

The Impact of Sri Lanka Financial Reporting Standards (SLFRS)-16 on Key Financial Ratios of Listed Companies in Sri Lanka.

Induranga, P.D.R.¹ and Karunarathne, W.V.A.D.²

¹induranga999@gmail.com; ²anurawvadk@kln.ac.lk

Abstract

SLFRS sets out new rules for the recognition and measurement of leases in an organization. The introduction of the new standard removes the lessee's distinction between operating and finance leases, leading to an increase in leased assets and financial liabilities on the statement of financial position or balance sheet of the lessee. Hence, companies with material off-balance sheet leases will encounter significant changes in their key financial metrics. Several prior studies have investigated the potential impact on financial metrics due to the change in the new lease standard of SLFRS 16. By reviewing the previous studies thoroughly, they have revealed mixed results. Accordingly, some studies showed that significant deviations from the financial indicators and some studies had tested the impact of operating lease capitalization on investor decision making. Therefore, the present study aims to analyze the potential impact of operating lease capitalization on listed companies' key financial ratios in Sri Lanka using an advanced constructive capitalization method. This research examines the lease capitalization effects on companies' financial ratios listed on the Colombo Stock Exchange in the year 2018. The comparative model examines the change of a company's financial ratios in the sample before and after the capitalization of operating leases. The research findings intend to extend the scope of regulators and standard setters by requiring companies to disclose their operating lease. Additionally, it will increase the benefit of information on operating lease in decision making. Further, it will reduce the accounting practices that hide debts by voluntarily disclosing the present value of lease commitments in notes to the financial statements.

Keywords: Colombo Stock Exchange, Financial Ratios, Lease Liabilities, Operating Lease, SLFRS 16.