



ASSOCIATION OF ACCOUNTING TECHNICIANS OF SRI LANKA

AA3 EXAMINATION - JULY 2018

(AA31) FINANCIAL ACCOUNTING AND REPORTING

• **Instructions to candidates** (Please Read Carefully):

- (1) **Time Allowed:** Reading : 15 minutes
Writing : 03 hours.

21-07-2018
Morning
[8.45 – 12.00]

No. of Pages : 10
No. of Questions : 09

- (2) **All questions should be answered.**
 (3) **Answers should be in one language, in the medium applied for, in the booklets provided.**
 (4) **Submit all workings and calculations. State clearly assumptions made by you, if any.**
 (5) **Use of Non-programmable calculators is only permitted.**
 (6) **Action Verb Check List with definitions is attached. Each question will begin with an action verb. Candidates should answer the questions based on the definition of the verb given in the Action Verb Check List.**
 (7) **100 Marks.**

SECTION A

Four (04) compulsory questions

(Total 20 marks)

Question 01

In addition to the fundamental qualitative characteristics, there are other qualitative characteristics that enhance the usefulness of information that is relevant and faithfully represented. The enhancing qualitative characteristics may also help to determine which of two ways should be used to depict a phenomenon if both are considered equally relevant and faithfully represented.

You are required to:

Explain any two(02) qualitative characteristics that enhance the usefulness of information. (05 marks)

Question 02

The primary purpose of an integrated report is to explain to providers of financial capital how an organization creates value over time. An integrated report includes eight key components. Business model and organizational overview and external environment are two key components included in an integrated report.

You are required to:

State two(02) key areas in business model and three(03) key areas in organizational overview and external environment of an integrated report. (05 marks)

Question 03

Osheeta Transport Services Ltd. has purchased a heavy vehicle for a value of Rs.6.5 million. Initial deposit of Rs.1.5 million was paid on 01st April 2017 and the company entered into a finance lease agreement with **AB Bank Ltd.** for the remaining value (Rs.5 million) on the same day. The terms of lease agreement are as follows:

Annual lease installment	Rs.1,473,959/-
Term	5 years
Interest rate	14.5% per annum
Lease rental due date	31 st March of each year

The useful life of the vehicle is 5 years and the company uses the straight-line basis to depreciate the vehicle.

You are required to:

Prepare the extracts of the statement of financial position as at 31st March 2018 and the statement of comprehensive income for the year ended 31st March 2018 in respect of the above.

(Assume that lease rentals were paid on due dates)

(05 marks)

Question 04

The following information was extracted from the books of **Jaz Ltd.:**

- (1) On 01st February 2018, **Jaz Ltd.** issued 100,000 ordinary shares at an issue price of Rs.10/- each. Of this total consideration, Rs.6/- per share is payable on application before 20th March 2018 and the balance of Rs.4/- per share is payable on allotment on 10th April 2018. The company has received applications for 120,000 shares and rejected the excess applications with money received by 30th March 2018.
- (2) The company has obtained a bank loan of Rs.5 million on 01st January 2018 from **ABC Bank**. As per the loan agreement, re-payments have been started from 31st January 2018 and the breakup of the installments paid was as follows:

	Total Installment paid (Rs.)	Interest portion (Rs.)
31.01.2018	77,955	68,700
28.02.2018	77,955	64,200
31.03.2018	77,955	61,380
Total	233,865	194,280

- (3) The company has obtained a bank overdraft facility of Rs.750,000/- on 31st March 2018.
- (4) The company has given a long term loan of Rs.1,000,000/- on 31st March 2018 to a founder employee of the company.

You are required to:

Prepare the Net Cash Flows generated from financing activities for the year ended 31st March 2018.

(05 marks)

End of Section A

SECTION B

Three (03) compulsory questions

(Total 30 marks)

Question 05

Extracts of the Statements of Comprehensive Income of **Multi Chemi Exports (Pvt) Ltd.** for the years ended 31st March 2018, 31st March 2017 and 31st March 2016 and extracts of the Statements of Financial Position as at 31st March 2018, 31st March 2017 and 31st March 2016 are as follows:

Extracts of Statements of Comprehensive Income (Rs.'000)

For the year ended	31st March 2018	31st March 2017	31st March 2016
Turnover	127,500	105,000	133,000
Cost of sales	88,500	71,200	93,100
Gross profit	39,000	33,800	39,900
Income tax	2,240	1,070	1,980
Profit after tax	8,020	8,130	12,020

Extracts of Statements of Financial Position (Rs.'000)

As at	31st March 2018	31st March 2017	31st March 2016
Current assets	20,470	26,260	38,000
Current liabilities	13,200	17,875	12,280
Trade receivables	15,460	14,220	18,900
Trade payables	6,400	6,100	8,440
Inventory	2,680	11,530	18,650
Shareholders' equity	39,540	31,520	23,390

You may assume that the credit sale is 55% from the total turnover. Further, 90% of cost of sales consists of purchases and out of that 70% is on credit terms.

You are required to:

Analyze the performance of **Multi Chemi Exports (Pvt) Ltd.** for the years ended / as at 31st March 2018 and 31st March 2017 considering the following ratios:

- (a) Gross Profit Ratio.
- (b) Net Profit Ratio.
- (c) Quick Assets Ratio.
- (d) Debtors' Collection Period
- (e) Creditors' Settlement Period.

(10 marks)

Question 06

The Statements of Financial Position of **Seven Roses Ltd.** as at 31st March 2017 and 31st March 2018 are given below:

Seven Roses Ltd.
Statements of Financial Position (Rs.'000)

	As at 31 st March 2018		As at 31 st March 2017	
Assets				
Non-Current Assets:				
Property, Plant and Equipment (at cost)	46,000		56,000	
Accumulated Depreciation	(24,000)		(20,000)	
Carrying value		22,000		36,000
Current Assets:				
Inventories	16,000		5,800	
Trade Receivables	33,500		29,400	
Cash and Cash Equivalents	3,500	53,000	5,000	40,200
Total Assets		75,000		76,200
Equity and Liabilities				
Equity:				
Ordinary Share Capital		50,000		50,000
Retained Earnings		7,200		6,000
		57,200		56,000
Current Liabilities:				
Trade and Other Payables	17,700		19,800	
Income Tax Payable	100	17,800	400	20,200
Total Equity and Liabilities		75,000		76,200

The following additional information is also provided:

- (1) During the year, the company paid interim dividend of Rs.2,000,000/- to its ordinary shareholders.
- (2) On 31st March 2018, the company sold a machinery for Rs.4 million which was purchased on 01st April 2015 at a cost of Rs.10 million. The useful life time of the machinery is 5 years.
- (3) There were no purchases of Property, Plant and Equipment during the year.
- (4) The income tax expense of the company for the year of assessment 2017/18 was estimated to be Rs.450,000/-.

Using the above information,

You are required to:

Prepare the Cash Flow Statement of **Seven Roses Ltd.** for the year ended 31st March 2018 using indirect method.

Question 07

- (a) The following information has been given in relation to **SRL Ltd.** for the year ended 31st March 2018.

The company has reviewed the useful life of Plant and Machinery on 01st April 2017. As per the review it was decided to change the useful life time of the Plant and Machinery from 3 years to 8 years from 01st April 2017. Cost and accumulated depreciation of Plant and Machinery as at 01st April 2017 were Rs.8,000,000/- and Rs.3,200,000/- respectively.

You are required to:

Explain the accounting treatment for the year ended 31st March 2018 for the above instance as per the LKAS 8 - Accounting Policies, Changes in Accounting Estimates and Errors. (04 marks)

- (b) The following information is related to **XYZ Ltd.** for the year ended 31st March 2018.

- (1) The entity sells goods with a warranty under which customers are covered for the cost of repairs of any manufacturing defects that become apparent within the 1st six months after purchase. The entity's past experience indicates that 2% on the sales has to be paid as repair cost for warranties and sales of Rs.30 million were recorded for the year ended 31st March 2018. Assume that sales are distributed evenly throughout the year.
- (2) There was an assessment raised by the Department of Inland Revenue on the income tax of Rs.2.5 million on a disallowed portion of an expense incurred in the year of assessment 2015/16. After sending several replies and correspondence, with reference to the expense, the tax appeals commission had finalized it as Rs.2 million on 30th March 2018. This had not been incorporated in the financial statements.
- (3) The company has dismissed an employee due to a fraud committed on 25th March 2018 and the employee has filed a case in courts against the company. Up to the date of authorization of the financial statements for issue, for the year ended 31st March 2018, the entity's lawyers have advised that it is probable that the entity will not be found liable.

You are required to:

Explain how each of the above instances could be recognized in the Financial Statements for the year ended 31st March 2018 as per the LKAS 37 – Provisions, Contingent Liabilities and Contingent Assets. (06 marks)

(Total 10 marks)

End of Section B

SECTION C

Two (02) compulsory questions.

(Total 50 marks)

Question 08

The Trial Balance of **Golden PLC** as at 31st March 2018 is given below:

Golden PLC		<i>(Rs.'000)</i>
Trial Balance as at 31st March 2018		
	Dr.	Cr.
Ordinary Share Capital - 5,000,000 shares		50,000
Retained Earnings as at 01 st April 2017		13,350
Property, Plant and Equipment (at cost):		
Land and Buildings (value of the land - Rs.30 million)	40,000	
Motor Vehicles	28,000	
Office Equipment	8,000	
Accumulated Depreciation as at 01 st April 2017:		
Buildings		4,000
Motor Vehicles		6,000
Office Equipment		1,500
Short-term Investments	25,000	
Inventory as at 31 st March 2018 (at cost)	30,000	
Trade Receivables / Trade Payables	87,000	101,850
Allowance for Trade Receivables as at 01 st April 2017		1,150
Accrued Expenses		800
Income Tax Payable for the year of Assessment 2016/17		2,000
15% Bank Loan		5,000
Cash at bank	1,200	
Cash in hand	600	
Cost of Sales / Sales	420,000	545,000
Investment Income Received		2,800
Interim Dividend paid for Ordinary Shareholders	5,000	
Administration Expenses	37,000	
Distribution Expenses	41,500	
Finance Expenses	1,350	
Income Tax Paid	8,800	
	733,450	733,450

The following additional information is also provided:

- (1) On 31st December 2017, the company has disposed five computers which were purchased on 01st April 2013 at Rs.60,000/- each. The disposal value of one computer was Rs.10,000/-. The company has not received cash yet for this transaction and no entries were made in the books of account regarding the disposal of computers.

- (2) The company obtained a Rs.5 million bank loan at an interest rate of 15% per annum on 01st April 2017 to build a new store to the company. The construction of the store was started on 01st May 2017 and finished for use on 31st December 2017. The bank loan has been fully utilized for the construction of the store and Rs.5 million has been included in the Buildings account as the cost of new store.

During the year, no repayments have been made by the company and $\frac{1}{4}$ th of the bank loan as at 31st March 2018 should be settled during the next year.

- (3) The net realizable value of the inventory as at 31st March 2018 was Rs.32,000,000/-.
- (4) On 01st March 2018, the company has revalued its land and the value of the land has increased by Rs.1.5 million due to the re-valuation. This has not been recorded in the books of accounts.
- (5) Depreciation of Property, Plant and Equipment is calculated on the straight line basis at cost or revalued amount. The useful life of Property, Plant and Equipment is as follows:

Buildings	:	25 years
Motor Vehicles	:	05 years
Office Equipment	:	10 years

- (6) As at 31st March 2018, Rs.1,500,000/- worth of trade receivables have become bad debts. A general provision of 2% is to be made for the remaining trade receivables balance as at 31st March 2018.
- (7) The investment income for the year ended 31st March 2018 is Rs.4,000,000/-.
- (8) The income tax liability of the company for the year of assessment 2017/18 is estimated as Rs.9,000,000/-.
- (9) The Board of Directors of the company has decided to pay a final dividend of 50 cents per Ordinary Share for the Ordinary Shares held on 31st March 2018 at the board meeting held on 20th May 2018.
- (10) The Financial Statements were authorized for issue by the Board of Directors on 10th June 2018.

You are required to:

Prepare the following, for **Golden PLC** in a form suitable for publication:

- (a) The Statement of Profit or Loss and Other Comprehensive Income (Statement of Comprehensive Income) for the year ended 31st March 2018. (10 marks)
- (b) Statement of Financial Position as at 31st March 2018. (07 marks)
- (c) Statement of Changes in Equity for the year ended 31st March 2018. (03 marks)
- (d) Statement showing movements of Property, Plant and Equipment for the year ended 31st March 2018. (05 marks)
- (Total 25 marks)

Question 09

- (A) **Mega Trading Ltd. (MT)** acquired 80% of the ordinary share capital of **Tiny Toys Ltd. (TT)** for Rs. 20 million on 01st April 2017. The Statements of Financial Position of **MT** and **TT** as at 31st March 2018 are as follows:

Statements of Financial Position
as at 31st March 2018 (Rs.'000)

	MT	TT
Non-Current Assets:		
Property, Plant & Equipment - Cost	60,000	15,000
Accumulated Depreciation	(12,000)	(6,000)
Carrying Value	48,000	9,000
Investment in TT	20,000	-
Current Assets:		
Inventories	15,100	18,000
Trade Receivables	40,250	10,500
	55,350	28,500
Total Assets	123,350	37,500
Equity:		
Stated Capital - Ordinary shares	78,000	20,000
Retained Earnings	8,750	4,600
	86,750	24,600
Non-Current Liabilities:		
Bank Loan	10,600	-
Current Liabilities:		
Trade Payables	15,100	10,500
Bank Loan	4,800	-
Bank Overdrafts	6,100	2,400
	26,000	12,900
Total Equity and Liabilities	123,350	37,500

The following additional information is also provided:

- (1) As at the date of acquisition, the Retained Earnings of **TT** were Rs.1,200,000/-.
- (2) Fair value of the non-controlling interest was Rs.5,000,000/- and the fair value of identifiable net assets of **TT** was equal to its book value as at the date of acquisition.
- (3) On 01st April 2017, **MT** sold one of its delivery vans purchased on 31st March 2015 at a cost of Rs.2.5 million to **TT** for Rs.3 million. Both companies depreciate their Motor Vehicles over 5 years on the straight-line basis at cost.
- (4) During the year, **TT** has sold goods for Rs.600,000/- to **MT** with a profit margin of 20% on cost. As at 31st March 2018, ½ of those goods were in the inventory of **MT**.
- (5) Trade receivables of **TT** included Rs.25,000/- which is due from **MT** for the sales transactions made during the year.

Using the above information,

You are required to:

- (a) **Compute** the goodwill arising from the consolidation. (05 marks)
- (b) **Prepare** the Consolidated Statement of Financial Position as at 31st March 2018. (14 marks)

- (B) The following ratios have been calculated on the performance of **Dynamic Enterprises Ltd.** for the financial years ended 31st March 2017 and 31st March 2018:

	For the year ended 31 st March 2018	For the year ended 31 st March 2017
Gearing Ratio	82%	65%
Return on Capital Employed (ROCE)	20%	35%
Asset Turnover Ratio	5 times	3 times

You are required to:

State two(02) possible reasons for the variations in each of the above computed ratios during the above 2 years concerned. (06 marks)

(Total 25 marks)

End of Section C

ACTION VERB CHECK LIST

Knowledge Process	Verb List	Verb Definitions
Level 01 Comprehension Recall & explain important information	Define	Describe exactly the nature, scope, or meaning.
	Draw	Produce (a picture or diagram).
	Identify	Recognize, establish or select after consideration.
	List	Write the connected items one below the other.
	Relate	To establish logical or causal connections.
	State	Express something definitely or clearly.
	Calculate/Compute	Make a mathematical computation
	Discuss	Examine in detail by argument showing different aspects, for the purpose of arriving at a conclusion.
	Explain	Make a clear description in detail revealing relevant facts.
	Interpret	Present in an understandable terms.
	Recognize	To show validity or otherwise, using knowledge or contextual experience.
	Record	Enter relevant entries in detail.
Summarize	Give a brief statement of the main points (in facts or figures).	

Knowledge Process	Verb List	Verb Definitions
Level 02 Application Use knowledge in a setting other than the one in which it was learned / Solve closed-ended problems	Apply	Put to practical use.
	Assess	Determine the value, nature, ability, or quality.
	Demonstrate	Prove, especially with examples.
	Graph	Represent by means of a graph.
	Prepare	Make ready for a particular purpose.
	Prioritize	Arrange or do in order of importance.
	Reconcile	Make consistent with another.
	Solve	To find a solution through calculations and/or explanation.

Knowledge Process	Verb List	Verb Definitions
Level 03 Analysis Draw relations among ideas and compare and contrast / Solve open-ended problems.	Analyze	Examine in detail in order to determine the solution or outcome.
	Compare	Examine for the purpose of discovering similarities.
	Contrast	Examine in order to show unlikeness or differences.
	Differentiate	Constitute a difference that distinguishes something.
	Outline	Make a summary of significant features.