

EXAMINER'S REPORT**LEVEL III EXAMINATION - JANUARY 2021****(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**

This question was required the candidates to explain 3 reasons why ethics are important in accounting.

Most students had produced acceptable answers for this question and had scored considerable marks. However few students had just mentioned the point without giving a proper explanation.

Overall performance for this question was at a satisfactory level.

Question No. 02

This question was required to explain two fundamental qualitative characteristics as per conceptual Framework of Financial Reporting.

Most of the Students had answered the question and scored notable marks. However some candidates did not know about the two fundamental qualitative characteristics as relevance and faithful representation.

Overall performance for this question was at a satisfactory level.

Question No. 03

This question was required to calculate the borrowing cost to be capitalized using the given information.

Majority of the candidates had showed poor performance in answering this question. Further, most of the candidates have failed to calculate WACC properly. It is suggested that candidates must have sound knowledge on LKAS 23 – Borrowing Cost. Some candidates have considered interest for 12 months instead of 10 months when capitalizing borrowing cost. It shows that they have not read the question properly.

Performance of this question was not at satisfactory level.

Question No. 04

This question was tested the candidates' knowledge on LKAS 38 – Intangible Assets.

Part (a) (1) of the question required to explain whether the costs that have incurred on staff training could be recognized as intangible asset as per LKAS 38.

Most students had failed to identify the criteria for to recognizing an intangible asset and hence they have treated staff training as an intangible asset.

Part (a) (2) of the question required to explain whether the research cost incurred prior to the product development could be recognized as an intangible assets as per LKAS 38.

Majority had correctly identified the facts and treated as an expense while few students had failed to identify the correct treatment.

Part (b) of the question required to state the two criteria to be met in recognizing a development cost as an intangible asset.

It was observed that, most of the candidates have shown poor performance and their technical knowledge on LKAS 38 needs to be improved.

Performance of this question was not at satisfactory level.

SECTION B

Question No. 05

This question was tested the candidates' knowledge on LKAS 37 – Provisions, Contingent Liabilities and Contingent Assets.

Part (a) required explaining how the given scenarios could be recognized in the financial statements:

- (1) A customer has filed a case for compensation of Rs. 10 million on poor quality of the product.

Majority of the candidates had proposed to make a provision of Rs. 10 million as the company lawyers have stated that there is a high probability to pay this amount. However, a few candidates had correctly mentioned that, this as a contingent liability and hence a disclosure should be made in the financial statements. Since reliable estimate cannot be made

- (2) Company sells its products with a warranty of 6 months for any manufacturing defects.

Most of the candidates correctly mentioned that a provision should be made in the financial statements. However majority had failed to calculate the correct amount to be provided. Further, candidates must improve their knowledge on LKAS 37 – Provisions, Contingent Liabilities and Contingent Assets.

Part (b) required to list 3 financial assets and 2 financial liabilities.

Majority of the candidates had answered correctly for this part of the question.

Overall performance for this question was at a satisfactory level.

Question No. 06

This question was tested the candidates knowledge on LKAS 16 – Property Plant and Equipment.

Part (a) of the question required to calculate the cost of a machine using given information.

Majority of the candidates had calculated the machine cost correctly. However, few students have made the following mistakes:

- Test run cost of Rs.55,000/- was not considered as a part of the cost of machine.
- Insurance premium of Rs.50,000/- was considered as a part of the cost of machine.

Part (b) of the question required to list down 4 duties of the Securities Exchange Commission.

It is suggested that candidates should have knowledge on duties and responsibilities of main regulatory bodies.

Overall performance for this question was at satisfactory level.

Question No. 07

This question tested the candidates' knowledge on preparing cash flow using indirect method.

Most of the candidates have answered this question well and managed to earned considerable marks.

However, few candidates have made the following mistakes:

- Incorrect profit before tax calculation. Some candidates have not added back dividend when calculating profit before tax.
- Incorrect disposal profit calculation.
- Incorrect identification of cash inflows and out flow.
- Incorrect identification of operational, Investment and finance activities.

Overall performance for this question was at a satisfactory level.

SECTION C

Question No. 08

Part (a) of the question required to calculate Gross profit ratio, Net profit ratio, Quick asset ratio, Return on capital employed (ROCE), Gearing ratio and Earnings per share using the given information while **part (b)** required to analyze the performance of the company using the above calculated ratios.

Majority had calculated the ratios correctly but failed to perform a proper analysis.

The following were the common mistakes identified:

- (1) GP ratio was calculated by dividing gross profit by cost of sales instead of the sales.
- (2) Net Profit ratio was calculated PBT instead of PAT.
- (3) Not deducted Inventories from the current assets, when calculating the Quick Assets Ratio.
- (4) ROCE was calculated by dividing PBT instead of PBIT by Equity and Long Term Loan.
- (5) Gearing ratio was calculated by dividing Long term loan by equity + long term loan instead of dividing long term loan by equity.
- (6) Some students had only mentioned the formula and not applied the figures.
- (7) Have not produced the valid/acceptable reasons for the ratio changes.
- (8) Considerable number of candidates have calculated the ration but they have not analyzed the performance.

It is suggested that students needs to do more practices on preparing performance analysis reports using ratios.

Performance of this question was not at satisfactory level.

Question No. 09

Part (a) of the question required to calculate Good will arising from consolidation.

Majority had correctly calculated the goodwill.

Part (b) of the question required to prepare the Consolidated Comprehensive Income Statement as at 31st December 2020.

Majority had scored considerable marks for this part. However, the following common mistakes have been identified.

- (1) Few candidates just mentioned income and expense figures of both companies separately in two columns without showing the column with the consolidated amounts, while few students just shown the consolidated figure column only without doing adjustments .
- (2) Unrealized profits on unsold goods were not calculated correctly.
- (3) Intercompany profit on sale of land of Rs 500,000 was added to other income instead of deducting.
- (4) Some candidates had showed the Goodwill amount in the consolidated comprehensive Income statement.
- (5) Some candidates deducted Rs.50,000/- for rent adjustment instead of Rs.600,000/-.

It was suggested that candidates should practice more on this kind of questions.

Performance of this question was at satisfactory level.

Question No. 10

This question was tested the preparation of Statement of Comprehensive Income, Statement of Financial Position, Statement of Changes in Equity and Property Plant and Equipment note using the given information .

Most students had scored considerable marks for this question.

Common Mistakes that were made by the candidates are as follows:

Statement of Comprehensive Income:

- (1) Most of the candidates, failed to adjust the cost of sales with the obsolete stock of Rs.425,000/-. Some candidates deducted the value of the lower of cost and NRV from the Cost of Sales whereas it should have been added to the cost of sales. There were candidates who expensed it to the P&L under other expenses. Some candidates did not show the workings for NRV calculation.
- (2) Some candidates, failed to consider the bad debt amounting to Rs.500,000/- when arriving at the closing bad debt provision.
- (3) Some have failed to show the revaluation gain of Rs. 2 million under other comprehensive income, Some showed this as an other income.
- (4) Failed to identify the tax expenses of Rs. 3.3 million even though this was clearly given in the question. Mixed up with the paid and payable amounts.
- (5) Failed to identify in audit fees Rs.400,000/- and insurance Rs.1500,000/- as Administration expenses.
- (6) Failed to bring in the calculated depreciation expenditure from the movement of Property Plant & Equipment schedule to the income statement as expenditure.
- (7) Failed to calculate correctly and reduce the over provision of doubtful debt (Rs.1,240 million) from the distribution expenditure.
- (8) Posting error of Rs.350,000/- was not corrected when calculating the depreciation of plant and machinery.
- (9) Impairment loss was not correctly calculated.

Statement of Financial Position:

- (1) Some candidates, failed to deduct the inventory written off amount of Rs.425,000/- from the inventory.
- (2) Failed to categorize the current and non-current portions of bank loan in the statement of financial position.
- (3) Failed to arrive at the correct income tax payable amount as they failed to account for the income tax expense and tax paid amounts correctly.

- (4) Failed to show the pre-paid portion of insurance expenditure of Rs. 4.5 million under the current assets of the statement of financial position.
- (5) Failed to show audit fee payable Rs.400,000/- under the current liabilities in the statement of financial position.

Statement of Changes in Equity:

- (1) Considerable number of candidates deducted the interim dividend paid (Rs. 6.5 million) from the share capital instead of deducting it from the Retained Earnings.
- (2) Further, some candidates failed to present the revaluation gain (Rs. 2 million) under revaluation gain instead showed it under the retained earnings.
- (3) Considerable number of candidates took the total comprehensive income or profit before tax of the year to the retained earnings instead of taking the profit after tax.

Overall performance for this question was at a satisfactory level.

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

- (1) Studying well the contents of the entire syllabus and develop a thorough understanding of the level of knowledge expected for each unit or area.
- (2) Candidates should read the questions carefully and provide answers to the question asked.
- (3) Should show all the workings for the figures arrived at.
- (4) Should state all the assumptions if there are any.
- (5) Should start each question on a fresh sheet of paper and question number should be clearly stated.
- (6) Hand writing should be legible.
- (7) Practising past questions many times will help sharpening knowledge, skills and gaining speed. This will also be advantageous as similar types of questions may be repeated in the future examinations.
- (8) Reference to Accounting Standards, Suggested Answers, Pilot Papers, Articles related to subject will definitely improve knowledge.
- (9) Time management is crucial at the examination. In answering questions, candidates should spend time based on the marks allocated to each question.
- (10) Should sit at the examination with due preparation and with firm determination of passing the examination.

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