

**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)-2018/2019 (August 2020)**  
**(Proper/Repeat)**

**DAF 4013 Financial Reporting and Statement Analysis**

**Answer All Questions**

**Time Allowed: 03 Hours**

**Non Programmable Calculators are permitted.**

- (I) Explain the meaning of financial statement analysis and state its objectives.  
**(05 Marks)**
- (II) Describe the information needs of internal and external users of financial statements.  
**(05 Marks)**
- (III) State five additional sources of financial reporting information (beyond financial statements) that are useful for analysis.  
**(05 Marks)**
- (IV) Explain how the efficient market hypothesis (EMH) depicts the reaction of market prices to financial and other data.  
**(05 Marks)**
- (Total 20 Marks)**

- (I) The Statement of Financial Position of MBC plc as at 31st December 2019, 2018, and 2017 are as follows:

	<b>2019</b>	<b>2018</b>	<b>2017</b>
	Rs.000	Rs.000	Rs.000
Property, plant, etc	277,500	255,000	229,500
Merchandise inventory	111,500	82,500	53,000
Accounts receivable, net	88,500	62,500	49,200
Prepaid expenses	9,700	9,375	4,000
Cash	30,800	35,625	36,800
<b>Total Assets</b>	<b>518,000</b>	<b>445,000</b>	<b>372,500</b>

Equity Capital (Rs.10 PS)	162,500	162,500	162,5
Retained Earnings	129,100	104,750	78,2
Long-term Loans mortgaged on plant assets	97,500	102,500	82,5
Accounts payable	128,900	75,250	49,2
<b>Total liabilities and equity</b>	<b>518,000</b>	<b>445,000</b>	<b>372,5</b>

**Required:**

Express the above statements of financial position information in common-size percent and assess the company's structure of financial position.

(10 Mar)

(II) The following are the information related to a statement of financial position of a company:

**Statement of financial position as at 31.12.2019**

Liabilities	Rs.	Assets	Rs.
Ordinary Share Capital	.....	Land	.....
Retained Earnings	100,000	Buildings	.....
Current Liabilities	.....	Inventory	50,00
		Accounts Receivable	.....
		Cash	.....
	.....		.....

**Additional Information:**

Assets – Liabilities = Rs.600,000; Shareholders' Equity = 3 x Total Liabilities; Carrying amount of Land is two-thirds of the building; Acid-test ratio = 1.25; Ending inventory turnover is 15; Gross profit is 44 percent of the cost of goods sold; Days' sales in accounts receivable is 20.

**Required:**

Reconstruct the statement of financial position using the additional information given above.

(10 Mar)

(Total 20 Mar)

- (I) The incomplete extracts of income statement of RMC plc. for the past five years are given below.

**RMC Plc's Income Statement for the years ended 31<sup>st</sup> of December**

	2019	2018	2017	2016	2015
	Rs.000	Rs.000	Rs.000	Rs.000	Rs.000
Net Sales	?	3,490	2,860	?	?
Cost of Sales	3,210	?	?	1,210	1,610
Gross Profit	3,670	680	1,050	1,670	1,200
Operating Expenses	?	?	?	?	550
Income Before Taxes	2,740	215	105	740	?
Taxes	?	?	?	350	250
Net Income	1,485	145	58	?	?

**Required:**

Perform a Horizontal comparative analysis of RMC plc by completing the above income statements and setting 2015 as the base year. Describe and comment on any significant findings in your comparative analysis.

**(10 Marks)**

- (II) The SLP plc experienced the following unrelated events and transactions during year ended 31<sup>st</sup> December 2019. The Company's existing current ratio is 2:1 and its quick ratio is 1.2:1.

1. Company estimates Rs.20,000 of accounts receivable are uncollectible.
2. A bank notifies Company that a customer's cheque for Rs.5,000 is returned marked insufficient funds. The customer is bankrupt.
3. The owners of Company make additional cash investment of Rs.100,000.
4. Inventory costing Rs.15,000 is judged obsolete when a physical inventory is taken.
5. Company declares a Rs.25,000 cash dividend to be paid during the first week of next reporting period.
6. SLP plc purchases long-term investments for Rs.250,000.
7. Accounts payable of Rs.24,000 are paid.
8. SLP plc borrows Rs.40,000 from a bank and gives a 90-day, 10 percent promissory note in exchange.
9. Company sells a vacant lot for Rs.250,000 that had been used in its business.
10. A three-year insurance policy is purchased for Rs.20,000.

**Required:**

Separately evaluate the immediate effect of each of the transactions for the company's

- (a) Current ratio
- (b) Quick (acid-test) ratio
- (c) Working capital

(10 Mark

(Total 20 Mark)

04. (I) Compare and contrast effects of the FIFO and LIFO inventory costing methods on earnings during a period of inflation.

(06 Mark

(II) Excerpts from the annual report of LDM plc are given for the two years:

	Year 2019 Rs.	Year 2018 Rs.
Inventory (LIFO)	219,700	241,100
Cost of sales	754,600	675,200
Net income	31,200	64,100
Tax rate	25%	25%

Note 1: If the First-In-First-Out (FIFO) method of accounting for inventory had been used, inventory would have been Rs.269,700 and Rs.251,500 at end of Year 2019 and Year 2018 respectively.

**Required:**

- (a) What would net income after tax for the year ended Year 2019 have been had FIFO been used?
- (b) Discuss the usefulness of LIFO to FIFO restatements for analysis purposes.

(14 Mark

(Total 20 Mark

) Briefly explain the following:

- (a) Credit analysis process
- (b) Credit rating agencies

**(10 Marks)**

II) Capital Structure and Earnings for Year 2019 of RET plc are as follows:

Number of ordinary shares outstanding on 31.12.2019	5,000,000
Number of 15% Convertible debentures of Rs.100 each	100,000
Ordinary Shares of issuable on conversion per debenture	10
Interest for the year	1,500,000
Net Income After Interest for Year 2019	Rs.12,000,000

**Required:**

Calculate the following:

- (a) Basic Earnings Per Share
- (b) Diluted Earnings Per Share

**(10 Marks)**

**(Total 20 Marks)**