

EXAMINER'S REPORT
LEVEL III EXAMINATION - JULY 2024
(301) FINANCIAL REPORTING

Most of the common mistakes made by the candidates have been identified. The unsuccessful candidates should identify the mistakes which they made and learn all the principles in order to be successful at the future examinations:

SECTION A

Question No. 01

- (a) This question consists of sub parts (i) and (ii) and which required to explain the concepts of a reporting entity and an economic resource as per the conceptual framework for financial reporting.

Most of the candidates have not attempted this question. Some candidates wrote the components of financial statements as the reporting entity. Some wrote in general saying it is a kind of an entity which reports financial transactions without saying preparing financial statements. This was due to lack of knowledge about a reporting entity.

However, many candidates wrote the definition of an economic resource according to economics, explaining factors of production such as land, labor, capital, and entrepreneurship as resources. This indicates that the candidates did not fully understand the requirements of the question. Economic resources should produce economic benefits; however, many candidates referred to them simply as benefits instead of specifying economic benefits. Additionally, some mentioned limited supply, scarcity, and opportunity cost as resources.

- (b) The examiner expected candidates to explain the objective of general-purpose financial statements. The performance on this part was satisfactory. Although the majority of candidates attempted this section, comprehensive answers were lacking. They noted that financial reporting provides information for interested parties but failed to mention that this information is useful for those parties in making decisions.

Question No. 02

- (a) This part was required to identify three types of capital included in an Integrated Report. Many candidates identified components of integrated reporting, such as the business model, value creation, and strategy, as the types of capital in an Integrated Report. This demonstrates a lack of knowledge about Integrated Reporting, even though it has been tested continuously at this level.

- (b) The requirement of this part of the question was to state two objectives of the Integrated Reporting. The majority of candidates repeated the objectives of financial statements that they answered in Question No. 1, **Part (b)**. This shows a lack of reading and understanding the question, particularly in differentiating between the objectives of general-purpose financial statements and those of integrated reporting.

Question No. 03

This question related with deferred tax and it was required to calculate deferred tax asset / liability and tax expenses for the year. Candidates' performance was at a very poor level. Most of candidates did not understand how to determine the tax base and temporary differences. Very few candidates accurately computed deferred tax liabilities and tax expenses, indicating a lack of understanding of deferred tax.

Question No. 04

The requirement of this question is to calculate goodwill arising from consolidation. The performance of this part was good. However, some candidates were not considered market value appreciation of motor vehicles in calculating net assets. Thus, arrived a wrong amount of goodwill. Also some candidates omitted the value of NCI from the goodwill computation which shows lack of knowledge on goodwill computation.

SECTION B

Question No. 05

- (a) It was required to calculate borrowing costs to be capitalized as per LKAS 23. Though final bill of the construction was raised on 30th November 2023, many candidates have computed till the end of financial year i.e. up to 31st December 2023. They failed to understand that final bill is raised at the completion of the construction. This shows a lack of understanding about the cessation of borrowing cost to be capitalized which is to till end of the completion of construction.
- (b) It was required to explain how each of the four instances mentioned would be recognized as per LKAS 10- Events after the Reporting Period. Most of the answers written saying whether the scenario is adjusting or non-adjusting event. But failed to mention whether it has to be disclosed or not for a non-adjusting event.

Question No. 06

- (a) It was tested how to calculate the impairment loss of motor vehicle as per LKAS 36. Many candidates have computed impairment loss as Rs.100,000/- by comparing "Fair Value" and "Value in Use" where they failed to compare with Carrying Value. Some candidates have not highlighted that higher of 'Fair Value' and 'Value In Use' should be considered.
- (b) It was expected is to identify the revenue for the years ended 31st March 2024 and 31st March 2025 for the given scenario. Average mark was scored by many candidates as they have not concentrated on SLFRS 15, Revenue Recognition standard.

Question No. 07

It was required to prepare the Statement of Cash Flow for the year ended 31st March 2024 using indirect method.

Most of the candidates performed well and scored a higher mark while some candidates obtained total marks allocated to the question. However, below shortcomings were observed from the answers:

- Some candidates failed to classify as operating, investing and financing activities. Rather, just stated as common activities.
- Although some have classify the activities separately, they failed to pin point to the correct activities. For eg: long term loan obtained was identified as investing activities which should be classified under financing activities.
- Certain candidates showed cash outflow without bracket and cash inflow with brackets.
- Depreciation and loss on disposal have not properly calculated.
- Profit before Tax calculation was incorrect.

SECTION C

Question No. 08

This question was related to the preparation of Financial Statements for publication. The adjustments include provision of bad debts and over/under provision adjustments, knowledge on lease liability, knowledge on revaluation surplus etc.

Poor answers were noted in the lease liability calculation and the classification of lease liability. There were common issue with lease purchase being incorrectly shown in the Property, Plant and Equipment note as an opening balance, despite these transactions occurred during the year. Many candidates have not adjusted the receivables from sale of machinery. Many candidates did not compute the depreciation for new construction completed on 1st January 2024. Also, they failed to add such capital work in progress to building account under PPE note. Profit on disposal was not correctly computed since disposal amount due (creditor) was not considered for the computation. Some candidates have taken 28 Million as the addition to the land value as revaluation without understanding of the given information. Due to lack of time management, candidates have left the question half attempted.

Question No. 09

This question is basically to calculate six ratios and to prepare a summary report to the management of **Sun PLC** comparing the two years period with possible reasons for the variances. Majority of the students have attempted the **part (a)** of the question whereas many have failed to attempt the **part (b)** of the question.

(a) Many candidates have written the formulas for the requested ratios and failed to compute the ratios. In order to compute earnings per share (EPS), many have computed Market Prices Per Share (MPS) and Price Earning (PE) ratio. This shows a lack of knowledge and candidates considered the information given on the market price per share. Some computed net assets ratio instead of quick assets ratio due to lack of understanding on the ratio. Majority of the candidates computed Gross Profit ratio and Net Profit ratio correctly. It is expected candidates to use average trade receivables and average inventories for the computation of Debtor's Collection Period and Stock Residence Period. However, many candidates used closing balances rather than using average balances. Some candidates have not written the formula to calculate the ratios. Rather, got the final answer where they ended up with a wrong answer.

Many candidates could not remember the formula for Debtor's Collection Period and Stock Residence Period and due to that they have not accurately performed the calculation.

(b) Those who have attempted this part wrote only that there is an increase/decrease comparing to two years where they failed to explain the possible reasons for the variances between two years. Some candidates provided overall comments as the answer comparing two periods rather comparing individual ratios for two periods. Many candidates failed to analyze the ratio as favorable or unfavorable with possible reasons for such ratios. Though, some have done the calculations properly, when comparing 2023 and 2024, they have taken 2023 as the current year and compared and provided reasons in a different way. Most of the candidates just wrote as increase or decrease by looking at the numbers only without analyzing whether it is favorable or unfavorable impact to the entity. Though some have identified whether the ratio is favorable or unfavorable, the reasons for such have not mentioned.

Question No. 10

This question was tested on participation of Consolidated Income Statements. Majority of the candidates attempted the question and some have properly understand and given the answer correctly. However, few students not even understand the question. Only few candidates stated the impairment of goodwill of Rs. 2 million correctly. Some candidates have not properly read the question and they have not done specific adjustments related to consolidation. For example management fee given in the question is for monthly which should be converted in to yearly fee. Instead of that, candidates adjusted monthly amount as yearly management fee. Majority of the candidates correctly done line by line additions.

Some of the common mistakes were noted are mentioned below:

- Inter-company sales (inventory) has not been calculated properly i.e. Rs. 144 million and not adjusted/ remove from both sales and cost of sales. Lack of knowledge in calculating unrealizable profit of 7.5 million and related adjustment to the cost of sales.
- By an oversight, some candidates taken the annual management fee of Rs.300,000/- (monthly figure). Few candidates correctly removed the management fee of Rs. 3.6 million from both management fee income and administrative income. Some candidates removed from management fee only.

- Average number of the candidates failed to calculate and/or adjust the depreciation calculation of machinery and remove it from Admin Expenses.
- Inter-company interest of Rs. 1.2 million of the short term loan was not properly adjusted from interest income and the finance expenses. However, majority of the candidates were able to remove Rs. 1.2 million from finance expenses and arrived an accurate finance expenses figure.
- Most of the candidates have not calculated the impairment of goodwill of Rs. 2 million.
- Some candidates added 80% of **Seetha Ltd.** figures to **Rama Ltd.** when preparing the Consolidated Comprehensive Income Statement.

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General points to be considered in developing the level of Understanding of candidates:

- (1) Many candidates were not mentioned the question numbers on the answer script.
- (2) Answers not commenced in a new page as instructed to the candidates.
- (3) Candidates attempted to answer the questions in an orderly manner starting with question 01 and ended up with question 10. Thus, many candidates do not have to do question no. 10.
- (4) It is advisable to candidates to go through all the questions during reading time and prioritize the questions based on convenience of candidates.
- (5) Candidates should read the study text of AAT and practice the examples given in the study text.
- (6) Candidates should practice past papers as much as possible within the allocated time and thus, should practice for time management.
- (7) It is advised to read the questions carefully and understand the requirements of the question with the action verbs provided in the question.

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