



ASSOCIATION OF ACCOUNTING TECHNICIANS OF SRI LANKA

AA3 EXAMINATION - JANUARY 2020

(AA31) FINANCIAL ACCOUNTING AND REPORTING

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

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

18-01-2020  
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**

The objective of general purpose financial reporting is to provide financial information about the reporting entity that is useful to existing and potential stakeholders in making decisions. If the financial information is to be useful it must be relevant and faithful representation. In addition to that there are four qualitative characteristics for enhancing the usefulness of financial information.

**You are required to:**

**Explain** two(02) qualitative characteristics that enhance the usefulness of financial information.

(05 marks)

**Question 02**

Integrated reporting has widely recognized as a process of creating corporate value and sustainability to organizations. Organizational overview and external environment is a component of an integrated report.

**You are required to:**

(a) **State** two(02) key objectives of integrated reporting (02 marks)

(b) **State** three(03) key areas included in organizational overview and external environment.

(03 marks)

(Total 05 marks)

### Question 03

As per SLFRS 15 - Revenue from contracts with customers, an entity recognizes revenue by applying the five steps.

**You are required to:**

**State** the five(05) steps followed to recognize revenue as per SLFRS 15. (05 marks)

### Question 04

The following balances were extracted from the Statement of Financial Position of **Ameen PLC**:

As at 31 <sup>st</sup> March	2019 (Rs.'000)	2018 (Rs.'000)
Non-Current Assets:		
Property, Plant and Equipment	58,500	57,500
Accumulated Depreciation	(34,800)	(28,200)
<b>Carrying Value</b>	<b>23,700</b>	<b>29,300</b>

The following additional information is also provided:

- (1) A motor vehicle was sold on 01<sup>st</sup> January 2019 and cost and accumulated depreciation at the date of disposal were Rs.4,500,000/- and Rs.2,800,000/- respectively. Loss on disposal of the motor vehicle was Rs.475,000/-. The company acquired a motor vehicle for Rs.3,000,000/- on 31<sup>st</sup> March 2019 to replace the sold vehicle.
- (2) Office furniture included in Property, Plant and Equipment was acquired on 31<sup>st</sup> March 2019.

Using the above information,

**You are required to:**

**Prepare** the cash flows from investing activities of **Ameen PLC** for the year ended 31<sup>st</sup> March 2019.

(05 marks)

End of Section A

## **SECTION B**

Three (03) compulsory questions

(Total 30 marks)

### Question 05

The following information has been extracted from the Financial Statements of **Medi Tec (Pvt) Ltd.** as at / for the years ended 31<sup>st</sup> March 2019, 31<sup>st</sup> March 2018 and 31<sup>st</sup> March 2017:

#### Extract from Statements of Comprehensive Income (Rs.'000)

For the year ended	31 <sup>st</sup> March 2019	31 <sup>st</sup> March 2018	31 <sup>st</sup> March 2017
Turnover	300,000	275,000	260,000
Cost of sales	179,960	178,425	169,450
Gross profit	120,040	96,575	90,550
Profit before interest and Tax	43,400	38,300	41,250
Profit before Tax	38,000	35,700	34,300
Profit after Tax	27,500	28,300	27,800

**Extract from Statements of Financial Position**

*(Rs.'000)*

As at	31 <sup>st</sup> March 2019	31 <sup>st</sup> March 2018	31 <sup>st</sup> March 2017
<b>Current Assets:</b>			
Inventories	19,000	15,000	14,000
Trade Receivables	40,500	27,000	21,500
Cash and cash equivalents	8,500	6,200	7,400
	<b>68,000</b>	<b>48,200</b>	<b>42,900</b>
<b>Equity:</b>			
Stated capital	110,000	110,000	110,000
Retained earnings	60,000	32,500	4,200
	<b>170,000</b>	<b>142,500</b>	<b>114,200</b>
Long-term Loan	42,000	56,000	38,000
<b>Current Liabilities:</b>			
Trade Payables	19,500	16,200	15,300
Income Tax Payables	9,500	9,100	7,600
Accrued Expenses	8,500	6,100	6,800
	<b>37,500</b>	<b>31,400</b>	<b>29,700</b>

You may assume that all sales are made on credit basis.

Using the above information,

**You are required to:**

**Analyze** the performance of **Medi Tec (Pvt) Ltd.** for the years ended / as at 31<sup>st</sup> March 2018 and 31<sup>st</sup> March 2019 calculating the following ratios:

- (a) Gross Profit Ratio.
- (b) Net Profit Ratio.
- (c) Stock Turnover Ratio.
- (d) Debtors' Collection Period.
- (e) Return on Capital Employed (ROCE). (10 marks)

**Question 06**

The Statements of Financial Position of **Wess (Pvt) Ltd.** as at 31<sup>st</sup> March 2019 and 31<sup>st</sup> March 2018 are as follows:

<b>Wess (Pvt) Ltd.</b>		
<b>Statements of Financial Position</b>		
<i>(Rs.'000)</i>		
<b>As at 31<sup>st</sup> March</b>	<b>2019</b>	<b>2018</b>
<b>Assets:</b>		
<b>Non-Current Assets:</b>		
Property, Plant and Equipment	23,820	22,420
Accumulated Depreciation	(10,590)	(9,470)
<b>Carrying Value</b>	<b>13,230</b>	<b>12,950</b>
<b>Current Assets:</b>		
Inventories	320	470
Trade and Other Receivables	1,702	1,270
Cash and Cash Equivalents	398	210
	<b>2,420</b>	<b>1,950</b>
<b>Total Assets:</b>	<b>15,650</b>	<b>14,900</b>
<b>Equity and Liabilities:</b>		
<b>Equity:</b>		
Stated Capital	12,200	12,200
Retained Earnings	1,260	660
	<b>13,460</b>	<b>12,860</b>
<b>Non-Current Liabilities:</b>		
Long Term Loans	450	1,000
	<b>450</b>	<b>1,000</b>
<b>Current Liabilities:</b>		
Short Term Loans	150	150
Trade Payables	1,470	540
Interest Payables on loans	-	50
Income Tax Payable	120	300
	<b>1,740</b>	<b>1,040</b>
<b>Total Equity and Liabilities</b>	<b>15,650</b>	<b>14,900</b>

The following additional information is also provided:

- (1) The income tax expense for the year ended 31<sup>st</sup> March 2019 was Rs.175,000/-.
- (2) A machinery was disposed for Rs.2,000,000/- on 31<sup>st</sup> March 2019. The cost of the machinery was Rs.1,900,000/- and accumulated depreciation as at 31<sup>st</sup> March 2019 was Rs.850,000/-.
- (3) During the year the company paid interim dividend of Rs.300,000/- to its ordinary shareholders.
- (4) Interest expense on loans for the year ended 31<sup>st</sup> March 2019 was Rs.325,000/-.
- (5) There was no other comprehensive income for the year ended 31<sup>st</sup> March 2019.

**You are required to:**

**Prepare** the Statement of Cash Flows of **Wess (Pvt) Ltd.** for the year ended 31<sup>st</sup> March 2019 using indirect method.

(10 marks)

## Question 07

(A) The Finance Manager of **Githmi Ltd.** has found the following incidents occurred during the year ended 31<sup>st</sup> March 2019:

- (a) **Githmi Ltd.** had introduced a new accounting system SAP B1 with effect from 01<sup>st</sup> April 2018 and accounting policy of valuing inventory has been changed at that date. Up to 31<sup>st</sup> March 2018, the company has valued its inventory on FIFO basis, as per the new accounting system inventory is to be valued on WAC basis. It was noticed that stocks have been overvalued by Rs.6.7 million than stock value shown in the financial statements as at 31<sup>st</sup> March 2018 due to the change in accounting policy of inventory valuation.
- (b) Assistant Accountant of **Githmi Ltd.** has failed to account for depreciation in last financial year (2017/18) in respect of office equipment of Rs.500,000/- acquired on 31<sup>st</sup> December 2017. The company depreciates office equipment at cost on the straight-line basis and useful life time of the office equipment is 5 years.

**You are required to:**

**Explain** the impact of the above two instances on the financial statements for the year ended 31<sup>st</sup> March 2019 of **Githmi Ltd.** as per LKAS 8 - Accounting Policies, Changes in Accounting Estimates and Errors. (05 marks)

(B) The following information is also provided with reference to **Githmi Ltd.** for the year ended 31<sup>st</sup> March 2019:

- (a) An assessment has been sent by Department of Inland Revenue for Value Added Tax (VAT) disallowing Rs. 1.5 million of input tax on imports for the year of assessment 2017/18. There were so many discussions with Department of Inland Revenue on this and final decision has been received on 02<sup>nd</sup> April 2019 to disallow Rs. 1 million. This was not considered in the Financial Statements.
- (b) A competitor has filed a legal case against the **Githmi Ltd.** regarding the advertisement published insulting the competitor's product. The compensation claim is Rs.50 million and up to the date of authorization of the financial statements for the year ended 31<sup>st</sup> March 2019 (on 15<sup>th</sup> May 2019) the company's lawyers have advised that it is probable the company 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 31<sup>st</sup> March 2019 as per LKAS 37 - Provisions, Contingent Assets and Contingent Liabilities. (05 marks)

(Total 10 marks)

---

*End of Section B*

---

## SECTION C

Two (02) compulsory questions.

(Total 50 marks)

### Question 08

The following trial balance was extracted from the books of **Medito PLC** as at 31<sup>st</sup> March 2019:

<b>Medito PLC</b>		
<b>Trial Balance as at 31<sup>st</sup> March 2019</b>		
<i>(Rs. '000)</i>		
	<b>Dr.</b>	<b>Cr.</b>
Stated Capital (900,000 ordinary shares)		90,000
Retained Earnings as at 01 <sup>st</sup> April 2018		17,000
<b>Property Plant and Equipment at Cost:</b>		
Land	55,000	
Buildings	32,000	
Plant and Machinery	14,000	
Motor Vehicles	10,000	
Office Equipment	7,200	
Capital work-In-Progress	16,000	
<b>Accumulated Depreciation as at 01<sup>st</sup> April 2018:</b>		
Buildings		15,000
Plant and Machinery		6,000
Motor Vehicles		5,500
Office Equipment		3,500
Pre-payments	1,500	
Payments made to <b>Medi Research Ltd.</b>	2,500	
Inventory as at 31 <sup>st</sup> March 2019	32,500	
Trade Receivables / Trade Payables	41,000	36,850
Gratuity Provision		20,500
Cash in Hand and Cash at Bank	16,500	
Income Tax Paid	2,750	
Interim Dividend Paid - Ordinary Shares	9,000	
Cost of Sales / Sales	269,400	378,500
Administration Expenses	46,000	
Distribution Expenses	29,500	
Finance Expenses	500	
Allowance for Trade Receivables as at 31 <sup>st</sup> March 2018		500
Bank Loan		12,000
	<b>585,350</b>	<b>585,350</b>

The following additional information is also provided:

- (1) Inventory held as at 31<sup>st</sup> March 2019 included obsolete stock of Rs.700,000/- at cost. This was sold for Rs.250,000/- on 05<sup>th</sup> April 2019 to a buyer incurring Rs.20,000/- for transporting these stocks to the buyer's location. No entries were made in this regard.
- (2) The company has revalued its land to Rs.60 million on 31<sup>st</sup> March 2019. This has not been recorded in the books of accounts.
- (3) On 01<sup>st</sup> July 2018, the company acquired a new machinery and purchase cost of Rs.3,500,000/- has been recorded under the purchase account. In addition to that the company has incurred further Rs.500,000/- on the same date for installation and testing the machine and this was recorded under the administration Expenses.
- (4) During the year, a research was done for a new product and the company has paid Rs.2,500,000/- to **Medi Research Ltd.** for that purpose. This has been debited to payments to **Medi Research Ltd.** account. The company started commercial operation of the new product in April 2019.
- (5) The company obtained Rs. 12 million bank loan at an interest rate of 12% per annum on 01<sup>st</sup> January 2019 to construct a new factory building. No capital repayments were made during the year and interest for the year has been accounted under the finance expenses.  $\frac{1}{2}$  of the bank loan should be settled in 2019/20. Construction of the factory building was commenced on 01<sup>st</sup> January 2019 and it is expected to complete by 30<sup>th</sup> September 2020. Cost incurred on construction was recorded under the capital work-in-progress account.
- (6) Depreciation of Property, Plant and Equipment is calculated on the straight line basis at cost. The useful life of Property, Plant and Equipment is as follows:

Buildings	:	20 years
Plant and Machinery	:	10 years
Motor Vehicles	:	05 years
Office Equipment	:	10 years
- (7) The income Tax Liability of the company for the year of assessment 2018/19 has been estimated to Rs.2,950,000/-.
- (8) On 31<sup>st</sup> March 2019, it was noticed that a customer owing Rs. 2 million has been missing. The company is not in a position to recover the amount due from him and it has become irrecoverable. Further a general provision has to be made at 2% of the remaining trade receivable balance as at 31<sup>st</sup> March 2019.
- (9) Electricity bill for March 2019 of Rs.700,000/- has not been recorded in the books of accounts.
- (10) The Board of Directors of the company decided to pay Rs.5/- per share as the final dividend for ordinary shares held on 31<sup>st</sup> March 2019 at the board meeting held on 02<sup>nd</sup> May 2019.
- (11) The Financial Statements were authorized for issue by the Board of Directors on 20<sup>th</sup> June 2019.

Considering the above information,

**You are required to:**

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

- Statement of Profit or Loss and Other Comprehensive Income (Statement of Comprehensive Income) for the year ended 31<sup>st</sup> March 2019. (10 marks)
  - Statement of Financial Position as at 31<sup>st</sup> March 2019. (07 marks)
  - Statement of Changes in Equity for the year ended 31<sup>st</sup> March 2019. (04 marks)
  - Statement showing movement of Property, Plant and Equipment for the year ended 31<sup>st</sup> March 2019. (04 marks)
- (Total 25 marks)

### Question 09

- (A) The statements of Financial Position of **Gajashakthi (Pvt) Ltd. (GPL)** and **Shakthi (Pvt) Ltd. (SPL)** as at 31<sup>st</sup> March 2019 are as follows:

**Statements of Financial Position** (Rs. '000)  
**As at 31<sup>st</sup> March 2019**

	GPL	SPL
<b>Assets:</b>		
<b>Non-Current Assets:</b>		
Property, Plant and Equipment at cost	52,000	23,500
Accumulated Depreciation	(12,500)	(7,500)
Carrying Value	<b>39,500</b>	<b>16,000</b>
Investment in SPL	40,000	-
<b>Current Assets:</b>		
Inventories	13,100	27,900
Trade and Other Receivables	40,250	10,500
Cash and Cash Equivalents	2,300	1,100
	<b>55,650</b>	<b>39,500</b>
<b>Total Assets</b>	<b>135,150</b>	<b>55,500</b>
<b>Equity and Liabilities:</b>		
<b>Equity:</b>		
Stated Capital - Ordinary Shares	80,000	35,000
Retained Earnings	13,300	8,150
	<b>93,300</b>	<b>43,150</b>
<b>Non-Current Liabilities:</b>		
Long Term Loans	16,200	-
<b>Current Liabilities:</b>		
Trade and Other Payables	20,250	11,400
Short Term Loans	5,400	950
	<b>25,650</b>	<b>12,350</b>
<b>Total Equity and Liabilities</b>	<b>135,150</b>	<b>55,500</b>



The following additional information is also provided:

- (1) **GPL** acquired 80% of ordinary share capital of **SPL** on 01<sup>st</sup> April 2018.
- (2) Fair value of the non-controlling interest on the date of acquisition was Rs. 7.72 million. As at the date of acquisition retained earnings of **SPL** were Rs. 6 million and the fair value of identifiable net assets of **SPL** was equal to its book value.
- (3) As at 31<sup>st</sup> March 2019, **SPL** held inventory worth of Rs. 4.5 million purchased from **GPL**. **GPL** has sold the goods to **SPL** at a profit margin of 20% on cost. Further, **SPL** has a trade payable balance of 2.5 million which is payable to **GPL**.
- (4) **GPL** has obtained a short term loan of Rs. 4 million from **SPL** at the interest of 15% per annum on 01<sup>st</sup> April 2018. Though no capital repayments were made during the year interest on loan for the year was paid by **GPL**.

**You are required to:**

- (a) **Calculate** the Goodwill arising from the consolidation. (05 marks)
- (b) **Prepare** the Consolidated Statement of financial position as at 31<sup>st</sup> March 2019. (14 marks)

- (B) The following ratios have been calculated by **Wakkumbura Holdings PLC** for the financial years ending 31<sup>st</sup> March 2019 and 31<sup>st</sup> March 2018:

	2018/19	2017/18
Current ratio	1.75	1.5
Return on Capital Employed (ROCE)	11%	13%
Stock residence period	50 days	38 days

**You are required to:**

**State** two(02) possible reasons for the variations in each of the above computed ratios during the 2018/19 in compared with 2017/18. (06 marks)

(Total 25 marks)

---

*End of Section C*

---

## ACTION VERB CHECK LIST

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

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

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