THE INSTITUTE OF CHARTERED ACCOUNTANTS OF SRI LANKA

Business Level
Fundamentals of Financial Reporting
Chapter A - Introduction to Financial Accounting

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Sandeepa Jayasekera

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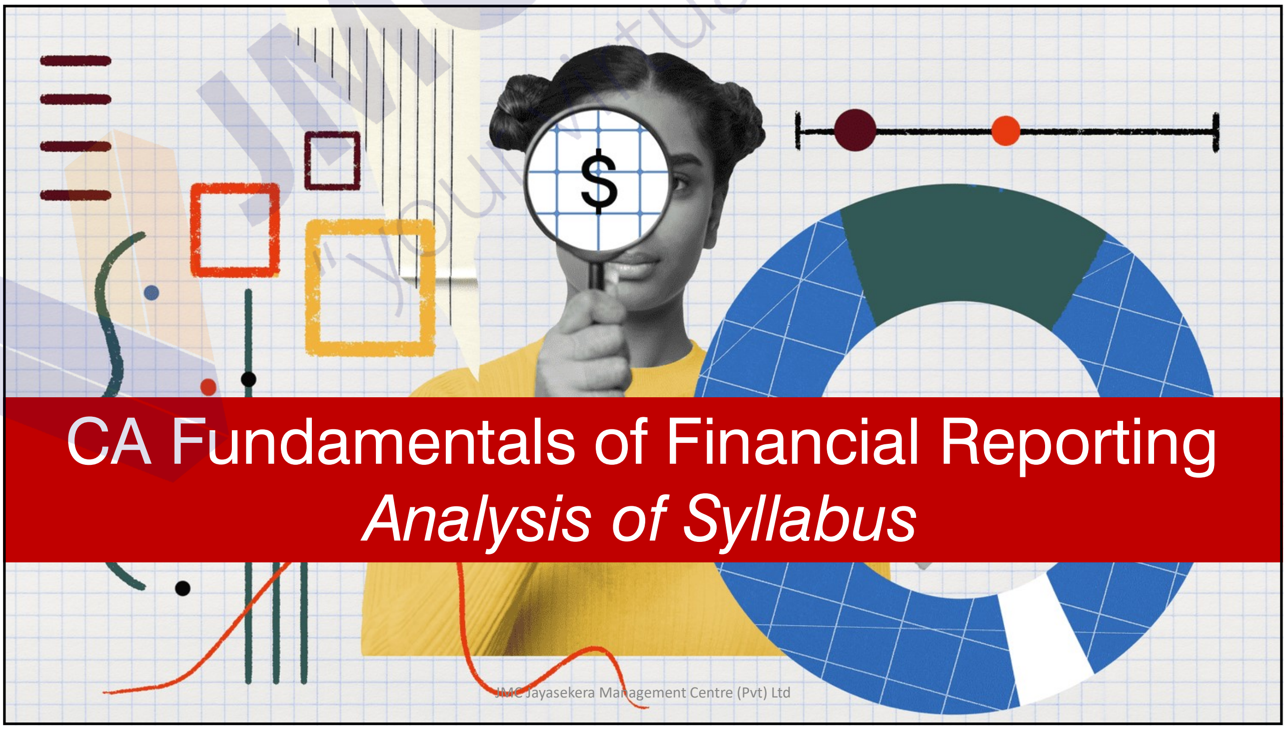
Sandeepa Jayasekera

- 11th in Sri Lanka in Advanced Level Commerce and 3rd in Colombo District
- First Class Degree in Accounting, Sri Jayewardenepura University and Gold Medal for Best Student
- Chartered Accountant (CA Sri Lanka)
- ACCA Accountant (UK)
- 1st in Sri Lanka for the second stage of Chartered Accountancy and the Advanced Financial Reporting Subject Prize in the final stage.
- Passed Finalist of Chartered Management Accountants in United Kingdom (CIMA-UK)
- CIMA (United Kingdom) 1st in Sri Lanka in Final Stage and 11th in the world

Sandeepa Jayasekera

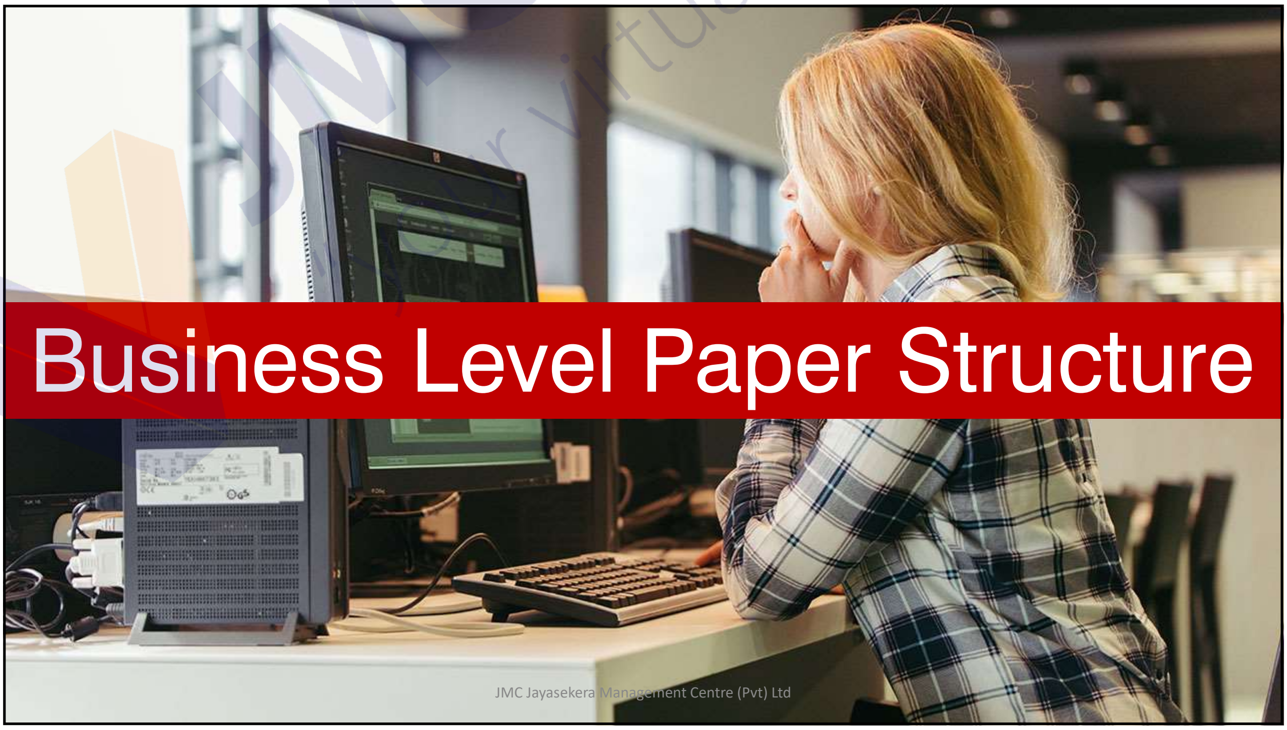
- Member of the Institute of Accounting Technicians of Sri Lanka (AAT Sri Lanka)
- Member of the Institute of Certified Management Accountants of Sri Lanka (CMA Sri Lanka)
- Postgraduate Institute of Management (PIM-USJP) Masters Degree in Management
- Chief Executive Officer
- Principal partner
- Lecturer at University of Colombo and University of Moratuwa
- Author who wrote ‘Awarjanayakata Awasarai’
- A motivational speaker and a trainer, conducted more than 250 sessions.



CA Fundamentals of Financial Reporting

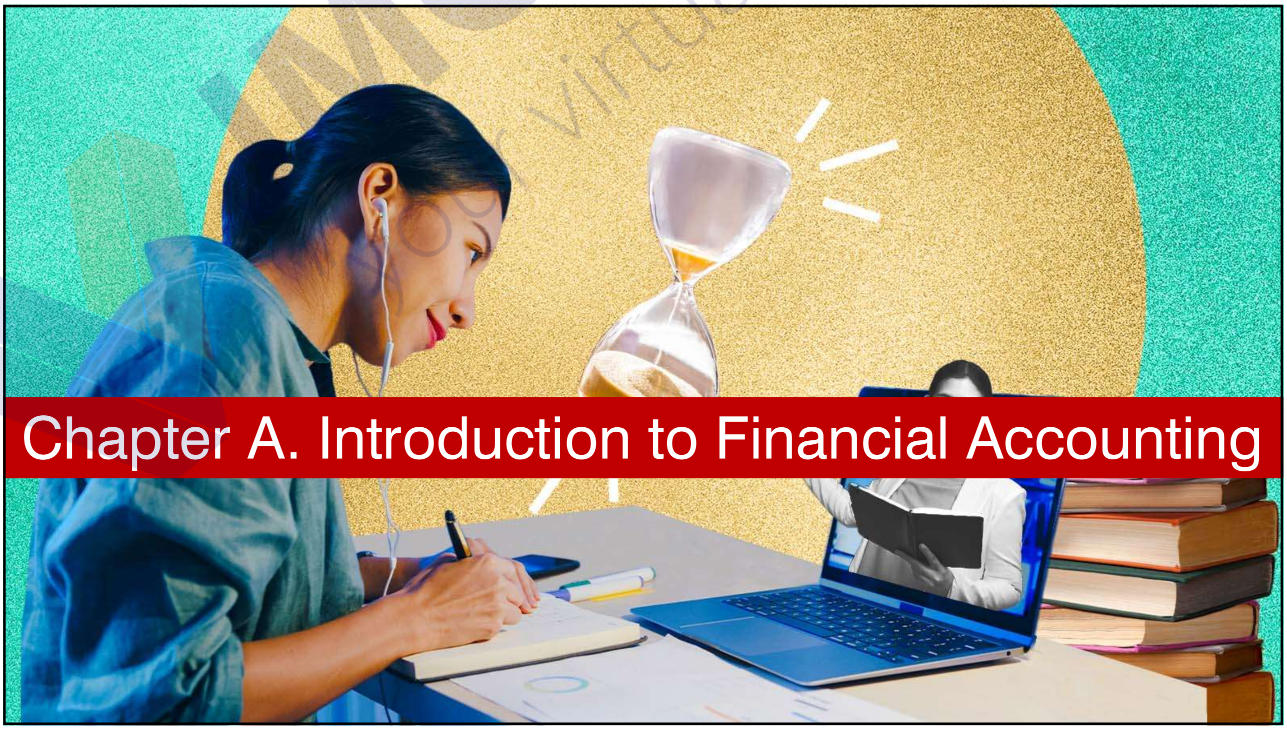
Analysis of Syllabus

Fundamentals of Financial Reporting Syllabus	Weight
A. Introduction to Financial Accounting	10%
B. Understanding the Accounting Process	25%
C. Preparation of Single Entity Financial Statements	15%
D. Application of Basic Accounting Standards for Financial Statements	25%
E. Analysis of Financial Statements	10%
F. Sustainability Reporting	5%
G. Digitalization of Accounting Process	10%



Fundamentals of Financial Reporting

Format	Mode	Duration	Pass Mark
50 Objective Test Questions (OTQs) of two marks each	Computer Based Examination	2 Hours	50/100



Chapter A. Introduction to Financial Accounting

1.1 Business Entity Types and Legal Structures

Business Entity Concept

Business ⟷ **Owner**

Two Separate Independent Parties

Business Entity Concept

Description	Examples
Business is a separate independent entity from the owners. This shows true picture of business performance, free from personal bias. It allows stakeholders to assess the health of the business itself.	• Equity is an internal obligation. • Drawings is a reduction of equity and not an expense. • Owner's personal transactions are not recorded in financials. • Financials named under the name of business. • Statement of changes in equity to show transactions with owners.


Business Organizations
Sole Proprietorships
Partnerships
Companies
JMC Jayasekera Management Centre (Pvt) Ltd


1.2 Differences among Business Organizations

Description	Sole Proprietorships	Partnerships	Companies
Ownership	Sole Proprietor	2 to 20 Partners Maximum number is not applicable for Professionals	Shareholders Pvt 1 – 50 Public 1 – No Limit
Management	Sole Proprietor	2 to 20 Partners	Board of Directors Pvt – Minimum 1 Public – Minimum 2
Profit and Loss	Sole Proprietor	Shared among Partners	Shared among Shareholders
Accounting and Auditing	Not Mandatory Simplified personal records are maintained	Not Mandatory Simplified personal records are maintained	Mandatory Companies act Section 151 and 154
Taxation	Assessed as Personal	Taxed as Partnership profit and allocated	Separate Corporate Tax

Description	Sole Proprietorships	Partnerships	Companies
Business Registration	Not Mandatory If the business is maintained under a different name than the owners, as per business name ordinance of 1918, business name shall be registered.	Not Mandatory If the business is maintained under a different name than the owners, as per business name ordinance of 1918, business name shall be registered.	Mandatory Companies act of Number 07 of 2007
Liability	Unlimited Liability is not limited to investment. Owners are personally liable.	Unlimited Liability is not limited to investment. Owners are personally liable.	Limited Liability is limited to investment. Owners are not personally liable.
Legal Status	No Legal Personality Entity is not considered as a person in front of law. Asset purchase, liabilities obtained, cases filed under the name of owner.	No Legal Personality Entity is not considered as a person in front of law. Asset purchase, liabilities obtained, cases filed under the name of owner.	Legal Personality Entity is considered as a person in front of law. Asset purchase, liabilities obtained, cases filed under the name of Company.
Succession	Business ceases upon owner's	Dissolves in a change of	Perpetual Succession Company continues despite the

Description	Sole Proprietorships	Partnerships	Companies
Setting Up	Easy	Moderate	Complex
Compliance Cost	Low	Moderate	High
Liability	Unlimited	Unlimited but shared among Partners	Limited
Access to Capital	Limited	Moderate	High
Business Continuity	Weak	Moderate	High
Tax	Personal	Allocated among Partners	Corporate Tax

1.4 The Purpose and Processes of Financial Reporting

Common Definition for Financial Reporting

Accounting is the process of providing Financial Information of an Accounting Entity

To the Stakeholders of the Entity

For them to Take Economic Decisions

Common Definition for Financial Reporting

Financial Reporting is the process of recording, analyzing, summarizing and presenting an entity's financial activities to assess financial performance and financial position.

Financial Reporting Process

Inputs	Process		Outputs
Transactions	Collecting	Source documents	**Financial Statements**
Exchange of recourses	Recording	Prime entry books	Statement of Profit or Loss
Two or more parties	Classifying	General ledger	Statement of Financial Position
Management decisions	Summarizing	Trial balance & FS	Statement of Changes in Equity
Measured monetary	Interpreting	Ratios	Statement of Cash Flows
E.g. Cash Sale Rs. 5,000	Communicating	Annual report	Notes
Events			
Change of recourses			
Measured monetary			
E.g. Fire damage Rs.1Mn			

1.5 Users of Financial Statements and Their Information Needs

Classification of Users

Category	Specific Users	Role/Interest
Primary External Users	Existing and Potential • Investors • Lenders • Other Creditors (Suppliers)	Provide capital (Equity and Debt). Assess the risk and return on their investment.
Internal Users	Management (Board of Directors)	Run the company on behalf of shareholders and monitor the operations.
Other External Users	Government and Regulatory agencies, Customer, Employees, Competitors and Public	To provide and receive economic resources.

Different Users and Their Information Needs

User	Information Need	Decisions
Investors	• Profitability • Growth • Risk and Return on Investment	• To buy, hold or sell shares • To assess the performance of Management
Lenders	• Ability to repay the loans and interest • Cash flow stability	• To assess creditworthiness • Setting credit terms
Management	• Profit or Loss • Efficiency • Assets	• Strategic planning • Budgeting • Controlling operations
Government	• Taxable income • Tax payable	• Tax • Compliance

Different Users and Their Information Needs

User	Information Need	Decisions
Employees	• Stability of Business • Profitability	• Job security • To negotiate pay and benefits
Customers	• Long term stability	• Reliability for long term contracts
Suppliers	• Ability to settle	• To decide whether to offer credit terms
Competitors	• Financial performance • Business strategies	• To benchmark own performance