaluation Deficit (on closing date) ***(while previous year has revaluation Deficit)***

The building has been revalued on 31/03/2021 for Rs.19500 for the second time (while first time revaluation results a loss of Rs.500)

- Building cost as at 01/04/2020 = Rs.25000
- Accumulated depreciation on building as at 01/04/2020 = Rs.500
- Building depreciation rate = 10% per annuum on cost (straight line method)

Disposal

Assignment 01

The trial balance of Sumith PLC as at 31.03.2020 is given bellow.

Description	Dr.	Cr.
Motor vehicle (cost)	920,000	
Accumulated depreciation as at 01.04.2019 Motor vehicle		400,000

Additional information

- **(i)** Motor vehicle which had been acquired for Rs 420,000 on 01.04.2017, was sold for Rs 220,000 on 01.10.2019, no entry has been made in this respect.
- **(ii)** The depreciation on motor vehicle 20% on straight line method.

Required: disclose the relevant ledger account for the year ended 31.03.2020.

Assignment 02

The trial balance of Akila PLC as at 31.03.2020 is given bellow.

Description	Dr.	Cr.
Motor vehicle (cost)	980,000	
Accumulated depreciation as at 01.04.2019 Motor vehicle		420,000

Additional information

- **(i)** Motor vehicle which had been acquired for Rs 380,000 on 01.01.2017, was sold for Rs 165,000 on 01.10.2019, no entry has been made in this respect.
- **(ii)** The depreciation on motor vehicle 20% on straight line method.

Required: disclose the relevant ledger account for the year ended 31.03.2020.

Assignment 03

The trial balance of Jude PLC as at 31.03.2020 is given bellow.

Description	Dr.	Cr.
Motor vehicle (cost)	960,000	
Accumulated depreciation as at 01.04.2019 Motor vehicle		410,000

Additional information

- **(i)** Motor vehicle which had been acquired for Rs 440,000 on 01.04.2017, was sold for Rs 210,000 on 01.01.2020, no entry has been made in this respect.
- **(ii)** The depreciation on motor vehicle 20% on straight line method.

Required: disclose the relevant ledger account for the year ended 31.03.2020.

Past Paper questions

Activity 01 (2013 A/l)

A land was acquired by a company on 01.10.2012 to construct a restaurant. In this respect the followings costs were incurred.

	Rs'000
Purchase price of the land	4 000
Stamp duty and legal fees	200
Cost of removing the old building in the land	200
Cot of preparation of the land for construction	250
Annual maintenance cost of the land	100

Further, the materials removed from the old building were sold for Rs.50 000.
What is the cost of the land as at 31.03.2013 as per LKAS 16 – property, plant and equipment?

(1) Rs.4 400 000 (2) Rs.2 450 000 (3) Rs.4 550 000
(4) Rs.4 600 000 (5) Rs.4 700 000

Activity 02 (2014 A/l)

The following information relates to the acquisition of a machine on 01.03.2014 by a company, which is registered for value added tax (VAT).

	Rs.
List price of the machine	800 000
VAT paid	86 400
Cost of transportation	30 000
Cost of site preparation	20 000
Cost of installation	40 000
Cost of initial testing	50 000

A trade discount of 10% was received at the time acquisition. 100 units manufactured during the initial testing were sold at Rs.300 per unit.
The cost of the machine at initial recognition as per LKAS 16 (property, plant and equipment):
(1) Rs.830 000 (2) Rs.860 000 (3) Rs.896 400
(4) Rs.910 000 (5) Rs.916 400

Activity 03 (2014 A/l)

The following information relates to motor vehicle owned by a firm.

	Rs'000
Motor vehicles at cost as at 01.04.2013	4 000
Accumulated depreciation as at 01.04.2013	750
Proceeds from the sale of motor vehicle on 01.10.2013 (purchased on 01.04.2011 at a cost of Rs.1 500 000)	1 000
Purchase of a motor vehicle on 01.01.2014	5 000

The motor vehicles are depreciated at 10% per annum on cost on the straight-line method and are available for use from the date of purchase.
What is the depreciation for motor vehicles and the loss on the sale of the motor vehicle during the year ending 31.03.2014?

	Depreciation (Rs.)	Loss (Rs.)
(1)	375 000	200 000
(2)	400 000	350 000
(3)	450 000	125 000
(4)	525 000	500 000
(5)	900 000	50 000

Activity 04 (2015 A/l)

Which of the following statement/ statements are correct in relation to defining property, plant and equipment as per LKAS 16 (property, plant and Equipment)?

A- They are tangible items.
B- They are held for use in the production of goods or supply of service or for administration purposes.
C- They are expected to be used for more than one financial year.

1) A only 2) A and B only 3) A and C only
4) B and C only 5) All A, B and C

Activity 05 (2015 A/l)

The following information relates to the acquisition of a machine on 31.03.2015 by a business registered for Value Added Tax (VAT)

	Rs.
Price paid inclusive of VAT	777 000
Transport cost from port to the business premises	40 000
Cost of site preparation	120 000
Cost of installation	80 000

Expenses of the opening ceremony	30 000
Cost of the initial testing of the machine	10 000

The applicable VAT rate is 11%

The cost of the machine at initial recognition as per LKAS 16 (property, plant and Equipment) :

1) Rs.931 530 2) Rs.950 000 3) Rs.971 530
4) Rs.980 000 5) Rs.1 027 000

Activity 06 (2016 A/l)

The following information relates to motor vehicles of Rakitha PLC.

Description	Rs.'000
Carrying amount as at 01.04.2015	6 500
Loss on a motor vehicle disposed on 30.09.2015	150
Acquisition of a new motor vehicle on 01.01.2016	4 000

All the motor vehicle available at the beginning of the year has been purchased on 01.04.2010. The motor vehicle disposed during the year had been purchased at a cost of Rs.3 000 000. The motor vehicles are depreciated at 10% per annum on the straight-line method.

The depreciation for motor vehicles for the year ending 31.03.2016 and the sales processed o the motor vehicles disposed were:

	Depreciation (Rs.)	Sales proceeds (Rs.)
1)	650	1 500
2)	1 000	1 350
3)	1 100	1 350
4)	1 100	1 200
5)	1 250	1 200

Activity 07 (2016 A/l)

A company purchased a new machine at a price of Rs.5 500 000. Indicate whether the following payments made in relation to this purchase will be recognized as per LKAS 16 (Property, Plant and Equipment) in the initial cost of the machine or in expenses by placing in the appropriate column.

Item	Amount (Rs.'000)	Initial cost	Expenses
A- Training of the machine operator	120	....	....
B- Engineer's fee for the certification of Installation	12	....	....
C- Testing of the machine	220	....	....
D- Ceremonial opening of the machine	150	....	....

Activity 07 (2017 A/l)

The following information relates to the acquisition of a machine on 31.03.2017 by a business This business is not registered for value added Tax (VAT)

Description	Rs.
• Price paid inclusive of 15% VAT	230 000
• Transport cost from supplier's company to the business	15 000
• Cost of installation and assembly	30 000
• Cost of dismantling and removing the old machine	2 000
• Cost of testing prior to the use of machine	8 000
• Cost of training of employees on the use of machine	12 000

What is the cost of the machine at recognition as per LKAS 16 (Property, plant & Equipment)?

1) Rs.255 000 2) Rs.267 000 3) Rs.283 000
4) Rs.285 000 5) Rs.297 000

Activity 08 (2018 A/l)

The following information relates to a machine acquired buy a company, which is registered for value added tax (VAT)

Date	Description	Amount (Rs.)
• 01.04.2017	Importing the machine (Including 15% VAT)	575 000
• 15.04.2017	Transporting the machine to the machinery	40 000
• 30.04.2017	Preparing the site and installing the machine	60 000
• 15.05.2017	Conducting a test run and ensuring thereby that the machine is Functioning properly	80 000
• 15.05.2017	Receiving cash from sale of items produced in the test run	30 000
• 30.06.2017	Conducting the opening ceremony	20 000

The cost of this machine at recognition and the date of commencing depreciation of the machine as per LKAS 16 (Property, Plant and Equipment):

	Cost (Rs.)	Date
(1)	540 000	15.04.2017
(2)	650 000	15.05.2017
(3)	650 000	30.06.2017
(4)	725 000	30.06.2017
(5)	755 000	15.05.2017

Activity 09 (2019 A/l)

Nethu PLC imported a machine on 01.03.2019 for use in the production by paying Rs.2 000 000 following expenses were also incurred by the company in this respect.

	Rs.000
• Site preparation	160
• Charges to connect power supply to the machine	10
• Cost of the initial test run	20
• Advertising cost on the product quality	60
• Licensing fee paid to obtain approval for use of the machine	30
• Cost of the inaugural ceremony of commissioning the machine	40

What is the cost of machine at recognition as per LKAS 16 (Property, plant and equipment)?

1) Rs.2 160 000 2) Rs.2 180 000 3) Rs.2 210 000
4) Rs.2 220 000 5) Rs.2 260 000

Activity 10 (2019 A/l)

Which of the following statement is correct as per LKAS 16 (Property, plant and equipment)?

A- Depreciation is the systematic allocation of the depreciable amount of an asset over its useful life
B- Depreciation amount is the cost or other amount substituted for cost of an asset. Less its residual value.
C- Useful life is the period over which an asset is expected to be available for use by an entity.

(1) A only (2) B only (3) A and B only

(4)B and C only (5) All A,B and C

Activity 11 (2020 A/l)

Which of the following statement is correct as per LKAS 16 (Property, plant and equipment)?

A- Depreciation amount for the period should always be recognized in profit or loss.
B- An item of property plant and equipment should be measured at cost at the initial recognition
C- The surplus resulting on the revaluation of an asset in the current year should be recognized in order comprehensive income in the absence of a previous revaluation deficit for the same assets

(1) A only (2) C only (3) A and B only

(4)B and C only (5) All A,B and C

Activity 12 (2020 A/l)

Suranga PLC purchased a machine for Rs.8 000 000 on 01.04.2017 and its estimated useful life and residual value were 8 years and Rs. 1 600 000 respectively. The useful life and the residual value of the asset were re-estimated on 01.04.2019. According to new estimates, the remaining useful life and the residual value are 4 years and Rs.1 000 000 respectively.

What is the depreciation of the machine for the year ending 31.03.2020 as per LKAS 16 (Property, plant and equipment)?

1) Rs.900 000 2) Rs. 1 166 777 3) Rs.1 350 000
4) Rs.1 600 000 5) Rs.1 750 000

Activity 13 (2020 A/l)

Sumudu PLC Purchased a machine on 01.01.2020 for Rs.2 500 000 to use in manufacturing activities

The following costs were also incurred by the company in this respect

	Rs.000
• Site preparation cost	200
• Installation cost	350
• Annual premium for fire insurance	275
• Cost of the initial test run	250

The net proceeds from the sale of items produced in the initial test run was Rs.50 000

What is the cost of this machine at recognition as per LKAS 16 (Property, plant and equipment)?

1) Rs.3 050 000 2) Rs. 3 250 000 3) Rs.3 300 000
4) Rs.3 525 000 5) Rs.3 575 000

<u>Model questions</u>

01. The following information relates to the acquisition of a machine on 31.03.2020 by a business is not registered for Value Added Tax

	Rs.
List price of machine	20,000,000
VAT paid	2,700,000
Engineer chargers for fixing	580,000
Transport cost from port to the business premises	850,000
Cost of site preparation	430,000
Cost of installation	320,000
Expenses of the opening ceremony	130,000
Cost of the initial testing of the machine	180,000
Cost of employee training for machine operation	120,000
Annual maintain cost	200,000

The trade discount is 10%
100 units manufactured during the initial testing were sold at Rs. 800 per unit.

The cost of the machine at initial recognition as per LKAS 16 (Property, Plant and Equipment):

	Rs. 23,430,000	(2)	Rs. 23,310,000	(3)	Rs. 23,110,000
	Rs. 20,280,000	(5)	Rs. 22,980,000		

02. Nethu PLC imported a machine on 01.03.2020 for use in the production by paying Rs.2,000,000. Following expenses were also incurred by the company in this respect.

	Rs.'000
Site preparation	160
Charges to connect power supply to the machine	10
Cost of the initial test run	20
Advertising cost on the production quality	60
Licensing fee paid to obtain approval for use of the machine	30
Cost of the inaugural ceremony of commissioning the machine	40

What is the cost of the machine at recognition as per LKAS 16 (Property, Plant and equipment)?

(1)	Rs. 2,160,000	(2)	Rs.2,180,000	(3)	Rs. 2,210,000
(4)	Rs. 2,220,000	(5)	Rs. 2,260,000		

03. The following information relates to motor vehicles of Kamal PLC.

Descriptio n	**Rs.' 000**
Carrying amount as at 01.04.2019	100,000
profit on a motor vehicle disposed on 30.09.2019	4,000
Acquisition of new motor vehicle on 31.12.2019	90,000

All the motor vehicle available at the beginning of the year have been purchased on 01.04.2016. The motor vehicle disposed during the year had been purchased at a cost of Rs. 120,000,000. The motor vehicle is depreciated at 20% per annum on the strait line method.

The depreciation for motor vehicle for the year ending 31.03.2020 and the sale proceeds of the motor vehicle disposed were:

	Depreciation (Rs.'000)	**Sales proceeds (Rs.'000)**
(1)	38,000	44,000
(2)	42,500	40,000
(3)	38,000	36,000
(4)	42,500	32,000
(5)	38,000	40,000

04. The following information relates to motor vehicles owned by a firm

	(Rs. 000)
Motor vehicles at cost as at 01.04.2019	400,000
Accumulated depreciation as at 01.04.2019	200,000
Proceeds from the sale of a motor vehicle on 30.09.2019 (Purchased on 01.04.2017 at a cost of Rs. 100,000,000)	70,000
Purchase of a motor vehicle on 31.12.2019	160,000

The motor vehicles are depreciated at 20% per annum on cost on the straight - line method and are available for use from the date of purchase. What is the depreciation for vehicle and the profit on the sale of the motor vehicle during the year ending 31.03.2020?

	Depreciation (Rs.000)	profit (Rs.000)
(1)	78,000	10,000
(2)	60,000	10,000
(3)	70,000	20,000
(4)	68,000	30,000
(5)	78,000	20,000

05. Manel PLC bought a machine on 01.04.2016 for Rs.1,000,000. On this day, its useful life and the residual value were estimated as 5 years and Rs.100,000 respectively. A main component of this machine was modified on 01.04.2019 incurring a cost of Rs.280,000. On this date, it was re – estimated that the remaining useful life of the machine as 4 years and its residual value as Rs.180,000.

Compute the following:

(a) Depreciation for the year ending 31.03.2020 : Rs. ....

(b) Carrying amount of the machine as at 31.03.2020 : Rs. ....

06. Which of the following statements is correct in relation to an asset recognized under LKAS 16 (Property, Plant and Equipment)?

(1) It is either a tangible or intangible asset held for use in the production of goods or supply of services.
(2) It is expected to be used for a period of more than one year.
(3) It is measured at recognition based on either cost model or revaluation model.
(4) All expenditure incurred subsequent to its recognition is always capitalized.
(5) Legal ownership is a necessary condition in order to recognize it as an asset.

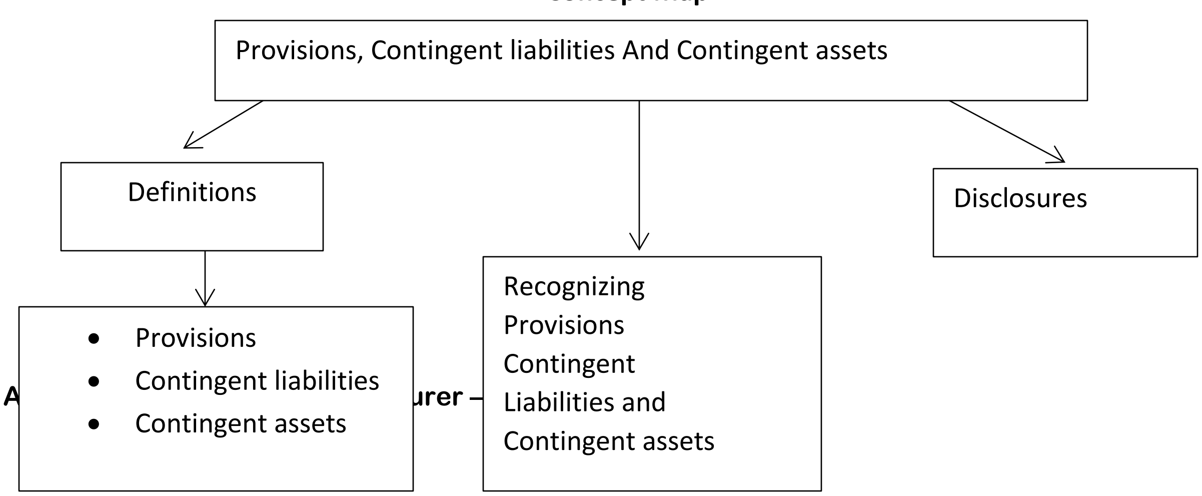
LKAS 37 Provisions, Contingent liabilities And Contingent assets

Learning outcomes

- Defines provisions, contingent liabilities and Contingent assets as per Sri Lanka Accounting standard.
- Compare provisions, Contingent liabilities and Contingent assets
- Recognition and disclosures according to Sri Lankan Accounting standard.

Basic terms and concepts

Concept Map



Guidance and subject matters:

Definitions according to standard

- **Provisions**
  <u>"is a liability of uncertain timing or amount"</u>
- Contingent liability
  A possible obligation that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events wholly with in the control of the entity.

  A present obligation that arises from past events but is not recognized because:
  I. It is not probable that an outflow of resources embodying economic benefits will require setting the obligation.
  II. The amount of the obligation cannot be measured with sufficient reliability.
  <u>If above conditions satisfied it could be recognized as an expense in the income statement and should show under current liabilities.</u>

Examples for provisions

- Provision for warrantee
- The government or any organization files a case selecting comprehensive or environmental pollution.
- An employment files a case seeking compensation as he was terminated from the employment. Amount could be reliably estimated.

Examples for Contingent liabilities

- An employee files a case seeking compensation as he was terminated in the current year and the amount could not be reliably estimated.
- Compensation payable due to closure of section of the business.

Examples of contingent assets

- The compensation claimed for a land which was taken over by the Road Development Authority.

<u>Past Paper questions</u>

<u>Activity 01 (2012 a/l)</u>

Which of the following would be disclosed as contingent liabilities of an entity?

A-A loan obtained from a financial institution.
B- An unresolved lawsuit against the entity.
C- An agreement to act as a guarantor for a loan obtained by another firm.
D- An overdrawn balance of the bank account.

(1) A and B only. (3) B and C only. (5)A,B and C only.
(2) A and C only. (4) A,B and D only. (….)

Activity 02 (2014 a/l)

State whether the following statements are true or false as per the relevant Sri Lanka accounting standard indicating with a 'tick' in the appropriate column.

Statement	True	False
A-Provision is a liability of uncertain timing or amount	....	....
B-Contingent liabilities are recognized in the financial Statement of a firm	....	....

Activity 03 (2015 a/l)

Which of the following items are recognized as provisions for liabilities in the Statement of Financial Position of a company as per LKAS 37 (Provisions, Contingent Liabilities and Contingent Assets)?

A- Provision for doubtful debts.
B- Provisions for a compensation claimed by employees.
C- Provision for depreciation.
D- Provision for warranty claims.

1) A and D only 2) B and D only 3) A, B and C only
4) B, C and D only 5) All A, B,C and D (....)

Activity 04 (2016 a/l)

A store selling electrical items has a policy of refunding the price for goods purchased by customers when there are defects. However, there is no such legal obligation. State the three criteria that should be satisfied to recognize a provision in this situation in items of LKAS 37 (Provisions, Contingent liabilities and Contingent assets.)

1)...
2)...
3)...

Activity 05 (2017 a/l)

Which of the following conditions/s should be satisfied in the recognition in accordance with LKAS 37 (Provisions, Contingent Liabilities and Contingent Assets)?

A- An entity has a present legal or constructive obligation resulting from a past event
B- There is a probable outflow of resources embodying economic benefits to settle the obligation
C- A reliable estimate can be made of the amount of the obligation

1)A only 2) C only 3) A and B only

4)B and C only 5) All A ,B, and C

Activity 06(2018 a/l)

State whether the following statement are true (T) or False (F) according to Sri Lanka accounting standards.

Statement	T/F
A- Provisions are 'possible obligations' with uncertain timing or amount	……………………………
B- Contingent liabilities are disclosed in the notes to financial statements	……………………………

Activity 07(2019 a/l)

Select the correct term indicated in parenthesis below to denote the nature of characteristics of provisions and other liabilities as per LKAS 37 (Provisions, contingent liabilities and contingent Assets.)

characteristics	provisions	Other Liabilities
A - Existence of a present obligation **(Yes/No)**	……………..	……………..
B - Amount payable on settlement **(Certain/Uncertain)**	……………..	……………..
C - Timing of settlement **(Certain/Uncertain)**	……………..	……………..

Activity 08(2020 a/l)

Gamage PLC Sells products with one year warranty period. The provision for warranty as at 01.04.2019 was Rs.525 000. The 'warranty expenses paid' and the 'warranty expenses recognized' for the year ending 31.03.2020 were Rs.375 000 and Rs.650 000 respectively.

What are the provisions for warranty to be recognized in the statement of financial position as at 31.03.2020 as per LKAS 37(Provisions, contingent liabilities and Contingent Assets)?

(1) Rs.150 000 (2)Rs.275 000 (3) Rs.650 000
(3) Rs.800 000 (5)Rs.1 175 000

LKAS 10 Events after Reporting period

Basic terms and concepts

Guidance on subject matter

Events after reporting period

"Are those events favorable and unfavorable that occur between the end of the reporting period and the date when the financial statements are authorized for issue "

Period where events after reporting occurred

2014/04/01
(reporting period beginning date)

31.03.2015
Closing date

10.08.2015
The date authorized by the directors

Classification of events after reporting period

Adjusting events

Evidence provides that existed at the reporting sheet date

Adjusting events

Example:

A debtor who existed at 31.03.2015 was bankrupt before authorization (10.08.2015) should be adjusted as at 31.03.2015.

Judgement given for a pending court case after the reporting period

Selling of stock less than cost value after the reporting periods which were held at the end of the period

Actual value of an asset purchased during the period was decided after the reporting period.

Non adjusting events

Events those are indicate of conditions that arose after the reporting date

Non adjusting events

Example:

Part of stocks as at 10.05.2015 was destroyed by fire. This event dose not affects the stocks as at 31.03. 2015.But it should be disclosed for the year ended 31.03.2015. This should be adjusted during the next accounting period.

Proposed divided for ordinary share holder after the reporting period.

Reduction in market value of investment after the reporting period.

A part of a building taken over by the government after reporting period

Dissimilarities between adjusting and non-adjusting events

Adjusting events	Non adjusting events
• Provides at the end of the reporting period	❖ Presents a situation existed after the reporting
• These would affect profit and loss, and statement of other comprehensive income and statement of financial position.	• Do not affect on profit and loss statement of other comprehensive income and statement of financial position
• Adjusting event in financial statement	• Non adjusting events in financial statements
• Disclosure and adjusting needed	• Disclosure by way of a note

Disclosure requirements

- ❖ Date of authorization for issue
- ❖ The person who authorizes
- ❖ Disclosure the situation as at the end of the period
- ❖ Nature of non-adjusting events
- ❖ Elements in financial effect

Assignment 47

List of transaction

Accounting period : 01.04.2016 - 31.03.2017
Date of Authorization : 15.08.2017

On 10.05.2017 it is proposed to pay 10% dividends for ordinary shareholders of Subodha PLC company
Value of investment on 31.03.2017 was Rs.450 000 directors decided that market value of investment of 15.08.2017 was Rs.350 000
Court decided to pay a compensation of Rs.150,000 0n 15.04.2017 to employee who has filed a case against the company.
Death of a debtor worth Rs.50,000 informed on 20.04.2017 who was existed at 31.03.2017.
Closing stock value as at 31.03.2017 amounted to be Rs.600,000. out of the Stock's closing Rs.100,000 was sold on 10.04.2017 for Rs.75,000
On 10.07.2017 a part of a build destroyed by fire and estimated loss is Rs.500,000.
On 10.07.2017 an insurance company agrees to pay a insurance claim of Rs.200,000 which were damaged at the end of the accounting year
The government has taken a land which belongs to the company on 12.07.2017 estimated value is Rs.15,000,000.

Past Paper questions

2012 A/l

Madura PLC's financial statement for the year ending 31.03.2012 were authorized by its directors on 30.06.2012. During the period between 01.04.2012 and 30.06.2012 the following events took place in the company.

A-An announcement of a plan to discontinue the operations of a business unit which was incurring loses continuously.
B- Bankruptcy of a debtor who owed a substantial amount as at the balance sheet date.
C- Decline in the value of short-term investments owing to a drop in the market place.
D- Decision of a court case that confirmed recognition of a liability as at the balance sheet date.

Which of the above events should be adjusted on the balance sheet date?

(1) A and C only. (3) A,B and D only. (5) All A, B, C, and D
(2) B and D only. (4) B,C and D only. (….)

2013 A/L

Financial statements of Nandana PLC for the year ending 31.03.2013 were authorized by the directors on 31.05.2013. The annual General Meeting of the Company was held on 15.06.2013. The following events place in relation to the company after 31.03.2013.

A- Decline in the market value of its investments in companies listed on the Colombo Stock Exchange from 01.04.2013 to 20.04.2013.
B- Decision of a court case delivered on 30.04.2103 confirming that the company is liable to pay compensation to a major customer who had filed a case against the company on 01.10.2013.
C- Declaration of a final dividend of Rs.2 per share on 10.06.2013 for the year ending 31.03.2013.
D- Sale of inventory on 25.05.2013 at a price lower than its cost at 31.03.2013.

Which of the above events should be adjusted in the financial statements as at 31.03.2013?

(1) A and C only (2) A and D only (3) B and D only
(4) B, C and D only (5) All A, B, C and D (…….)

2014 A/L

The accounting year of a company ended on 31.03.2014. the directors authorized the issues of financial statements on 30.06.2014. The annual general meeting of the company was held on 15.07.2014. The following events took place in relation to the company after 31.03.2014.

A- A debtor with a balance of Rs.500 000 as at 31.03.2014 was declared bankrupt on 30.04.2014.
B- A debtor with a balance of Rs.800 000 as at 31.03.2014 was declared bankrupt on 10.07.2014.
C- The inventory value at a cost Rs.600 000 as at 31.03.2014 was sold for Rs.550 000 on 10.04.2014
D- The market value of investments had reduced by Rs.300 000 during the period on 30.06.2014

Which of the above event should be adjusted in the financial statements for the year ending 31.03.2014?

(1) A and B only
(2) A and C only
(3) B and C only
(4) A, C and D only
(5) B, C and D only

2015 A/L

The financial statements of Nalanda PLC for the year ending 31.03.2015 were authorized by the directors on 15.05.2015. The Annual General Meeting of the company was held on 30.05.2015. The following events took place in the company after 31.03.2015.

A- A debtor who owed Rs.750 000 as at 31.03.2015 was declared bankrupt on 20.04.2015.

B- Inventory with a cost of Rs.800 000 as at 31.03.2015 was sold for Rs.720 000 on 30.04.2015.

C- The judgement of a court case was delivered on 25.05.2015 confirming a liability of Rs.500 000 as at 31.03.2015.

D- A final dividend of Rs.3 per ordinary share was declared on 15.05.2015.

Which of the above events should be adjusted on the financial statement of the company or the year ending 31.03.2015 as per LKAS 10 (Events after the Reporting Period)?

1) A and B only
2) C and D only
3) A, B and C only
4) B, C and D only
5) All A, B, C, and D

(....)

2016 A/L

The financial statements of Isuru PLC for the year ending 31.03.2016 were authorized by the directors on 15.06 2016. The following events took place in the company during the period 31.03.2016 to 15.05.2016.

A- Announcement of a plan to discontinue a segment of the business from 15.04.2016. Which is expected to cave Rs.600 000 annually.

B- Destruction of a main production plant by fire on 20.04.2016 causing a loss of Rs.1 000 000.

C- Bankruptcy of a debtor on 30.05.2016 who had a balance of Rs.750 000 arising from a credit sale made on 30.04.2016.

D- Declaration of the final dividend of Rs.300 000 for ordinary shareholders on 15.06.2016

Which of the above events are considered as non-adjusting events for the year ending 31.03.2016 as per LKAS 10 (Events After the Reporting Period)?

1) A and B only
2) B and C only
3) A, C and D only
4) B, C and D only
5) All A, B, C, and D

(....)

2017 A/l

The financial statements of Amila PLC for the year ending 31.03.2017 were authorized by the directors on 30.06.2017. The following events took place in the company from 31.03.2017 to 30.06.2017

A. Decline in the market value of an investment of the company continuously from 01.05.2017.
B. Declaration of the bankruptcy of a debtor by a court of law on 19.05.2017 who had purchased goods on credit on 01.03.2017.
C. Destruction of inventory that had been in existence from 31.03.2017 due to a fire occurred on 30.05.2017.
D. Receipt of a letter from the government on 20.06.2017 informing that a land owned by the business as at 31.03.2017 will be acquired in order to construct a road

Which of the above events are considered as **non-adjusting events** in the financial statements of the company for the year ending 31.03.2017 as per LKAS 10 (Events After the Reporting period)?

(1) A and B only (2) A and D only (3) A,C and D only

(4) B,C and D only (5) All A,B,C and D

2018 A/l

The financial statements of Anjula PLC for the year ending 31.03.2018 were authorized by the directors on 15.05.2018 and the annual general meeting of the company was held on 30.05.2018. The following events took place in the company after 31.03.2018.

A. A building costing of Rs.1 000 000 was destroyed to a fire that occurred on 10.04.2018
B. A debtor who owed Rs.500 000 was declared bankrupt on 05.05.2018. This debtor's balance arose due to a sale of goods on 05.04.2018.
C. A tax estimate of Rs.400 000 payable for the vehicle imported on 31.03.2018 was informed to the company by the Sri Lanka Customs on 10.05.2018

Which of the above events should be adjusted for, in the financial statements of this company for the year ending 31.03.2018 as per LKAS 10 (Events After the Reporting period)?

(1) A only (2) B only (3) C only

(4) A and B only (5) B and C only

2019 A/l

The financial statements of Tharaka PLC for the year ending 31.03.2019 were authorized by the directors on 20.06.2019. Following events had been taken place in the company during the period 31.03.2019 to 20.06.2019.

A. A trade debtor who owed Rs.500 000 as at 31.03.2019 was declared bankrupt on 28.05.2019
B. The value of investments of shares in quoted public companies as at 31.03.2019 declined by Rs.1 000 000 by 20.06.2019.
C. The judgement of the court case, which has been filed against the company on 05.04.2019, was delivered on 01.06.2019 ordering to pay a penalty of Rs.4 000 000 to the government.

Which of the above events should be adjusted for, in the financial statements of this company for the year ending 31.03.2019 as per LKAS 10 (Events After the Reporting period)?

(1) A only (2) B only (3) A and B only

(4) A and C only (5) B and C only

2020 A/l

The financial statements of Ajith PLC for the year ending 31.03.2020 were authorized for issue by the directors on 15.06.2020. The following events had taken place in the company during the period 31.03.2020 to 15.06.2020.

A. A machine with a carrying amount of Rs.5 million as at 31.03.2020 was completely destroyed due to fire on 15.04.2020
B. A trade debtor who owed Rs.800 000 as at 31.03.2020 was declared bankrupt by the court on 10.05.2020.
C. A public issue of Rs.10 million shares was made on 10.06.2020.

Which of the above events are considered as **non-adjusting events** in the financial statements of the company for the year ending 31.03.2020 as per LKAS 10 (Events After the Reporting period)?

(1) A only (2) C only (3) A and C only

(4) B and C only (5) All A,B and C

2021 A/l

Anuradha PLC produces and sells electronic goods. There was a court case in progress as at 31.03.2021. Relating to defective goods sold to a customer. As per the legal advice, the company made a provision of Rs.50 000 in this respect on 31.03.2021. On 25.04.2021, the court ordered the company to pay Rs.75 000 as compensation to the customer. The directors of the company authorized on 15.05.2021 to issue the financial statements for the year ending 31.03.2021.

State whether this court order would lead to an adjusting event or a non-adjusting event as per LKAS 10 (Events after the Reporting Period)

……

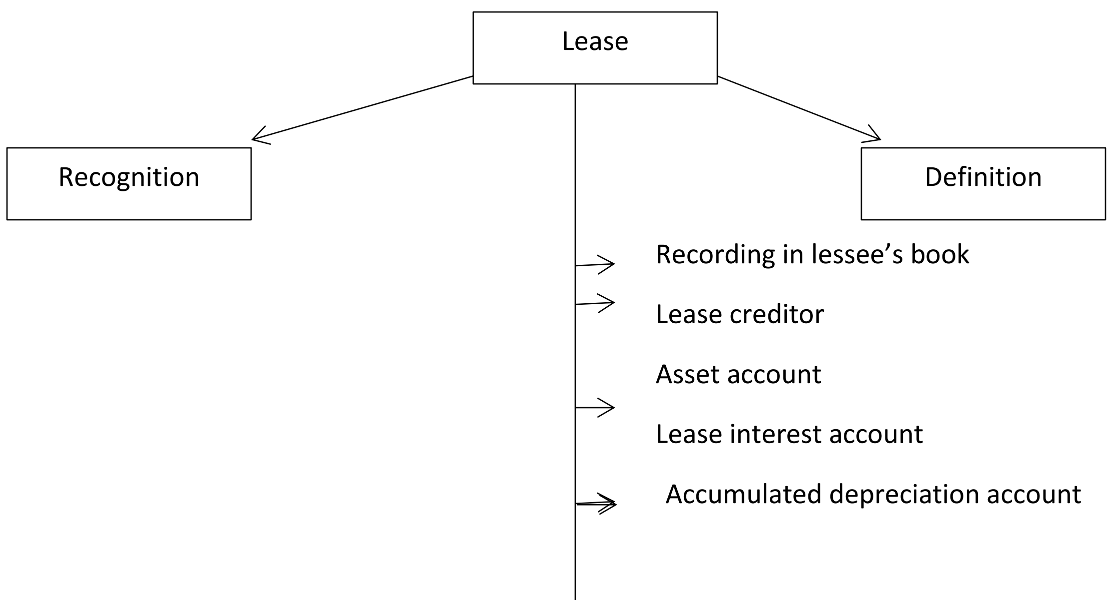
SLFRS 16 / LKAS 17LEASE

Learning outcomes:

- Defines leases according to the Sri Lanka Accounting Standard
- Records leases in books of purchaser
- Accounting for interest on lease
- Presents how to show lease creditors on statement on of financial position

Basic terms and concepts

Concept map



Proposed instructions for learning

- Parties related to lease- lessee and lessor
- Assets acquired terms- building, machines, and motor vehicles, equipment
- Lease means- A lease is an agreement whereby the lessor conveys to the lessee. The right to use as asset for an agreed period in return for a payment or senses of payment
- Risk and rewards of rights to use of lease property

Risks	Rewards
• Idle capacity • Technical obstacles • Maintenance and repair	• Generating of economic benefits • Increases in asset value • Gain from appreciation in value

The accounting for the lease in the books of the lease

- **Lower of fair value or present value of right of use of lease property**
  Relevant asset account Dr xxx
  Lease creditor account Cr xxx
- **Initial deposit value/ down payment**
  Lease creditor account Dr xxx
  Cash account Cr xxx
- **Payment of installment**
  Lease interest expense account Dr xx
  Lease creditor account Dr xx
  Cash account Cr xx
- **Adjustment of depreciation t the year-end balance of the asset**
  <u>If title transferred at the end of the lease period</u>

  Calculation of depreciation = $\dfrac{\text{fair value - Residual value}}{\text{Useful economic life}}$

  <u>If title not transferred at the end of the lease period</u>

  Calculation of depreciation = $\dfrac{\text{fair value - Residual value}}{\text{Lease period}}$

Relevant Depreciation account Dr xxx
Relevant accumulated depreciation account Cr xxx

Presenting closing lease creditor value on statement of financial position

Current liabilities

Annual installment	xx
Next year lease interest	(xx)
Current portion of lease	xx

Non-current liabilities

Closing lease creditor value	xx
Current portion of lease creditor value	(xx)
lease creditor	xx

Assignment 01

Amanda PLC Ltd purchased a machine on 01.04.2017 for financial lease. Following transactions are providing.

Fair value of the machine	Rs.1,541,992
Initial payment	Rs.400,000
Annual instalment at the yearend	Rs.400,000
Lease period	4 years
Useful economic life	5 years
Residual value	Rs.41,992

Title is transferred at the end of the lease period

Following is the interest for each year

Year	interest on lease
2107/2018	171 289
2018/2019	136 994
2019/2020	97 174
2002/2020	52 174
Total interest	**457 999**

Required

01. If title is transferred at the end of the lease period
    a) Relevant journal entries and accounting for annual depreciation for the year ended 31.03.2018
    b) Relevant ledger account and accounting for annual depreciation for the ended 31.03.2018
    c) Discloser requirement in financial statement for the year ended 31.03.2018
02. If title is not transferred at the end of the lease period
    a) Relevant journal entries and accounting for annual depreciation for the year ended 31.03.2018
    b) Relevant ledger account and accounting for annual depreciation for the ended 31.03.2018
    c) Discloser requirement in financial statement for the year ended 31.03.2018

Assignment no 02

On 01.04.2016 Sahan Ltd acquired a motor vehicle on financial leases terms

Following details are provided

Fair value of motor vehicle	Rs. 2 300 000
Lease period	5 years
No initial deposit	
Annual lease installment (paid at the end of each year)	Rs.606 800
Annual interest	10%
Useful life of the motor vehicle	5 years
Residual value	Rs. 300 000

Required
Relevant journal entries and ledger accounts of Sahan Ltd for the year ended 31.03.2017

Assignment 03
A firm bought a machine under a finance lease on the following terms
The lease term is 3 years
Annual installment of Rs.250 000 is payable at the year end
The interest rate implicit in the lease is 10%
Present value of minimum lease payment is Rs.621 725

01. Write the journal entry to recognize the lease liability at the commencement of the lease in lessee's book
02. Calculate the following in lessee's book
    a) Interest on lease for year one
    b) Lease liability at the end of year one
03. Prepare extracts of financial statements for the year one.

Assignment 04

Gold Motors PLC acquired a moto vehicle worth Rs. 5 000 000 on 01.04.2017 from Kelani PLC on a finance lease.

Lease term period is 7 years it is paid with equal installments
The first installment on 31.03.2018 was Rs.1 000 000 (inclusive lease interest was of Rs.120 000)
Lease interest of the second year - Rs.100 000

State the values relevant for the following items that should be disclosed in statement of financial position of gold motors PLC as at 31.03.2018

1. Non-current liabilities Rs ……………………………
2. Current liabilities Rs……………………………

Assignment 05

On 01.04.2017 machine was purchased on a finance leasing and related information are a follows

Fair value of machine	Rs. 1 200 000
Down payment	Rs. 400 000
Lease installment	Rs.300 000
Lease period	4 years
Useful life of machine	5 years
Scrap value of machine	Rs. 200 000

- Lease interest included in first and second installment were Rs.160 000 and Rs.140 000 respectively. First installment was paid on 31.03.2018
- Lease installment should be paid at the end of each financial year

Required
1. Extracts to statement of profit or loss and other comprehensive income for the year ended 31.03.2018
2. Extracts of statement of financial position as at 31.0.2018 showing all amounts related to lease liability.

Initial recognition – lease liability

Measure the lease liability at present value of the lease payments

Assignment 07

Supun PLC acquired a machine on lease basis on 01.04.2017. following information is provided.

Initial payment on 01.04.2017 Rs.200 000
Annual installment is Rs 80 000 starting from 31.03.2018
Lease term 4 years
Initial direct cost incurred on 01.04.2017 by lessee Rs.10 000
The interest rate implicit in lease 10%
Depreciation provided for machinery 20% on straight line basis
Discounting actors at 10% rate

Year	1	2	3	4
Discounting factor	0.909	0.826	0.751	0.683

Required

1. The amount of lease liability
2. The amount to be recognized as right of use of lease property.

Assignment no 08

A company acquired a motor under lease agreement on 01.04.2018 and following information are relevant for it. Life time motor vehicle is 5 years. Lease term 4 years. down payment is Rs.400

Annual installment	Rs
Year 1	600
2	500
3	400
4	300

At the end of the agreement the lease should pay Rs.100 000 in addition annual installment. The company spent Rs.300 00 to take the asset to expected usable condition. The interest rate implicit in agreement is 10%

Discounting factors at 10% rate

Year	1	2	3	4
Discounting factor	0.91	0.83	0.75	0.68

Required

Relevant ledger accounts and extracted of financial statements

Past Paper questions

2013 A/L

- **Use the following information to answer question No 43 and 44.**

A firm bought a machine under a finance lese on the following items:

- The lease term is 3 years.
- Annual installment of Rs.250 000 is payable at the year-end.
- The interest rate implicit in the lease is 10%
- Present value of minimum lease payments is Rs.621 725.

Write the journal entry recognize the lease liability at the commencement of the lease in lessee's books.

(Narration is not required)

………

………

Calculate the following in lessee's books:

(a) Interest on lease for the year on (Rs.) ………………………………………………………………………………………

(b) Lease liability at the end of year one (Rs.) ……………………………………………………………………………….

2016 A/L

1.State two criteria used in classifying a lease as a finance lease in terms of LKAS 17 (Lease)

1) ……..
2) ……..

2018 A/l

Gamage PLC acquired a motor vehicle on 01.04.2017 on a finance lease. On this date the fair value of the motor vehicle was Rs. 5 400 000 and a down payment of Rs. 1 400 000 was paid on the same day. A lease installment of Rs 1 262 000 is payable on 31st March of each year over the lease term of 4 years. The first installment was paid on 31.03.2018. The interest rate implicit in the lease is 10% per annum.

The lease liability presented as a current liability and a non-current liability in the statement of financial position as at 31.03.2018 as per SLFRS 16 lease

	Current liability	non-current liability
1.	862 000	2 189 800
2.	852 000	3 138 000
3.	948 200	2 189 800
4.	948 200	3 138 000
5.	1 262 000	1 876 000

2020 A/l

Sachin plc entered into a lease agreement on 01.04.2019 to obtain right of use of a machine for a period of 4 years. On this date, the initial measurement of the lease liability was Rs.1 713 000. According to the lease agreement, the annual lease rental is Rs.600 000 and the first installment was paid on 31.03.2020. The lease interest for the year ending 31.03.2020 and 31.03.2021 are Rs.257 000 and Rs.205 500 respectively.

The lease liability presented in the statement of financial position as at 31.03.2020 as per SLFRS 16 (Lease)

a) Current Liabilities: Rs. …………………………………………………..
b) Non-Current Liabilities: Rs. …………………………………………………..

SLFRS 15 Revenue from contracts with customers

1. **Core principle**
   The core principle is that an entity will recognize relevant at an amount that reflects the consideration to which the entity expects to be entitled in exchange for transferring goods or services to a customer.
2. **Revenue recognition**
   Revenue from contracts with customers states that an entity recognized revenue by applying the following five steps;
   01. Identify the contract(s) with a customer
   02. Identify the performance obligation in the contracts
   03. Determine the transaction price
   04. Allocate the transaction price to the performance obligation in the contract
   05. Recognize revenue when the entity satisfies a performance obligation

The five step model of SLFRS 15 on revenue recognition is given in detail below

<u>Step 1 – Identify the contract</u>

According to SLFRS 15, contact is an agreement which creates enforceable rights and obligations. Such contacts may be written, oral or implied by an entity's customary business practices.

If an entity has an established practice of starting performance based on oral agreement with its customers, it may determine that such oral agreement meet the definition of a contract.

An entity can only account for revenue from a contact if it meets the following criteria;

a) The parties to the contact have approved the contract and are committed to perform their respective obligations;
b) The entity can identify each party's rights regarding the goods or services to be transferred
c) The entity can identify the payment terms for the goods or services to be transferred
d) The contact has commercial substance (i.e. the risk, timing or amount of the entity's future can flow is expected to change as a result of the contract)
e) Is it probable that the entity will collect he consideration to which it will be entitled in exchange for the goods or services that will be transferred to the customer.

<u>Step 2 – Identify the separate performance obligations within contact</u>

An entity has to determine which of the promised goods and services will be treated as separate performance obligations.

Promised goods and services in a revenue contract represent separate performance obligations if the goods or services are distinct. (By themselves, or as parts of a bundle goods and service)

Of a promised good or service is not distinct, an entity should combine that good or service with other promised goods or services until it identifies a bundle of goods or services that, together, is distinct.

SLFRS 15 outlines a two-step process for determining whether a promised good (or service for a bundle of good and services) is distinct.

- Consideration at the level of the individual good or service (i.e. the good or service is capable of bring distinct)
- Consideration of whether the good or service is separate from other promises in the contract (i.e. the good or service is distinct within the context of the contract)

Both of these criteria must be to conclude that the good or service is distinct. Of these criteria are met, the individual good or service must be accounted for as a separate unit of account (I.e. performance obligation)

Some revenue contracts more than one performance obligations

For example:

- ❖ Sale of software with implementation and maintenance
- ❖ Provide a meal at a hotel with a discount of price for a future reservation
- ❖ Sale of an apartment with free maintenance for one year

Principal Vs Agent considerations

When more than one party is involved in providing goods or services to a customer, SLFRS is requires an entity to determine whether it is a principal or an agent in these transactions by evaluating the nature of its promise to the customer.

- ❖ An entity is a principal if it contracts a promised good or service before transferring that good or service to the customer.
- ❖ An entity is an agent if its role is to arrange for another entity to provide the goods or services

If any entity is the principal, it should records revenue on a gross basis and if the entity acts as an agent, records as revenue the net amount that it retains for its agency services.

<u>Step 3 – Determine the transaction price</u>

The transaction price is the amount of consideration to which an entity expects to b entitled in exchanges for transferring promised goods or services to a customer, excluding amounts collected on behalf of third parties

The consideration promised in a contract with a customer may include fixed mounts, variable amounts, or both.

When determining the transaction price, the impact of following must be considered.

- Variable consideration
- Significant financing components
- Non cash consideration
- Consideration payable to a customer

Variable consideration

If the consideration promised in a contact includes a variable amount, an entity shall estimate the amount of consideration to which the entity will be entitled in exchange for transferring the promised goods or services to customer.

An amount of consideration can vary because of discounts, rebates, refunds, credits, price, concessions, incentives, performance bonuses, penalties or other similar items.

This estimate can only be included in the transaction price to the extent that it is highly probable that a significant reversal in the amount of cumulative revenge recognized will not occur when the uncertainty is subsequently resolved.

Step 04 – Allocate the transaction price to the performance obligations in the contract

The allocation objective is to allocate the transaction price to each performance obligation in an amount that depicts the amount of consideration to which the entity expects to be entitled.

This allocation needs to be done in proportion to stand alone selling prices.

The best evidence of a stand-alone selling price is the observable price when the good service is sold separately.

If a stand-alone selling price is not directly observable then it must be estimated. Observable inputs should be maximized whenever possible.

If a customer is offered a discount for purchasing a bundle of goods and services, then the discount should be allocated across all performance obligations within the contract in proportion to their stand-alone selling prices.

Step 5 – Recognize revenue when (or as) a performance obligation is satisfied

According to SLFRS 15, an entity only recognize revenue when it satisfies as identified performance obligation by transferring a promised good or services to a customer.

A good or service is considered to be transferred when the customer obtains control

An entity must determine at contract inception whether it satisfies the performance obligation over time or satisfies the performance obligation at a point in time.

Recognition of revenue over time

SLFRS 15 states that an entity transfers control of a good or service over time (and, therefore, satisfies a performance obligation and recognition revenue over time) if one of the following criteria is met.

a) The customer simultaneously receives and consumes the benefits provided by the entity's performance as the entity performs.
b) The entity's performance creates or enhances as asset (e.g work in progress) that the customer controls as the asset is created or enhanced; or
c) The entity's performance does not create an asset with an alternative use to the entity and the entity has an enforceable right to payment for performance complete to date

If a performance obligation is satisfying over time, then revenue is recognized over time based on progress towards the satisfaction of that performance obligation.

Assignment 01

The following example may help you to understand the core principle of the SLFRS 15 revenue recognition model.

On 1st January 2018 Z co. entered into an agreement with a customer to sell air conditioner along with maintenance services for 2 years. Z co. delivers that air conditioner and the legal ownership of the equipment to the customer at the inception.

The customer agreed to pay LKR 120,000/- for both air conditioner and maintenance service. If sold separately, the selling price of the air conditioner is LKR 100,000 and the selling price of the maintenance services is LKR 50,000.

Requirement

Apply the five-step model of SLFRS 15 and estimate how much revenue Z c. should recognize for the year ended 31.12.2018.

<u>Application of five steps model</u>

<u>Step 1 – identify the contract</u>

There is an agreement between Z Co. & its customer to provide the goods and services as specifies in the agreement.

<u>Step 2 – identify the separate performance obligations within contract</u>

There are two performance obligations (promises) within the contact

- Sale of the air conditioner
- Sale of maintenance services

<u>Step 3 – determine the transaction price</u>

The total transaction price is LKR 120,000

<u>Step 4 – Allocate the transaction price to the performance obligations in the contract</u>

Based on the given stand-alone selling price LKR 120,000 should be allocated to two performance obligations (POs) as follows:

Identified POs	Stand-alone selling prices (LKR)	Transaction price allocation (LKR)
1. Air conditioner	100,000	80,000 (100,000/150,000*120,000)
2. Maintenance service	50,000	40,000 (50,000/150,000*120,000)
Total	150,000	120,000

Step 5 – Recognize revenue when (Or as) a performance obligation is satisfied.

- Control over the air conditioner has been transferred to the customer at the inception. So, the full revenue of LKR 80,000 allocated to the supply of the air conditioner should be recognized on 1st January 2018.
- The maintenance services are provided overtime, so the revenue allocated to this should be recognized overtime for the year ended 31 December 2018, revenue of LKR 20,000 (1/2* LKR 40,000) should be recognized for the year 31/12.2018 & A provision of maintenance services should be provided to the unearned revenue Rs.20 000 for the year ending 31.12.2018.

Assignment no 02

Century link is a telecommunication company selling branded tablet units and providing network connection facilities. Company entered into a contact with a customer to supply a tablet and provide network service facility for 2 years for a monthly rental of Rs.10 000/-

The market price of the tablet is Rs.80 000/- and network charge is Rs.5,000/- per month

Required

You are required to show the accounting entries for year 01 and year 02 for the recognition of revenue in line with SLFRS 15

Past Paper questions

2019 A/l

State the following as per SLFRS 15 (Revenue from Contracts with customers)

a) When to recognize revenue of an entity:
………
………

b) Definition of 'Transaction price':
………
………
………

2020 A/l

State whether the following statements are True (T) or False (F) as per SLFRS 15 (Revenue from Contracts with customers)

Statement	True/False
A. A contract with a customer could include several 'performance obligations'	………………………..
B. Revenue and all other income of a business entity should be recognized in Financial statements only as per this standard.	………………………..

C. An entity should recognize revenue on a contract only when each performance Obligation in the contract is satisfied ………………………..

D. The transaction price is the amount of consideration to which an entity expects To be entitled in exchange for transferring promised goods or services to a customer ……………….

2021 A/l

Suranga PLC sells machinery in the local market. The installation of these machinery is also carried out by the company as it requires a specialized knowledge. The selling price and the installation fee of a machine are Rs.3 000 000 and Rs.400 000 respectively. The company entered into a contract to sell and install 05 machines on 01.03.2021. The company has delivered 03 machines and completed the installation of 02 of these machines by 31.03.2021. The company received an advance of Rs.11 000 000 for this contract on 01.03.2021

Identify the following for this contract as per SLFRS 15 (Revenue from contracts with customers).

(a) Revenue recognized for the year ending 31.03.2021: Rs…………………………………

(b) Unearned Revenue as at 31.03.2021 : Rs…………………………………

2022 A/l

Amali PLC is a company engaged in renting of power generators. The daily rental of the power generator is Rs.20 000. On 29.03.2022, the company entered into a contract to rent a generator to saman PLC for a period of 7 days. The company received Rs.100 000 as an advance on this date. This advance includes a refundable deposit of Rs.50 000. The generator was delivered to the business premises of Saman PLC in the early morning of 30.03.2022.

Identify the following for this contract as per SLFRS 15 (Revenue from contracts with customers).

(a) Rent income recognized for the year ending 31.03.2022: Rs…………………………………

(b) Unearned Rent income recognized as at 31.03.2022 : Rs…………………………………

AKILA FERNANDO

PCM at (SLIM) / PGDip in Mkt Mgt.

Affiliate Member of ACCA

BSc. in Applied accounting (oxford Brookes university U.K.) UG

0776340075 (WhatsApp)