

EASTERN UNIVERSITY, SRI LANKA
FACULTY OF COMMERCE AND MANAGEMENT

Final Year First Semester Examination in Bachelor of Commerce / Bachelor of
Commerce (Specialization in Accounting and Finance)-2014/2015(May 2017)

(Proper)

DAF 4013 Financial Reporting and Statement Analysis

Answer All Questions

Time Allowed: 03 Hours

Programmable Calculators are permitted.

Describe the different types of business analysis.

(04 Marks)

Identify the category of users of financial statements that applies to different types of business analysis.

(04 Marks)

Identify and discuss four major activities of a business enterprise.

(04 Marks)

Explain how financial statements reflect the business activities of a company.

(04 Marks)

Briefly describe the four specialized financial analysis tools.

(04 Marks)

(Total 20 Marks)

The year - end balance sheets of GSK Plc are as follows:

	2016	2015	2014
	Rs.	Rs.	Rs.
Plant and Machinery	277,500	255,000	229,500
Merchandise inventory	111,500	82,500	53,000
Accounts receivable	88,500	62,500	49,200
Prepaid expenses	9,700	9,375	4,000
Cash	30,800	35,625	66,800
Total Assets	518,000	445,000	372,500
Ordinary share capital (Rs.10 each)	162,500	162,500	162,500
Retained earnings	129,100	104,750	78,250
Long-term notes	97,500	102,500	82,500
Accounts payables	128,900	75,250	49,250
Total liabilities and equity	518,000	445,000	372,500

GSK Plc's Income Statements for the years ended December 31, 2016 and 2015 show the following:

	2016		2015	
	Rs.	Rs.	Rs.	Rs.
Sales		672,500		530,000
Cost of goods sold	410,225		344,500	
Other operating expenses	208,550		133,980	
Interest expenses	11,100		12,300	
Income taxes	8,525		7,845	
Total costs and expenses		(638,400)		(498,625)
Net Income		34,100		31,375
Earnings per share		2.10		1.93

Required:

- (a) Compare the year-end short-term liquidity position of GSK Plc at the end of 2016, 2015, and 2014 by computing the: (i) current ratio and (ii) acid-test ratio. Comment on the ratio results.
- (b) For the years ended December 31, 2016 and 2015, assume all sales are on credit and then compute the following: (i) days' sales in receivable, (ii) accounts receivable turnover, (c) inventory turnover, and (iv) days' sales in inventory. Comment on the changes in the ratios from 2015 to 2016.
- (c) Compare the long-term risk and capital structure positions of the company at the end of 2016 and 2015 by computing the following ratios: (i) total debt to equity ratio and (ii) times interest earned.
- (d) Evaluate the efficiency and profitability of the company by computing the following: (i) net profit margin, (ii) total asset turnover, and (iii) return on total assets.

(10 Marks)

- Describe the major disclosure requirements for long-term liabilities. **(04 Marks)**
- Discuss the implications of lease accounting for the analysis of financial statements. **(04 Marks)**
- Identify types of equity securities that are similar to debt. **(04 Marks)**
- Distinguish between different kinds of deferred credits on the balance sheet and discuss how to analyze these accounts. **(04 Marks)**
- Discuss key estimates in accounting for pension and other postretirement benefits and how these estimates affect net income and total liabilities. **(04 Marks)**
- (Total 20 Marks)**

Describe the impact of the operating cycle concept for classification of current assets in the following industries: (i) tobacco (ii) liquor, and (iii) retailing **(04 Marks)**

Describe information, other than that usually available in financial statements, that analyst should collect to assess the risk of noncollectibility of receivables. **(04 Marks)**

FDV Plc purchases its merchandise at current market costs and resells the product at a price 20 percent higher. Its inventory costs are constant throughout the current year 2016. Data on the number of units in inventory at the beginning of the year, unit purchases, and unit sales are shown below:

	Unit Price (Rs.)	Units
Inventory at the beginning of the year 2016	1000	1000
Purchased during the year 2016	1500	1000
Sales during the year 2016	1800	1000

- (II) Comparative statements of Financial Positions of LHN plc for years ended 31 December 2010 - 2016 are reproduced below (Rs.000):

Assets	2016	2015	2014	2013	2012	2011	2010
Plant and equipment	2,120	2,114	1,852	1,044	1,078	960	825
Long-term investment	0	0	0	136	136	136	136
Inventory	1,738	1,264	1,104	932	836	710	510
Accounts receivable	480	504	456	350	308	292	200
Other current assets	46	42	24	44	38	38	19
Cash	68	88	92	94	98	96	90
Total assets	4,452	4,012	3,528	2,600	2,494	2,232	1,800
Liabilities and Equity							
Ordinary share capital	1,000	1,000	1,000	840	840	640	640
Preference share capital	250	250	250	180	180	160	160
Retained earnings	888	780	648	596	548	490	330
Long-term liabilities	1,194	1,040	1,012	470	480	520	330
Current liabilities	1,120	942	618	514	446	422	270
Total liabilities and equity	4,452	4,012	3,528	2,600	2,494	2,232	1,800

Required:

- (a) Compute trend percents for the individual items of the statements of Financial position using 2010 as the base year
- (b) Prepare common-size statements showing the percent of each item to total assets or total liabilities and equity for the years 2010 - 2016.
- (c) Analyze and comment on financial positions using figures in (a) and (b) above.

(10 Marks)

(Total 20 Marks)

The beginning of the year 2016 balance sheet for FDV Plc reports the following:

	Rs.
Inventory	1000,000
Other assets	1500,000
Total equity	1200,000
Other liabilities	1300,000

Required:

Determine the after tax net income for the year 2016 using each of the following inventory accounting methods. Assume an operating cost of Rs.120,000 and 40% income taxes which are accrued currently and paid in the following year.

- (i) First In First Out (FIFO)
- (ii) Last In First Out (LIFO)

If all sales, purchases, and operating cost are for cash, construct the balance sheet at the end of the year 2016 separately for both the (i) FIFO and (ii) LIFO methods of inventory valuation.

(12 Marks)

(Total 20 Marks)

Distinguish between the permanent and transitory components of income. Cite an example of each and discuss how each component affects analysis.

(04 Marks)

Accounting practice distinguishes among different types of accounting changes. Identify three different types of accounting changes.

(04 Marks)

What conditions are necessary for an item to qualify as a prior period adjustment?

(04 Marks)

- (IV) FRH Plc reported net income totaling Rs.1000,000 for the year 2016. The following is additional information obtained from the company's financial reports:
- (a) The company purchased 100,000 shares of MRH plc for Rs.10 per share during the fourth quarter of 2016. The investment is accounted for as "available for sale". The value of the shares is Rs.9 at the end of 2016.
 - (b) The company purchased 10,000 shares of SJF Plc for Rs.20 per share during the fourth quarter of 2016. The investment is accounted for as "Trading" securities. The value of the shares is Rs.22 at the end of 2016.
 - (c) The company began operations in the Baltic region of Europe during the year and reports a foreign currency translation gain of Rs.50,000 at the end of 2016.
 - (d) The actual return on assets in its pension fund is Rs.150,000. The expected return was Rs.110,000.
 - (e) The company has substantial prior service cost associated with its employee pension plan. As a result, the company had to record an additional minimum pension liability of Rs.25,000 during the year.
 - (f) The company reported unrealized holding losses of Rs.12,000 on its derivatives instruments.

Required:

- (a) Compute the Comprehensive Income for the year 2016 for FRH Plc.
- (b) For each item in comprehensive income, discuss the balance sheet account affected by the item.

(08 Marks)

(Total 20 Marks)