JMC JAYASEKERA MANAGEMENT CENTRE
"Pioneers in Professional Education"

Chartered Accountancy – BL 01

Financial Accounting

Sandeepa Jayasekera

B.Sc. (Acct.) Hons. Gold Medal Winner, ACA, SAT, ACMA (UK), CGMA (UK), CA Prize Winner for AFR subject in Strategic Level II, CA First in Order of Merit Prize Winner in CAB II Level, CIMA Strategic Level Aggregate Prize Winner, Reading for MBA (PIM-SJP).

1

1

LKAS 01 – Presentation of Financial Statements

2

Purpose of Financial Statements
To provide financial information of an entity that is useful to a wide range of users in making economic decisions.

Components of Financial Statements

- **Statement of Financial Position** – Financial position as at the reporting date. This shows the Internal and external ways of getting finance and where those were invested
- **Statement of Profit or Loss and Other Comprehensive Income** – Financial performance for the reporting period. Income less expenses and other comprehensive income.
- **Statement of Changes in Equity** – Transactions occurred between the entity and its owners during the reporting period. *Entity Concept*
- **Statement of Cash Flows** – Ways in which cash and cash equivalents flowed in and flowed out of the entity, in the form of operational, investing and financing activities during the reporting period
- **Notes and other disclosures** – Additionally, important information that are not being provided through other financial statement components

Other Comprehensive Income

Other non-operational income and expenses that are not included in profit or loss. Other Comprehensive Income includes the following:

- Revaluation gains/losses arising through LKAS 16 and LKAS 38
- Actuarial gains/losses on Defined Benefit Plans arising through LKAS 19
- Gains/losses arising from translating financial statements of a foreign operation in accordance with LKAS 21
- Gains/losses from financial instruments measured at fair value through other comprehensive income (FVOCI) in accordance with SLFRS 09 Financial Instruments
- Gains/losses on hedging instruments

Important features in presenting financial statements

Fair Presentation

Financial Statements shall present fairly the financial position and financial performance of an entity.

Compliance with SLFRSs

Financial Statements shall be prepared and presented in compliance with SLFRSs.

A disclosure of such compliance shall be made in the financial statements.

Offsetting

An entity shall not offset assets and liabilities or income and expenses, unless permitted by a SLFRS.

Materiality and Aggregation

An entity shall present **separately** each **material class of similar items.**
An entity shall present separately items of a dissimilar nature and immaterial items.

Important features in presenting financial statements

Frequency of reporting

An entity shall present financial statements at least annually. If an entity presents financial statements for a period longer or shorter than one year, an entity shall disclose:

- the reason
- the fact that amounts presented in the financial statements are not entirely comparable.

Consistency of presentation

An entity shall retain the presentation and classification of items in the financial statements from one period to the next. Unless;

- It is apparent that another presentation or classification would be more appropriate having regard to the criteria for the selection and application of accounting policies in LKAS 8
- A SLFRS requires a change in presentation

Comparative information

Except when SLFRSs permit, an entity shall present comparative information (preceding period) for all amounts reported in the financial statements.

Contents of Financial Statements

Following information should be presented in Financial Statements in general

- Name of the reporting entity
- Whether financial statements are of an individual entity or a group of entities
- Reporting period
- Presentation currency
- Level of precision used in presenting amounts in financial statements (Rs., Rs. ‘000, Rs. Mn.)

Information to be presented in the face of the Statement of Financial Position

- Property, Plant and Equipment
- Investment Property
- Intangible assets
- Financial assets
- Inventories
- Trade and other receivables
- Trade and other payables
- Provisions
- Financial liabilities
- Cash and Cash Equivalents
- Deferred Tax Assets and Deferred Tax Liabilities
- Issued capital and reserves

Current/ Non-current Distinction

The asset gets realized or liability gets settled within **Normal operating cycle** or **Trading Nature** or **within 12 months** after the reporting date

More than 12 months or Operating Cycle

Current

Non-current

Question 01

An entity shall apply LKAS 01 – Presentation of Financial Statements in preparing and presenting general purpose financial statements.

You are required to:

(a) State three (03) criteria to classify an asset as a current asset.

(03 marks)

Information to be presented in the face of the Statement of profit or loss and other comprehensive income

- Revenue
- Finance costs
- Share of profits or losses of associates and joint ventures accounted for using the equity method
- Tax expense
- Profit or loss for the period attributable to non-controlling interests and owners of the parent and comprehensive income for the period attributable to non-controlling interests and owners of the parent
- Other comprehensive income

Information to be presented in the face of the Statement of changes in equity

- Total profit or loss for the period
- Other comprehensive income for the period
- Dividends
- Share issues
- Effects of retrospective application or retrospective restatement recognised in accordance with LKAS 08

Information to be included under Notes and Disclosures

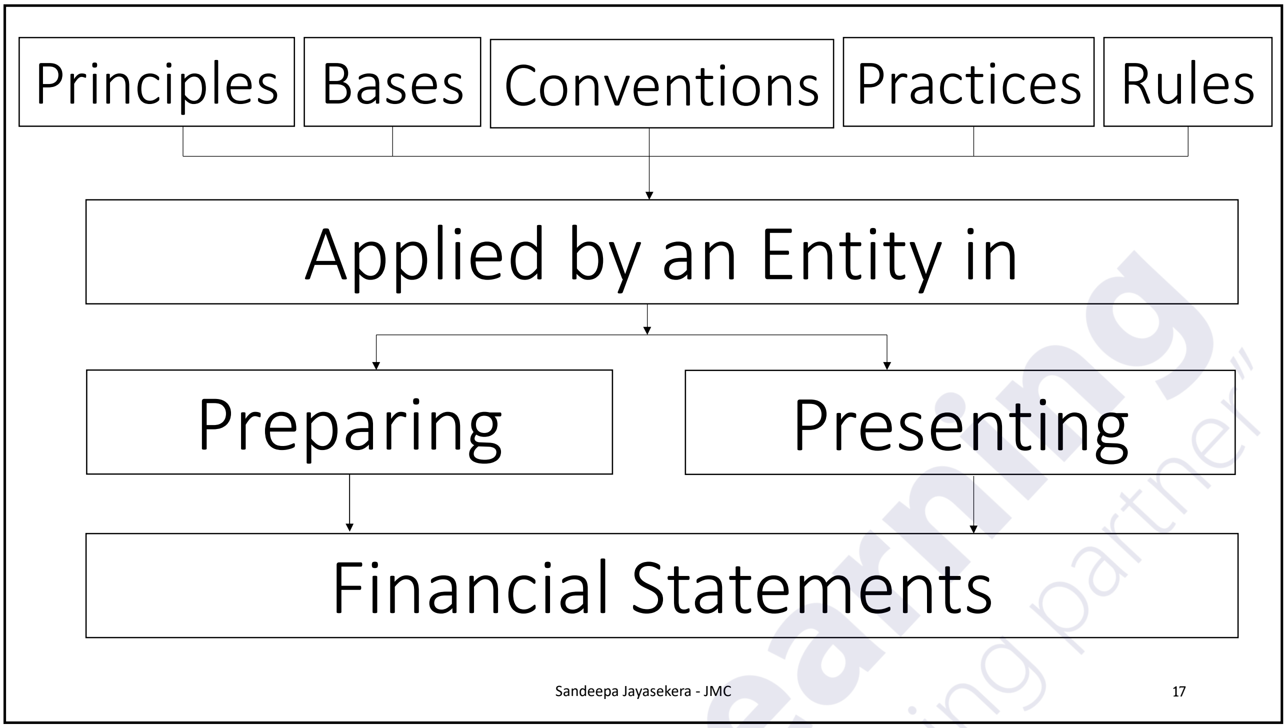
- A note stating that financial statements are prepared in compliance with SLFRSs
- Accounting policies
- Additional information in relation to information presented in other components of financial statements
- Contingent liabilities
- Events after the reporting period
- Non-financial disclosures
- Measurement basis used in preparing the financial statements

LKAS 08 - Accounting Policies, Changes in Accounting Estimates and Errors

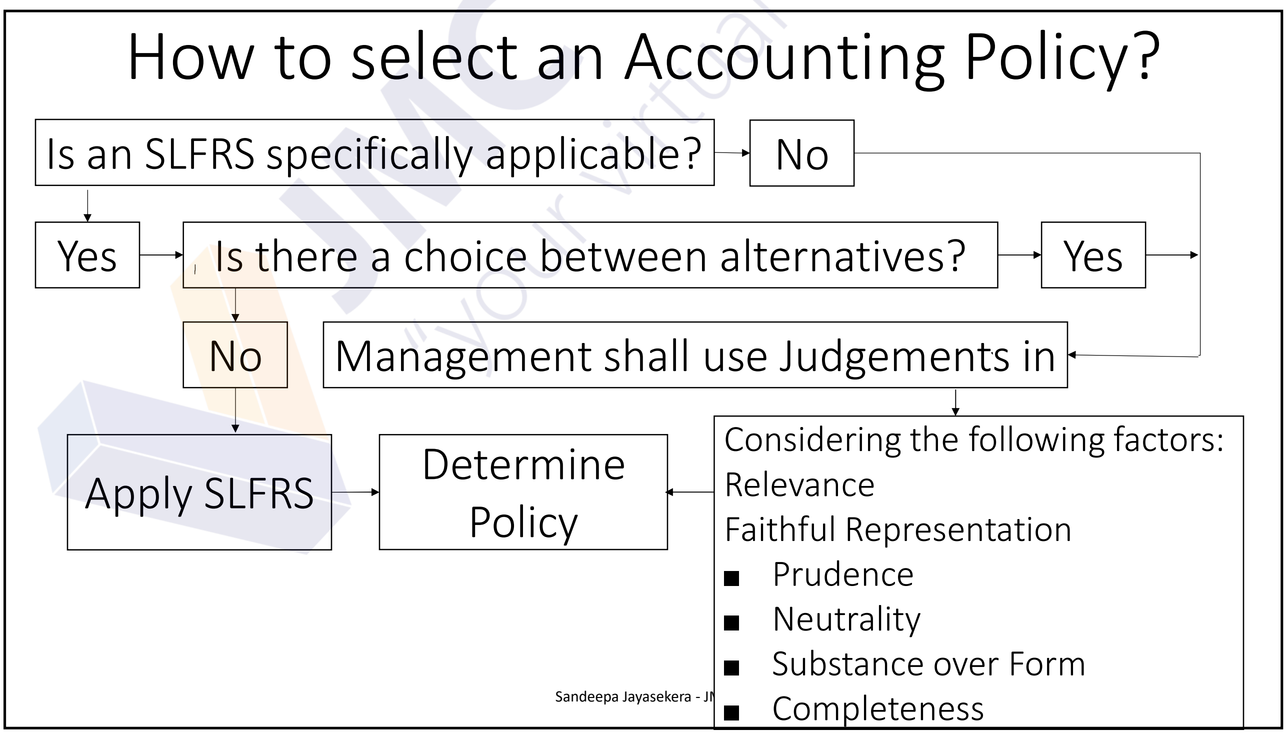
Examples for Accounting Policies

- Subsequent measurement of property, plant and equipment
- Inventory formulas (FIFO, WAC)
- Capitalisation of borrowing cost on qualifying assets
- Subsequent measurement of investment property
- Subsequent measurement of intangible assets
- Charging of research expenses to Statement of Profit or Loss

What is an Accounting Policy?


Principles
Bases
Conventions
Practices
Rules
Applied by an Entity in
Preparing
Presenting
Financial Statements
Sandeepa Jayasekera - JMC
17

17


How to select an Accounting Policy?
Is an SLFRS specifically applicable?
No
Yes
Is there a choice between alternatives?
Yes
No
Management shall use Judgements in
Apply SLFRS
Determine Policy
Considering the following factors:
Relevance
Faithful Representation
■ Prudence
■ Neutrality
■ Substance over Form
■ Completeness
Sandeepa Jayasekera - JMC

18

Application of Accounting Policies

Shall apply consistently

Changing an Accounting Policy

Apply transitional provisions in SLFRS ← Required by a SLFRS

Retrospective Application ← Voluntarily

Apply change in accounting policy as if the new policy had been applied from the beginning

Only if, it can provide more relevant and reliable financial information

Examples for Accounting Estimates

- Useful life of PPE
- Inventory obsolescence
- Debtor impairment provisions
- Fair value of financial assets or financial liabilities
- Warranty obligations
- Depreciation method

What is an Accounting Estimate?

Sandeepa Jayasekera - JMC 21

21

Accounting Estimate is

Management Judgements used

In measuring value of Assets and Liabilities using Latest available

Information

Conditions

Sandeepa Jayasekera - JMC 22

22

Change in Accounting Estimates

- **is** → Adjustments made to → Previously estimated →
  - Carrying value of an asset
  - Carrying value of a liability
  - Periodic consumption of asset

  → Based on new information or new developments
- **Accounting** → Prospective application → Recognise the effect of change in current year and future periods, as applicable
- **Examples** →
  - Based on the experience received in using an asset, changing the estimate of its useful life from 5 years to 4 years.
  - Based on the actual claim on warranty liabilities, changing the warranty provision by increasing from 5% of income to 7.5% of income.

Question 01

Abdul Ltd. purchased a machine worth Rs. 1,000,000/- on 01/01/2020, where its useful lifetime was estimated as 10 years.

Based on the experience gained from the use of machines, the useful lifetime was estimated again on 01/01/2021 and changed as 8 years.

Calculate the depreciation for the years 2020 and 2021, assuming financial year ends on 31/12.

Answer 01

Depreciation for Year 2020

Depreciation for Year 2021

Sandeepa Jayasekera - JMC 25

25

Question 02

Vijini Ltd. sells mobile phones. A one year warranty is given for each mobile phone sold.
Total sales for year 2020 was Rs. 2,500,000/- and 2% of sales was provided as warranties.
Actual warranty payment in relation to sales was Rs. 75,000/-.
Account for warranties, using ledger accounts.
(Financial year ends on 31/12.)

Sandeepa Jayasekera - JMC 26

26

Answer 02

Warranty expense for 2020

Warranty under-provision in 2020

Answer 02

Warranty expense

Warranty provision

Answer 02

Cash

Sandeepa Jayasekera - JMC 29

29

Examples for Accounting Errors

- Mathematical errors
- Oversight (an unintentional failure to notice or do something)
- Printing mistakes
- Mistakes in applying policies
- Misinterpretation of facts
- Frauds

Sandeepa Jayasekera - JMC 30

30

What are Accounting Errors?

Sandeepa Jayasekera - JMC 31

31

Accounting Errors are

Omissions | Misstatements

Arising from

Failure to use | Misuse of

Information that could reasonably
be expected to be considered

In preparation | In presentation

Financial Statements

Sandeepa Jayasekera - JMC 32

32

Adjustments to Accounting Errors

Immaterial Errors	Material Errors
Prospective Adjustment	Retrospective Restatement
Adjusting the current and future years, without adjusting prior periods.	Correction of financial information from the year in which the error occurred up to the current period
	Adjusting the comparative amounts in the current period financial statements and the Statement of changes in equity

Question 03

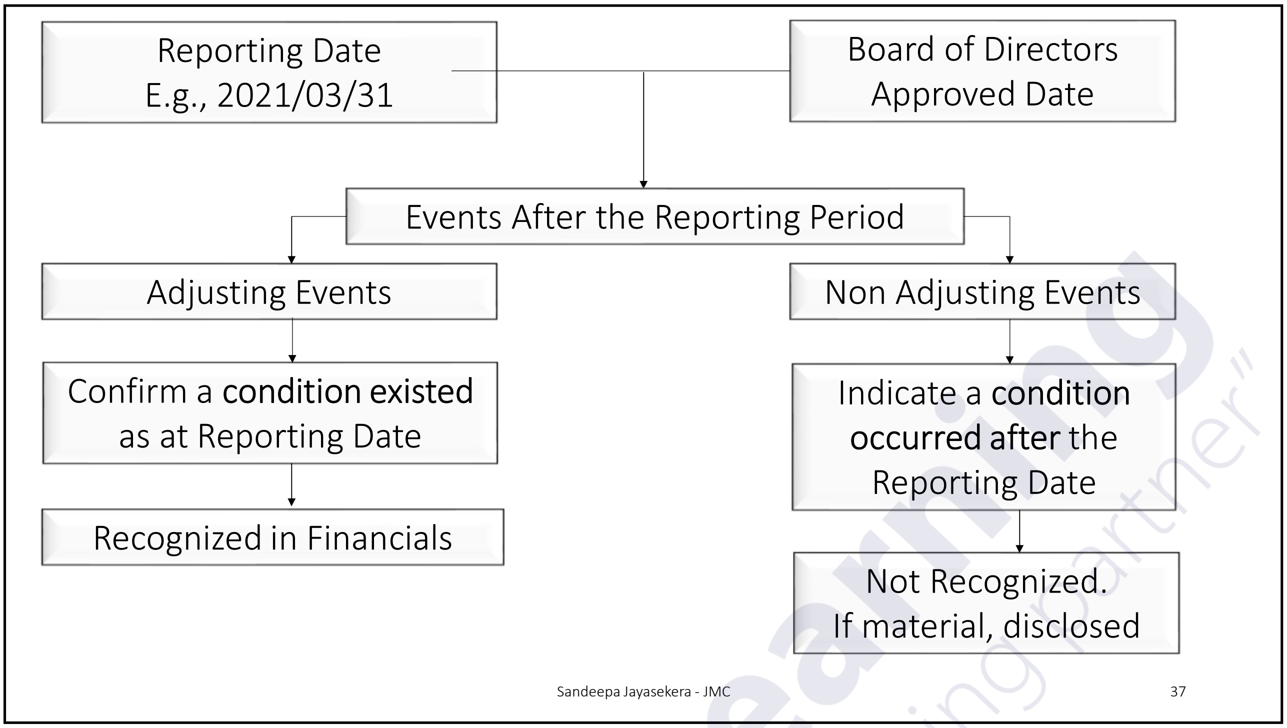
A stock of goods sold by Sajidha Ltd. was erroneously included in the closing stock as at 31/03/2020. The stock was valued at Rs. 10,000/-. Retained Earnings as at 01/04/2019 was Rs. 100,000/- and Stated Capital was Rs. 700,000/-.
Assume there is no impact on income tax, due to this error. Financial statements prior to adjusting the error is set out below.

Question 03

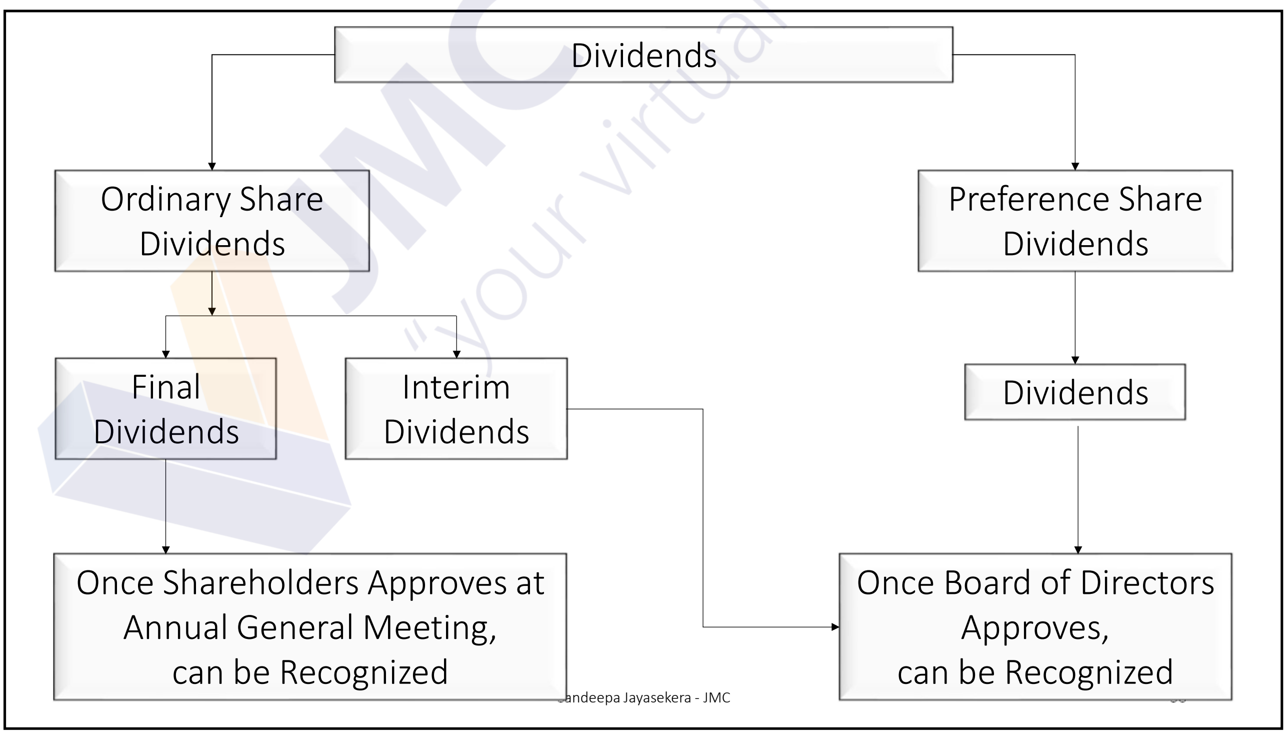
	2020/21	2019/20
Sales	200,000	150,000
Cost of Sales	(150,000)	(120,000)
Profit before tax	50,000	30,000
Tax	(10,000)	(5,000)
Profit after tax	40,000	25,000

Demonstrate how the error would be corrected in the Financial Statements for the year 2020/2021.

LKAS 10 – Events After the Reporting Period


Reporting Date
E.g., 2021/03/31
Board of Directors
Approved Date
Events After the Reporting Period
Adjusting Events
Non Adjusting Events
Confirm a **condition existed** as at Reporting Date
Indicate a **condition occurred after** the Reporting Date
Recognized in Financials
Not Recognized.
If material, disclosed
Sandeepa Jayasekera - JMC
37

37


Dividends
Ordinary Share Dividends
Preference Share Dividends
Final Dividends
Interim Dividends
Dividends
Once Shareholders Approves at Annual General Meeting, can be Recognized
Once Board of Directors Approves, can be Recognized
Sandeepa Jayasekera - JMC

38

Question 01

Vini Ltd's financial year ends on 31 March 2021. Board authorized the issue of financial on 15 May 2021.

Following events were occurred after reporting date

1. List of trade debtors as at reporting date who went bankrupt in subsequent period
   I. Xena traders' worth of Rs.10mn on 28 April 2021
   II. Polymax Ltd. worth of Rs.5mn on 16 May 2021

2. Company has done a credit sale worth of Rs.2Mn to Mano limited on 3 April 2021. However, Mano Limited was unable to settle the dues and declared the bankruptcy on 1 May 2021.

3. Company decided to close the rubber products sector on 25 April 2021. This was one of the key operating segments of the company.

4. A fraud done by cashier of Rs.1mn during March 2021 was discovered by the internal auditors on 3 May 2021

5. A fire occurred on 3 April 2021 in a warehouse located in Ekala. The damage was quantified as Rs.3mn.

6. Company obtained the technical advices from Boston consultants Group in USA and initiated a business process re-engineering project. This was commenced on 10 May 2021.

7. On 25 April 2021 judgment of a court case was given in the Colombo high courts. Thereby company has to pay Rs.10mn damage to a customer. This case was in trials as of reporting date.

8. Company has invested in John Keels shares in Colombo Stock Market (CSE). As of 31 March 2021, company had 20,000 shares. These shares were valued at Rs.215/= per share which was the market value as at the reporting date. However, the market price started falling down suddenly due to political instability of the country. On 3 April 2021, shares were traded at a price of Rs.155/=.
9. Board declared following dividends on 1 May 2021
   I. Preference share dividend of Rs.2/= per share (number of shares 1mn)
   II. Ordinary shares dividend of Rs.5/= per share (number of shares 10mn)
10. On 20 April 2021 company decided to merge with Galaxy PLC which was one of the key competitors in the same industry.

11. On 30 March 2021 company purchased a Rubber glove manufacturing plant. The final price of the plant was concluded as Rs.12mn on 5 May 2021.
12. On 5 May 2021 Auditors found that company's revenue recognition is erroneous for following transaction. Company has sold Rs.15mn worth of rubber carpets to lalan rubber on 30 March 2021 agreeing with a right to return basis. Return period elapsed on 30 April 2021 but company had recognized total revenue in 2020/21 financials.
13. A supplier has filed a case against the company on 17 June 2020 demanding a claim for not paying the dues. As of 31 March 2021, the case was on courts. On 01 August 2021 case was finalized not in favor of company. Thereby company is liable to pay a claim of Rs.1Mn to the supplier.

14. Company has carried out a revaluation of the lands as the lands are valued using revaluation model. Revaluation exercise was commenced on 1 March 2021. The revaluation report was received to the company on 5 April 2021. As per revaluation report a revaluation increase of Rs.10Mn was noted.
15. As a policy, generally company grants 5% of the operating profits as bonus. Based on company's profits for the year 2020/21, directors approved the 5% bonus on 1 May 2021.

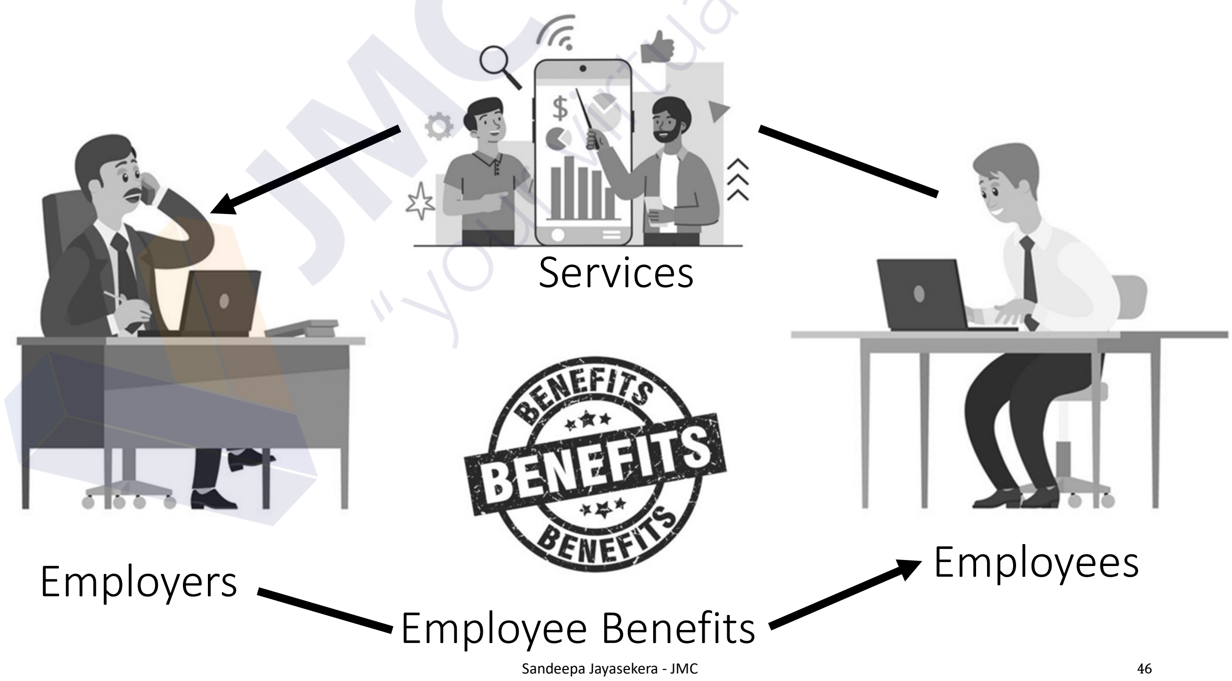
16. Following details are relevant to inventory
    I. Brand X 10,000 units were sold on 1 May 2021 at Rs.1,000 incurring Rs.100 as the selling cost. The cost of an inventory item was Rs.950/-
    II. Brand Y 20,000 units were sold on 16 May 2021 at Rs.800 incurring Rs.50 as the selling cost. The cost of an inventory item was Rs.900/-

You are required to state how you would treat each of the above events in Financial statements for the year ended 31 March 2021.

LKAS 19 – Employee Benefits

Sandeepa Jayasekera - JMC 45

45



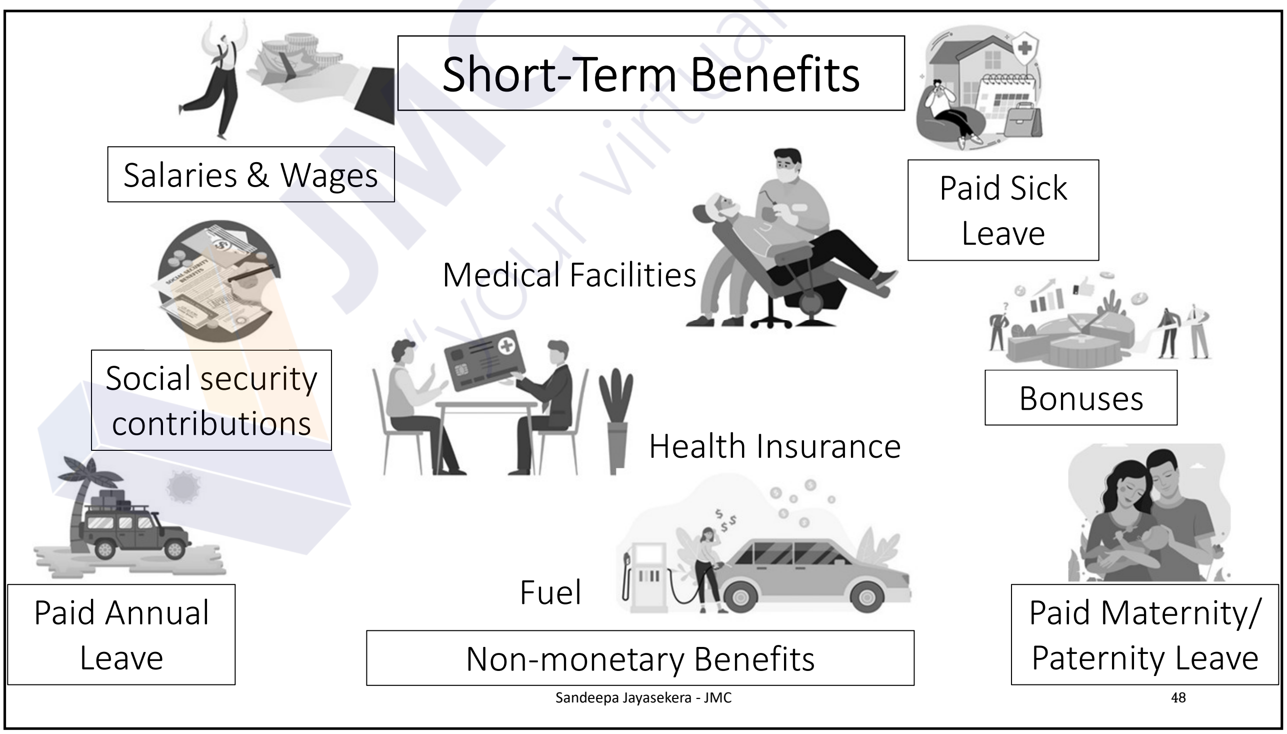
Sandeepa Jayasekera - JMC 46

46

Short-term Employee Benefits

Benefits expected to be settled → Within 12 Months → From the date of rendering the service

Recognised as an Expense



Question 01

Amana Ltd's Salaries related to the month of March 2021 was Rs. 6,750,000/-. This will be paid in the next month. Show the double entry of this transaction.

Sandeepa Jayasekera - JMC 49

49

Short-term Paid Non-Absenteesm

Non-accumulating Paid Non-Absenteeism	Accumulating Paid Non-Absenteeism
If current period's entitlement is not used, it cannot be carried forward	If current period's entitlement is not used, it can be carried forward for the next year
• Maternity/Paternity Leave • Sick Leave	• Paid Holiday Leave

Benefit related to Absence: If it's accumulating paid non-absenteeism, the value of the unused leaves as at the reporting date shall be recognized as an expense.

50

Sandeepa Jayasekera - JMC

50

Question 02

Hasitha PLC allows to carry forward unused holiday leaves to the next year. The company has a total of 150 employees. It is expected that 30 employees will carry forward 2 days from the unused holiday leaves of the current year to the next year. The daily pay of an employee is Rs. 1,500/-. Show the accounting entries.

Bonuses

Bonuses

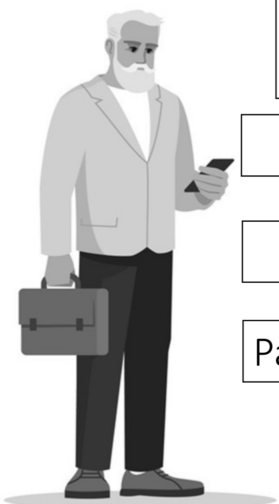
As a Policy	}	Sharing part of the Profit with Employees
As a Practice		

Recognised as an expense in the year
in which the profit is generated

Question 03

Amali PLC pays 1% of the annual profit generated as a Bonus.
Only employees with a service period of more than one year and who rendered their service till the end of the financial year will be entitled for this.
The company had 40 employees at the beginning of the financial year and only 35 employees were there by the end of financial year.
03 new employees joined the service during the year.
Annual Profit is Rs. 50 Mn.
How much is the bonus received by one employee?
Show the accounting entries.

Post-employment Benefits (Benefit Plans)



Defined Contribution Plans

Employees' Provident Fund
Employees' Trust Fund

- Employers → Contribute
- Employees → Contribute
- Contribute → To a Fund of another entity
- To a Fund of another entity → Invest
- Invest → Investment Income
- Invest → Sale of Investments
- Investment Income → Payment of Benefits
- Sale of Investments → Payment of Benefits
- Payment of Benefits → Employees

Defined Benefit Plans

- Plans other than the contribution plans
- Employee Gratuity

55

55

Other Long-term Employee Benefits

- Long-service Paid Leave
  Eg: Paid leave entitled to University Professors every 7 years
- Jubilee or long-service benefits
- Long-term disability benefits

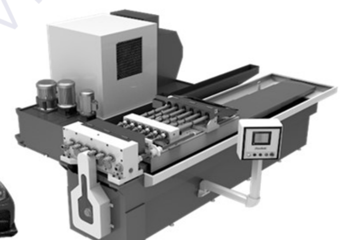
Termination Benefits

- Payments related to Early Retirement
- Payment made to Employee for the decision to leave on Redundancy as a result of excess employees

LKAS 16 – Property, Plant and Equipment

Examples for Property, Plant and Equipment

- Land
- Buildings
- Machinery
- Computers
- Equipment
- Motor vehicles



What are these Property, Plant and Equipment (PPE)?

Tangible assets held for

- Production
- Rental to others
- Administrative purposes

having a useful life of more than one year

At what point do we record PPE in the books of accounts? (Recognition)

Recognition Criteria

- Probable that future economic benefits will flow to the entity.
- Cost can be measured reliably.

Equipment used to protect the health, safety and environment

Sandeepa Jayasekera - JMC 63

63

Major Inspection Expenses

Sandeepa Jayasekera - JMC 64

64

At what value should PPE be initially measured? (Initial Measurement)

At Cost

Cost include

+ Purchase Price	XXX
(-) Trade Discounts	(X)
(-) Rebates (Note 01)	(X)
+ Non-refundable Taxes (Import duties, CESS tax, Custom duties, Port Authority Levy)	X
+ Directly attributable costs on bringing the asset to current working location and condition	X

Directly attributable costs incurred on bringing the asset to current working location and condition

- Transport expenses
- Handling expenses
- Clearing expenses
- Net cost of testing whether the asset is working properly (after deducting net proceeds from selling samples produced)
- Site preparation cost
- Installation costs
- Assembly costs
- Professional fees for those who engaged in installation
- Staff costs arising directly from the construction or acquisition of assets
- Borrowing cost of qualifying assets
- Present value of cost of dismantling and removing the asset (Note 02)

67

Note 01 – Rebates

Reimbursement of cost received from a customer, supplier, government or a third party.

68

Cost of PPE shall exclude:

- Staff training
- Administration overhead
- Sales overhead
- Cost of opening a new facility
- Cost of introducing a new product or service
- Relocation cost
- Recoverable taxes (VAT)
- Initial operating losses
- Subsequent expenditure

69

Note 02 – Present value of cost of dismantling and removing the asset

An entity may have a legal or constructive obligation to dismantle and remove an asset at the end of its useful life. The present value of the expected costs of dismantling, removing and rectification are capitalized as part of the cost of the asset and recognized as a provision.

Example:
The Government has demanded to dismantle chemical production facility after 5 years of operation. This is expected to cost Rs. 500,000/- at the end of 5th year. The present value of it is Rs. 300,000/-.

Production facility	Dr	300,000
Provision for removal	Cr	300,000

70

Question no. 01

Isumi (Pvt) Ltd. imported a machine from USA. Following information are relevant for the purchase.
Purchase price $ 1,000,000/- ($ 1 = Rs. 200)
Trade discount 10%
Port authority levy 2% (on the purchase price, net of trade discounts)
VAT rate 15% (on the purchase price, net of trade discounts)
Based on an agreement between Isumi Ltd. and the Government, the government granted a rebate of $ 100,000/-
Clearing charges Rs. 300,000/-
Handling charges Rs. 200,000/-

Question no. 01

Transport cost Rs. 180,000/-
Site preparation cost Rs. 900,000/-
Initial feasibility study cost of suppliers Rs. 50,000/-
Staff training cost Rs. 45,000/-
Cost of technical experts hired in fixing the machine Rs. 100,000/-
Initial trial run cost Rs. 400,000/-
Sales income from selling the output of initial trial run Rs. 50,000/-
Initial operational losses Rs. 100,000/-
Administration overheads Rs. 50,000/-
Cost of introducing the new product Rs. 200,000/-
Calculate the initial cost of the machine to be capitalized.

What is Residual Value?

Estimated amount obtained from disposal at the end of its useful life

Estimated disposal price − Estimated disposal cost

In many cases, residual value is immaterial. In such cases, the residual value is considered as 0 and ignored.

Residual Value → Carrying Amount of asset → Depreciation charge is zero

What is Depreciable Amount?

The amount remaining for depreciation.
Depreciable Amount of an asset at acquisition is;

Cost − Residual Value

Depreciable amount of an asset changes when the asset continues to be depreciated, when more expenses are capitalized and when the asset continues to be revalued.

What is Useful Life?

Period or Number of Products

asset is expected to be available for use/ expected to be obtained

Factors considered in determining useful life:

- Legal limits
- Expected usage
- Physical wear and tear
- Industry average
- Prior experience

Depreciation

Depreciation is
Systematic allocation of
depreciable amount
over the useful life

Depreciation begins when
An asset is available for use

Depreciation ceases when
- Asset is fully depreciated
- Asset is disposed
- Asset is classified as held for sale in accordance with SLFRS 05

Land
Not depreciated as land has an unlimited useful life

Depreciation Methods

Straight line

- Assumption → Similar returns received over the useful life of the asset
- Similar depreciation charge recognized over the useful life.
- $\text{Depreciation} = \dfrac{\text{Depreciable amount}}{\text{Remaining useful life}} \times \text{Time proportion}$

Reducing balance

- Assumption → Asset generates higher returns in initial years and gradually declines over the useful life
- Initially higher depreciation charge recognized, and it gradually reduces over the useful life.
- $\text{Depreciation} = \text{Opening NBV} \times \text{Depreciation \%} \times \text{Time proportion}$

Reducing Balance Method

Depreciation Rate = $\sqrt[1-n]{\frac{r}{c}}$

n = Useful life
r = Residual value
c = Cost

Production Unit Method

Depreciation charge recognized in line with production units.

$$\text{Depreciation} = \frac{\text{Depreciable Amount}}{\text{Total Expected Units}} \times \text{No. of produced units}$$

Question no. 02

Vihanga (Pvt) Ltd. purchased a machine at a cost of Rs. 10 Mn. Its residual value is Rs. 2 Mn and useful life is 2 years. If the machine is depreciated using the straight-line method,

1. Calculate the depreciation per annum.

2. Calculate the depreciation rate.

Question no. 02

3. Fill the following table:

Year	Cost	Depreciation	Accumulated Depreciation	Net Book Value
1				
2				

Question no. 03

Assume the same information as Question 02, except the depreciation method. Assume the machine is depreciated using the reducing balance method.

1. Calculate the depreciation rate.

Question no. 03

2. Fill in the following table:

Year	Cost	Depreciation	Accumulated Depreciation	Net Book Value
1				
2				

83

Question no. 04

Assume the same information as Question 02, except the depreciation method. Assume the machine is depreciated using production unit method. Total production capacity of the machine is 8,000 and production units produced in 1st year and 2nd year were 2,500 units and 5,500 units respectively.

1. Calculate the depreciation charge for Year 1 and Year 2.

Question no. 04

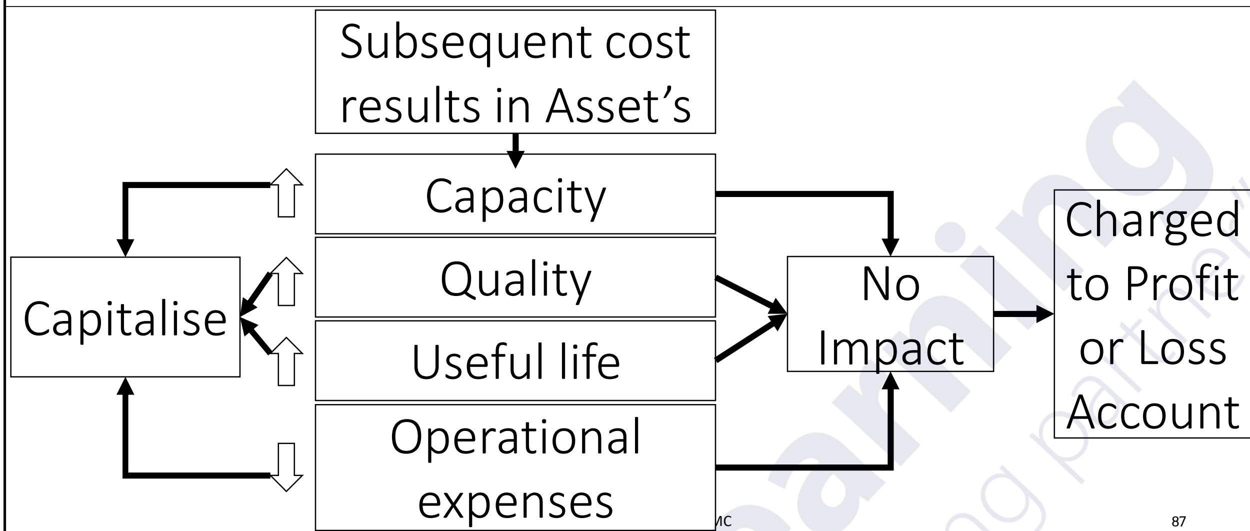
2. Fill in the following table:

Year	Cost	Depreciation	Accumulated Depreciation	Net Book Value
1				
2				

Subsequent costs incurred on Assets

- Maintenance
- Repairs
- Replacing of spare parts
- New additions
- Renovations

How do you account for subsequent costs incurred on assets?



Question no. 06

Jeniffer (Pvt) Ltd. acquired a machine at a cost of Rs. 20 Mn on 01/01/20X8. The residual value is zero and useful life is 5 years.

The machine maintenance expenses incurred for year 20X8 and 20X9 were Rs. 1 Mn and Rs. 1.5 Mn respectively.

On 01/01/20X9, Rs. 4 Mn was incurred on increasing the production capacity of the machine. There is no impact on the remaining useful life. Financial year ends on 31st December.

Question no. 05

1. Explain the accounting treatment for the maintenance expense.

2. Calculate the depreciation for year 20X8.

3. Can this Rs. 4 Mn expense incurred on 01/01/ 20X9 be capitalized? Explain.

4. Calculate the depreciation for year 20X9.

Subsequent Measurement

Once PPE is initially measured at cost, at the end of each reporting period, the PPE shall be assessed for subsequent measurement.

- Cost Model
- Revaluation Model

Cost Model

The asset is measured at initial cost and capitalized subsequent costs less any accumulated depreciation and accumulated impairment losses. The cost model applies a historical cost basis.

Cost (Initial + capitalized subsequent costs)	XX
(-) Accumulated Depreciation	(XX)
(-) Accumulated Impairment Losses (Refer LKAS 36)	(XX)
Net Book Value	XX

Question no. 06

Ashen (Pvt) Ltd. purchased a motor vehicle on 01/04/20X8 at a cost of Rs. 5 Mn. Its useful life is 5 years. On 31/03/20X9 this motor vehicle met with an accident and its resulting impairment loss was Rs. 1 Mn.

Financial year ends on 31st March.

1. Calculate the depreciation for the year 20X8/X9.
2. Show the double entries for depreciation.
3. Provide the double entries for impairment loss.
4. Calculate the depreciation for the year 20X9/X0.

Revaluation Model

This involves incorporating the current market value of assets into books of accounts. Firstly, a valuation will be carried out to obtain the market value of the asset. Then, the difference between the carrying amount of the asset and the market value will be recognized as the revaluation gain or loss.

Revalued Amount		XX
(-) Carrying amount of the asset		
Cost	XX	
(-) Accumulated Depreciation	(XX)	
(-) Accumulated Impairment losses	(XX)	(XX)
Revaluation Gain/ Loss		X/(X)

- JMC

93

93

Accounting for Revaluation

Firstly, bring in the Net Book Value into one account.

Accumulated Depreciation Dr

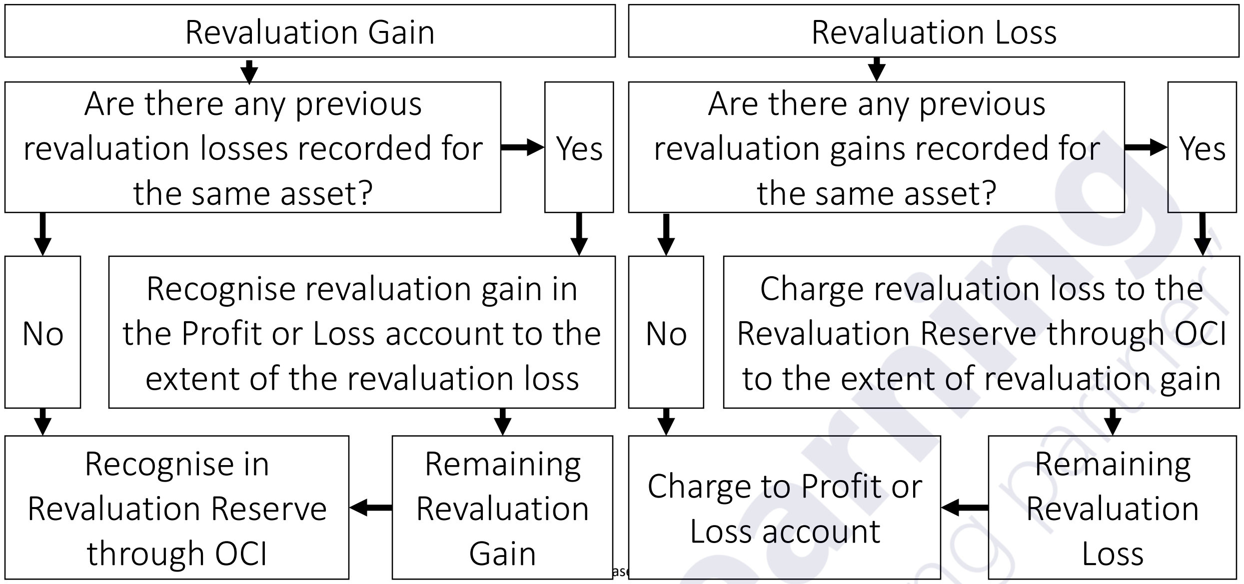
Asset Account Cr

Secondly, account for the revaluation gain or loss (Note 01)

Revaluation Gain		Revaluation Loss	
Asset Account	Dr	Revaluation losses	Dr
Revaluation Reserve	Cr	Asset Account	Cr

94

Adjusting Revaluation Gains/Losses



95

How frequently should Revaluation be carried out?

Depending on the frequency of changes in fair value of PPE, the management shall decide an appropriate revaluation cycle.

Subsequent Measurement using Revaluation Model

Revalued Amount	XX
(-) Subsequent Accumulated Depreciation	(XX)
(-) Subsequent Accumulated Impairment losses	(XX)
Net Book Value	XX

96

Can we revalue selected assets of a particular class of assets?

Question no. 07

Niranjala PLC purchased a machine on 01/01/20X1 for Rs. 50 Mn. It has a useful life of 5 years. Financial year ends on 31st December. Show the financial statement impact for each of the following 2 independent scenarios.

1. On 31/12/20X1 the machine was revalued at Rs. 45 Mn and on 31/12/20X2 it was revalued at Rs. 25 Mn.
2. On 31/12/20X1 the machine was revalued at Rs. 38 Mn and on 31/12/20X2 it was revalued at Rs. 35 Mn.

Derecognition of Assets

PPE shall be derecognized,

- On disposal of assets
- No future economic benefits are expected from the assets.

Calculation of Disposal gain or loss

Disposal Proceeds		xxx
(-) Carrying Amount of the asset		
Cost/ Revalued Amount	xx	
(-) Accumulated Depreciation	(xx)	
(-) Accumulated Impairment losses	(xx)	(x)
Disposal gain/(loss)		xx/(x)

Double entries relevant for Disposal

1. Cost of the disposed asset

   Disposal Gain or Loss Account Dr

   Asset Account Cr

2. Accumulated Depreciation and Accumulated Impairment Losses of the disposed asset

   Accumulated Depreciation Account Dr

   Accumulated Impairment Loss Account Dr

   Disposal Gain or Loss Account Cr

101

Double entries relevant for Disposal

3. Disposal Proceeds

   Cash Book Dr

   Disposal Gain or Loss Account Cr

4. Disposal Gain

   Disposal Gain or Loss Account Dr

   Profit or Loss Account (Other Income) Cr

5. Disposal Loss

   Profit or Loss Account (Other Expenses) Dr

   Disposal Gain or Loss Account Cr

102

Disposal of revalued assets with a revaluation gain

When a revalued asset is disposed of, the revaluation gain of such asset becomes realized. Therefore, the related revaluation reserve needs to be transferred to retained earnings. This adjustment is made in the Statement of Changes in Equity.

Revaluation Reserve	Dr	
Retained Earnings		Cr

103

Question 08

Abdul purchased a motor vehicle at a cost of Rs. 4 Mn on 01/01/20X1. Its residual value is Rs. 1 Mn and the useful life is 6 years. On 31/12/20X2 this was sold for Rs. 2 Mn. Financial year ends on 31st December.

1. Calculate the depreciable amount of the motor vehicle.
2. Calculate the depreciation per annum.
3. Calculate the depreciation rate.
4. What is the carrying amount of the motor vehicle on the date of disposal?
5. Calculate the disposal gain or loss of the motor vehicle.

104

Exchange of Assets

On some occasions, an entity's existing asset may be exchanged with another asset. This is also like a disposal of an asset. However, the entity would receive another asset as disposal proceeds, instead of cash.

Recognition of the cost of new asset

Asset Account Dr
Disposal Gain or Loss Account Cr

Cost of new asset shall be

- Fair value of the new asset received or
- Fair value of the asset given up or
- Carrying amount of the asset given up

105

Question no. 09

Imasha PLC purchased a motor vehicle worth Rs. 5 Mn on 01/04/20X1. Its useful life is 5 years. On 31/03/20X2 this motor vehicle was exchanged with another new motor vehicle. The fair value of this new motor vehicle was Rs. 5 Mn, while the fair value of the old motor vehicle was Rs. 4.5 Mn. Useful life of the new motor vehicle is 5 years. Financial year ends on 31st March.

1. Calculate the depreciation charge for year 20X1/X2.
2. Calculate the depreciation rate of the old motor vehicle.
3. Calculate the carrying amount of the old motor vehicle as at the date of exchange.
4. What is the cost of new asset?
5. Calculate the asset exchange gain/loss.

106

SLFRS 16 - Leases

This is Vihanga

Vihanga wants a car

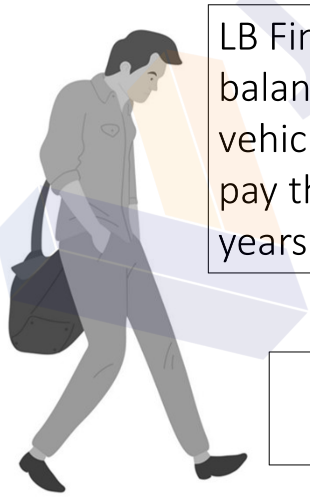
Car is worth of Rs. 5,000,000/-

But Vihanga has only Rs. 1,200,000/- in hand

Vihanga has 3 options

Using Savings	By obtaining a Loan	By Leasing
Buying the car using savings will take a long time	Bank loans take time, not as long as savings. But more hassles such as finding guarantors, providing documents etc.	Obtaining through a lease is faster and need lesser documents

Vihanga went to LB Finance and asked for a vehicle lease facility



LB Finance said they will pay the balance Rs. 3,800,000/- to the vehicle seller. But asked him to pay the Rs. 3,800,000/- in 5 years with a 10% interest

Accordingly, this is also a **Loan**.
Paid for the vehicle, without giving cash.

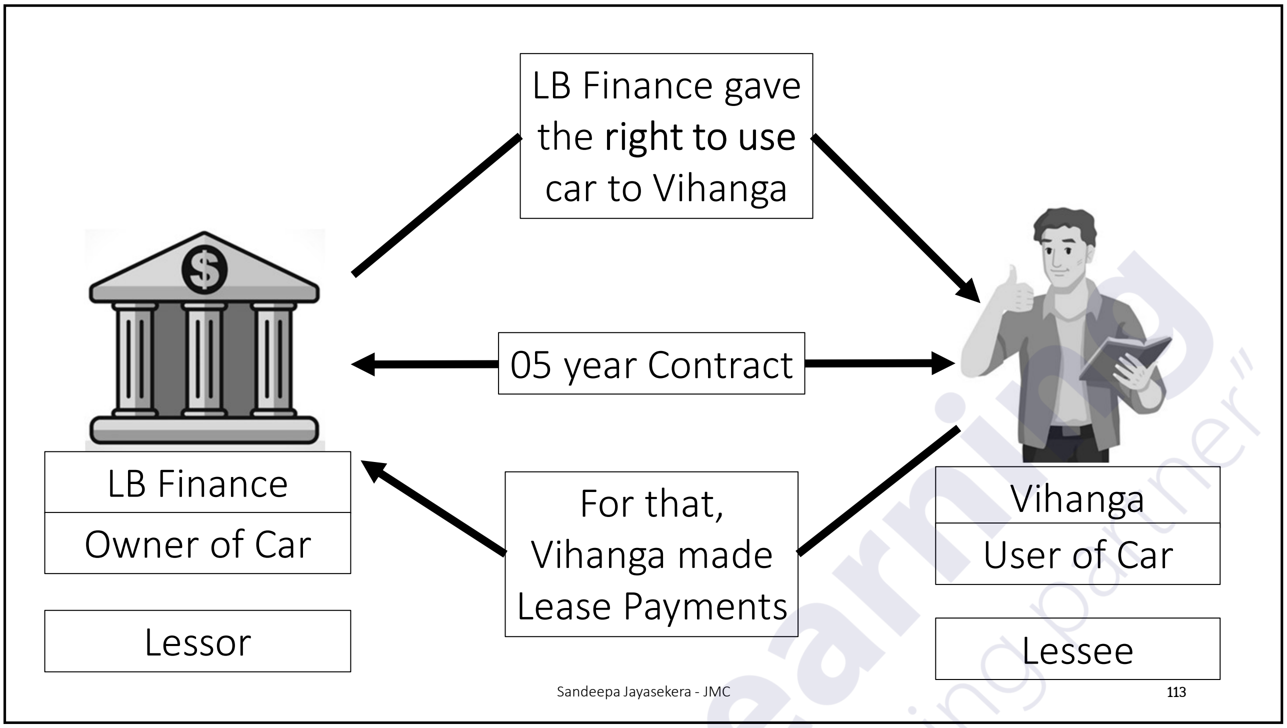
As hold over the loan, until the end of 5 years, the ownership of vehicle needs to be under the LB Finance. Vihanga can use the vehicle, even though the ownership is with LB Finance. But if Vihanga does not pay, LB Finance would come and takeover the vehicle, using the key they have.

When the total amount has been paid, Vihanga can get the ownership of the vehicle, under his name. Vihanga got the vehicle, agreeing to these terms.

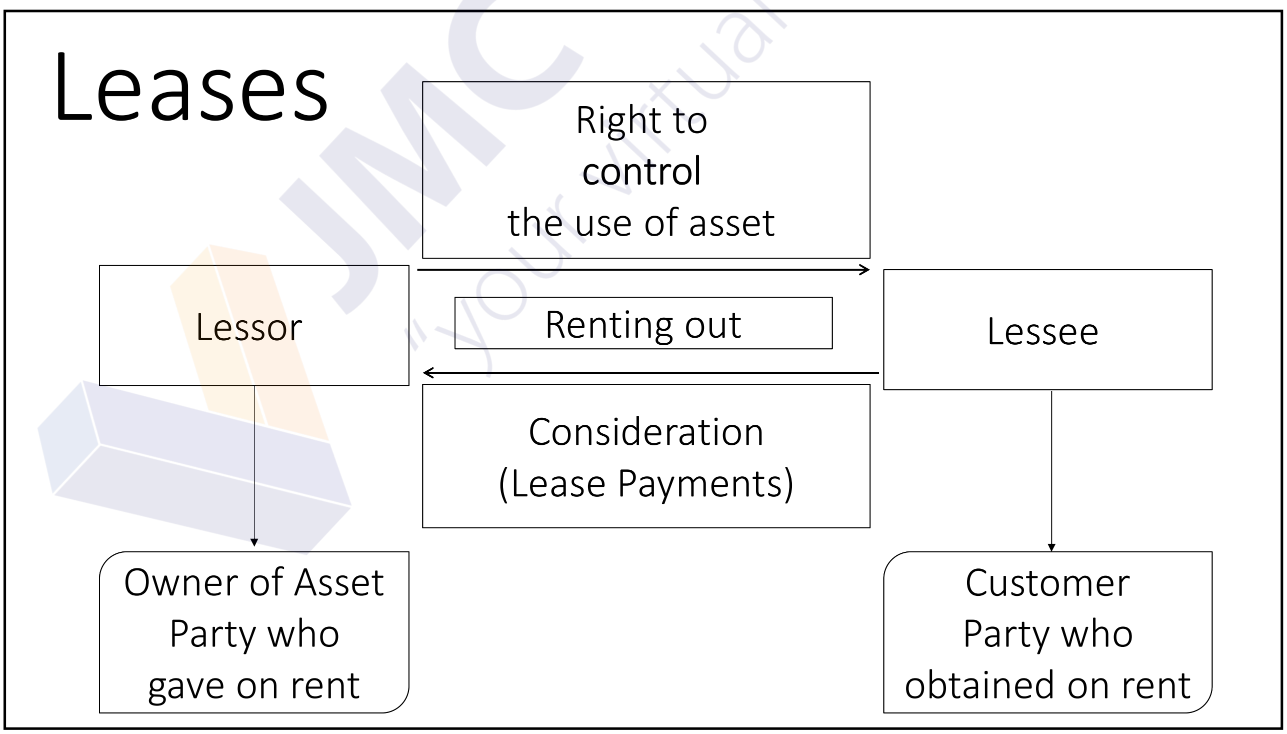
At the end of 05 years, Vihanga has paid Rs. 5,000,000/- for Loan

Excess Rs. 1,200,000/- paid was the Leasing Interest

According to the contract, once the total amount has been paid, Vihanga got the ownership of the car.


LB Finance gave the right to use car to Vihanga
05 year Contract
For that, Vihanga made Lease Payments
LB Finance
Owner of Car
Lessor
Vihanga
User of Car
Lessee
Sandeepa Jayasekera - JMC
113

113


Leases
Right to control the use of asset
Renting out
Consideration (Lease Payments)
Lessor
Lessee
Owner of Asset Party who gave on rent
Customer Party who obtained on rent

114

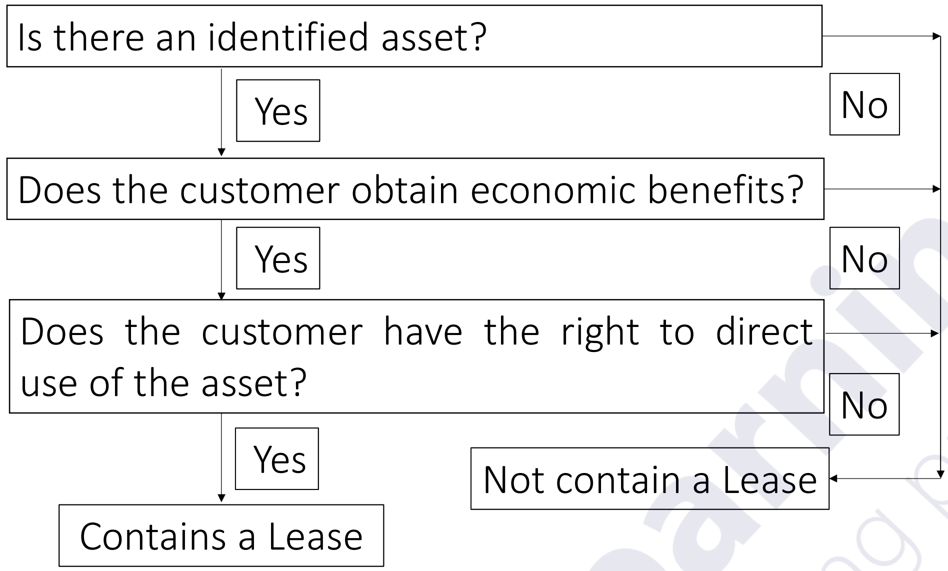
Accounting in Lessee’s Books

115

Accounting for Leases
Step 01
Determining whether a Contract contains a Lease

116

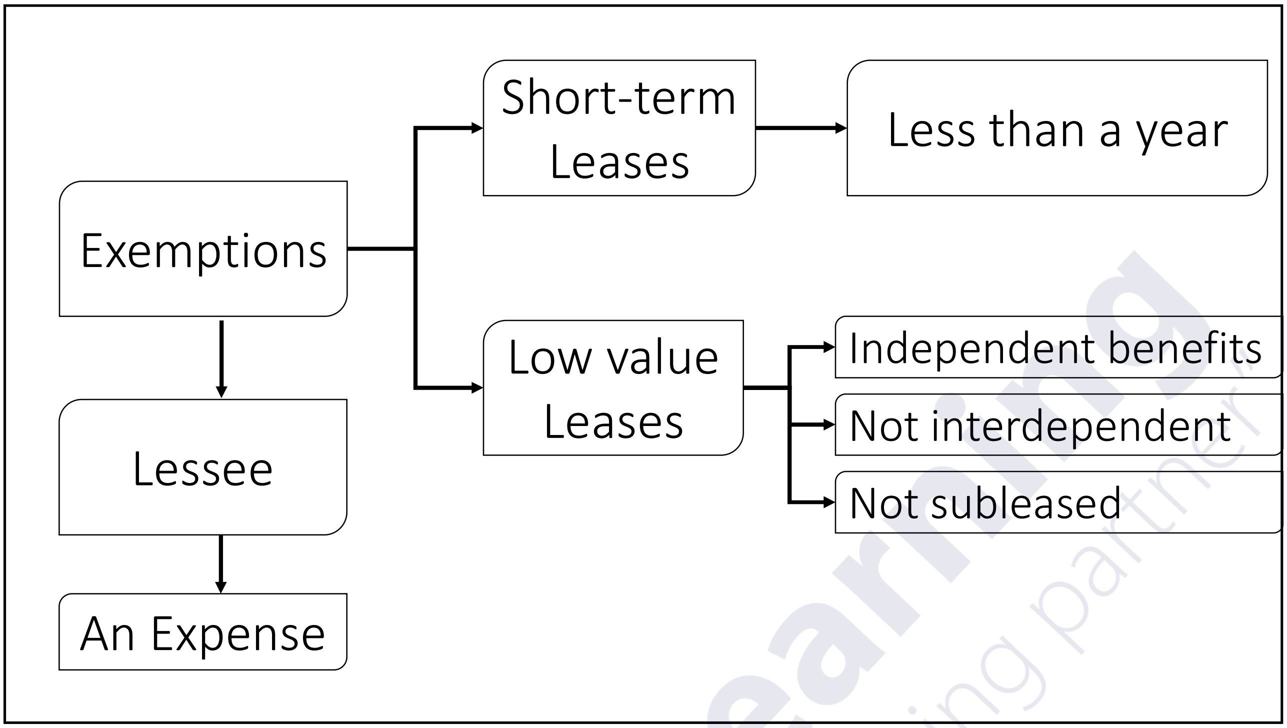
Determining whether a Contract contains a Lease



117

Accounting for Leases
Step 02
Exemptions -
Instances that can be excluded from Accounting for Leases

118



119

What is Subleasing?

120

120

Question 01

Namal PLC obtained a photocopy machine on 01/01/20X1 for a 08-month period based on a lease term.

Total lease expense of Rs. 80,000/- was fully paid on the date of entering the contract.

Show the accounting entries, assuming the accounting year ends on 31/03/20X1.

Lease Expense paid in Advance

Cash Book

Lease Rental Expense Account

Question 02

Dilki (Pvt) Ltd. has obtained the following assets under lease agreements. Identify the low value leases from the assets given below.

Asset	Is it a low value lease?
Motor Vehicle	
Office Building	
Office Computer	
Photocopy machine that has been subleased to another office	
Mobile Phone	

123

123

Accounting for Leases
Step 03
Lessee Accounting

124

Similar to acquiring an asset under a **Long-term Loan**

Lease Liability ← → Right-of-use Asset

125

Lease Liability is

Present Value of the

Amount obligated

To pay the Lease Creditor

126

Let's understand the Time Value of Money

Do you like to receive Rs. 100/- today or in another one year's time?

You like to receive it today!

Reasons
1. If you receive it today, you can invest it and earn an income.
2. Goods and services that can be purchased from Rs. 100/- today, cannot be purchased for the same price in another one year's time.
3. Money received today is certain. Receiving money in one year's time is uncertain.

127

Therefore, if a sum of money is received in the future, for the

Investment Income that will be lost - Opportunity Cost

Decline in Real Value - Inflation

Uncertainty

An Interest is expected as compensation

Present Cash flows + Interest = Future Cash flows

128

Discounting is defined as the process of **eliminating** the interest included in future cash flows.

Future Cash flow × Discounting Factor = Present Cash flow

$$\text{Discounting Factor} = \frac{1}{1 + r\,\hat{}\,n}$$

r = Interest Rate

n = Time

Question 03

Calculate the Present Values of the cash flows given below.

(Assume the interest rate as 10%)

Year	Future Cash Flow	Discounting Factor	Present Value	Interest
	A	B	C = A*B	D = A - C
0	100	1		
1	110	0.91		
2	121	0.83		
3	133	0.76		

130

Initial Measurement of the Lease Liability

- **Fixed Payments**
- **Variable Payments** – Lease rental that varies depending on a particular factor (production units, income)
- **Residual value guarantees** – The value guaranteed to a lessor (by a party unrelated to the lessor) out of the asset's realization value at the end of the lease term.
- **Exercise price of a purchase option if it is reasonably certain to exercise that option**
- **Penalties charged (if any) for early termination of the contract**

131

131

Subsequent Measurement of the Lease Liability

Opening Lease Liability + Lease Interest − Lease Payments = Closing Lease Liability

Lease Interest = Lease Interest Rate × Lease Liability balance as at the beginning of the period

132

132

Right-of-use Asset is

The Right

Received by the Lessee

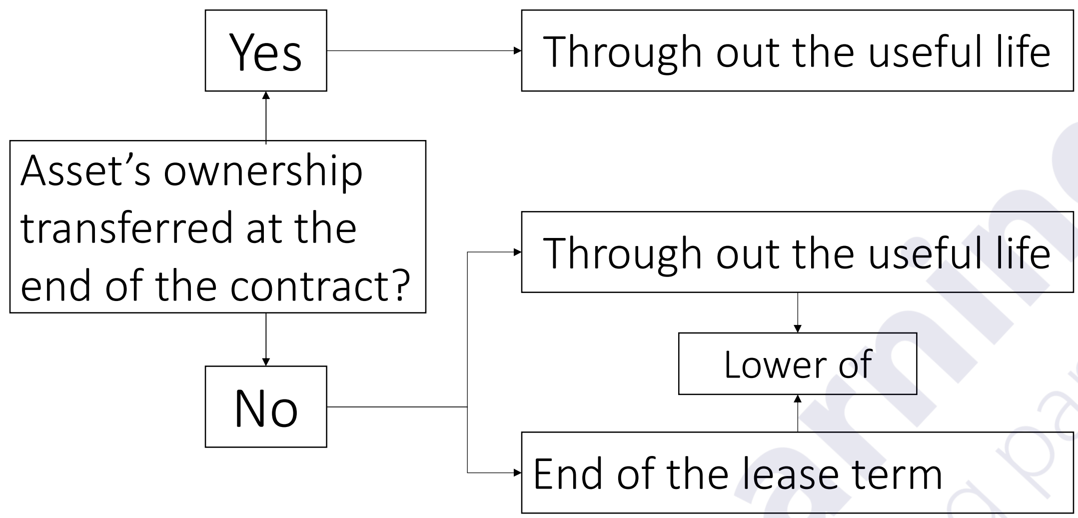
To direct the use of an underlying asset

Over the lease term

Initial Measurement of the Right-of-use Asset

- Initial Measurement of the Lease Liability
- Initial Down Payments (Lease prepayments)
- Initial Direct Costs
- Estimated costs to be incurred in dismantling and removing the asset at the end of the contract

Rule on Depreciating the Right-of-use Asset



135

135

Subsequent Measurement of the Right-of-use Asset

Cost Model		Revaluation Model	
Cost	XX	Revalued Amount	XX
(-) Accumulated Depreciation	(X)	(-) Subsequent Accumulated Depreciation	(X)
(-) Accumulated Impairment Losses	(X)	(-) Subsequent Accumulated Impairment Losses	(X)
Net Book Value	XX	Net Book Value	XX

136

Lessee Accounting

Description	Double Entry
Initial Payment	
Right-of-use the Asset account	Dr
Cash book	Cr
Amount recognized as the Lease Liability	
Right-of-use the Asset account	Dr
Lease Liability account	Cr

137

Lessee Accounting

Description	Double Entry
Payment made as Initial Direct Cost	
Right-of-use the Asset account	Dr
Cash book	Cr
Annual Interest on lease	
Interest Expense account	Dr
Lease Liability account	Cr

138

Lessee Accounting

Description	Double Entry
Payment of Lease Rental	
Lease Liability account	Dr
Cash book	Cr
Deprecation of Asset	
Depreciation account	Dr
Accumulated Depreciation account	Cr

139

Presentation in the Statement of Financial Position

Right-of-use Asset → Non-current Asset

Lease Liability

- Current Liability
  - Capital portion included in the next instalment
  - Next instalment − Interest included in the next instalment
- Non-current Liability
  - Capital portion to be paid after next year
  - Total Lease Liability − Current portion

140

140

Presentation in the Statement of Profit or Loss

Depreciation

Lease Interest

Question 04

Vihanga obtained a motor vehicle on 01.04.20X7, under lease agreement with LB Finance PLC. According to the agreement,

Lease period - 05 years Down payment - Rs. 1,200,000/-

The remaining amount is to be paid in 05 equal installments of Rs. 1,000,000/- annually. All installments are to be paid in arrears (At the end of the year). The useful life is also 05 years.
The present value of unpaid lease payments was Rs. 3,800,000/-.

Interest rate - 10%

The interest included in the 1st installment and 2nd installment is Rs. 380,000/- and Rs. 318,000/- respectively. Ownership transfers at the end of the lease term.

You are required to,

Show the accounting entries for the year ended 31.03.20X8 and the extracts of Statement of Financial Position and Statement of Profit or Loss for that date.

Question 05

Luckyland PLC obtained a machine from People's Leasing PLC under a lease agreement on 01.04.20X1. The present value of unpaid lease payments was Rs. 1,000,000/-. According to the lease agreement, Rs. 100,000/- has to be paid on 01.04.20X1. The balance has to be settled in 03 equal installments of Rs. 400,000/- annually. Installments have to be paid in arrears. Interest on lease is 10% per annum, calculated based on the opening loan value.

On 01.04.20X1 a cost of Rs. 100,000/- was incurred to transport and install the machine. The ownership of the asset does not transfer at the end of the lease term. The useful life of the machine is 4 years.

You are required to,

Show the accounting entries of Lucklyland PLC for the year 20X1/20X2 and extracts of Statement of Financial Position as at 31.03.20X2 and Statement of Profit or Loss.

143

Question 06

Kesara PLC leased a machine from Sampath Leasing Ltd. On 01.04.20X1 Rs. 200,000/- was made as a down payment. The balance was agreed to be settled in 03 equal installments of Rs. 400,000/-. Interest rate is 10%.

Discounting factors are as follows:

Year 01	0.91
Year 02	0.83
Year 03	0.76

The useful life of the machine is 02 years. The ownership of the machine does not transfer at the end of the contract. The company uses the revaluation model for the machine. The machine was revalued as at 31.03.20X2, where the revalued amount was Rs. 800,000/-.

You are required to demonstrate how the above transaction should be reflected in the Financial Statement as at 31/03/20X2 and Statement of Profit or Loss for the year 20X1/X2.

144

Disclosures

- Amortisation
- Interest
- Lease Payments
- Carrying amount of the Right-of-use the Asset
- Additions to the Right-of-use the Asset

145

145

LKAS 12 – Income Taxes

Sandeepa Jayasekera - JMC

146

146

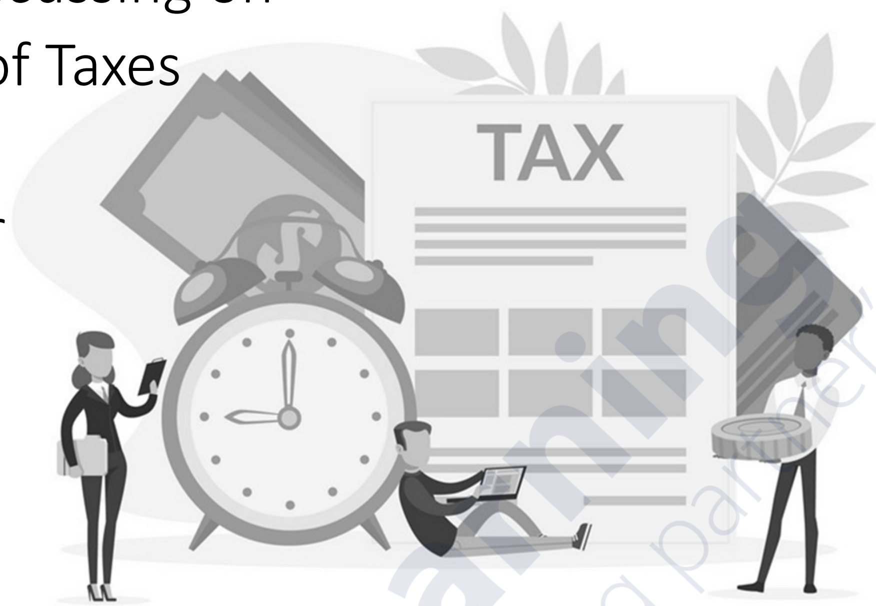
We are not discussing on

Computation of Taxes

But on

Accounting for

Taxes



Accounting for Taxes

- Past Taxes
- Current Taxes
- Future Taxes

Current Tax

Tax payable on the taxable profit for the current period

Accounting Profit ± Tax Adjustments = Taxable Profit × Tax % = Current Tax

Accounting Profit: Profit Before Tax included in Profit or Loss Account

Tax Adjustments:

+ Disallowable Expenses
- Allowable Expenses
+ Allowable Income
- Disallowable Income

Tax %: According to Income Tax laws

Question 01

The Profit or Loss account of Shalitha PLC for the year ended 31st March 20X1 is as follows:

Sales	1,000,000
Cost of Sales	(600,000)
Gross Profit	400,000
Other Expenses	(150,000)
Profit before Tax	250,000

Question 01

The accounting depreciation included under expenses is Rs. 50,000/-.
Capital Allowance applicable for those assets is Rs. 60,000/-.
Non-deductible entertainment expenses Rs. 30,000/-.
Gratuity expense is Rs. 40,000/-. It is not allowed to be deducted.
Actual Gratuity payment is Rs. 25,000/-. It is allowed to be deducted.

If the Tax rate is 28%,
1.1 Calculate the Taxable Profit.
1.2 Calculate the Tax Expense.
1.3 Show the double entry for taxes.

Past Tax

Under/Over provision of Income Tax for the previous year

Income Tax provision of the previous year

Actual payment made for the previous year

Under Provision

Over Provision

These are changes in accounting estimates. Therefore, adjusted to the current year.

Question 02

Sunanda PLC recognized a Tax Expense of Rs. 100,000/- for the year 20X0. But the actual tax payment was Rs. 120,000/-. Tax provision for the year 20X1 is Rs. 75,000/-.

2.1 What is the income tax under/over provision for the prior year?

2.2 Show the double entry for the income tax under/over provision for the prior year.

2.3 Show the double entry for the current year tax provision.

2.4 What is the Total Tax Expense for the year 20X1?

Question 03

Sameera PLC provided Rs. 30,000/- as income tax expense for the year 20X0. Actual tax payment for the year 20X0 was Rs. 20,000/- Income tax provision for the year 20X1 was Rs. 40,000/-.

3.1 Calculate the income tax under/over provision for the prior year.

3.2 Show the double entry for income tax under/over provision for the prior year.

3.3 Show the double entry for the current year tax.

3.4 What is the Total Tax Expense for the year?