SRI LANKA

Association of Accounting Technicians of Sri Lanka

AA3 Examination - January 2019

Questions and Suggested Answers
Aubject No. (AA 31)

FINANCIAL ACCOUNTING AND REPORTING (FAR)

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THE ASSOCIATION OF ACCOUNTING TECHNICIANS OF SRI LANKA

EDUCATION AND TRAINING DIVISION

AA3 Examination - January 2019
(AA 31) Financial Accounting and Reporting

SUGGESTED ANSWERS

SECTION A

Four (04) compulsory questions.
(Total 20 marks)

Suggested Answers to Question 01:

Chapter 01 - Conceptual Framework for Financial Reporting

a) Under financial capital maintenance, the profit is earned when the net assets at the end exceeds the net assets at the beginning after adjusting for contribution and distributions.

Under Physical capital maintenance, the profit is earned when the net productive capacity at the end exceeds the net productive capacity at the beginning after adjusting for contribution and distribution.

Main differentiation is that, the financial capital maintenance considers the capital at the nominal monetary value and any excess over the capital is considered as profit. The physical capital maintenance considers at the productive capacity term and only the increase in productive capacity is considered as profit and not the price changes of assets and liabilities.

(03 marks)

b) Net Assets = Net Assets at End – Net Assets at Beginning – Additional Capital + Drawings

= 4,500,000 - 3,200,000 - 1,000,000 + 500,000

Profit = 800,000/-

(02 marks)

(Total 05 marks)

Suggested Answers to Question 02:

Chapter 02 - Regulatory Framework

a) A sustainability report is an organizational report that gives information about economic, environmental, social and governance performance.

A sustainability report is a report published by a company or organization about the economic, environmental and social impacts caused by its everyday activities. A sustainability report also presents the organization's values and governance model, and demonstrates the link between its strategy and its commitment to a sustainable global economy.

(03 marks)

b)

1. It allows the organization to benchmark and assess sustainability performance.
2. It allows the organization to compare the performance with different organizations.
3. Holistic view of risk and opportunities.
4. Emphasizing the relationship between financial and non financial performance.
5. Benchmarking sustainability performance with respect to laws, norms, codes, performance standards and voluntary initiatives.
6. Assessment on the basis of benchmark set.
7. Improving reputation and brand image of the company.
8. Demonstrating how an organization can bring change by sustainable development.
9. Enabling external stakeholders to understand the organizations intrinsic value.

(02 marks)

(Total 05 marks)

Suggested Answers to Question 03:

Chapter 03 - Part II - Accounting Standards

a. Where the items are identified and invoiced then it is the time the sale contract is made. In this case, SHL has transferred risks and rewards to the customer. Therefore, sale of Rs. 7.5 Million should be recognized as revenue for the year ended 31st March 2018.

b. The dividend shall be recognized, when the right to receive the dividends were established. On 30.03.2018 at the AGM the right to receive dividend was established. Therefore, the dividend shall be recorded in the financial year 2017/18

c. The revenue arising from rendering of services will be recognized on a straight-line basis, as the service is for 4 year, SHL can use degree of completion and recognize the revenue, as follows;

DOC = 150,000 / 600,000 x 100 = 25%

Therefore Revenue will be = 1,000,000 X 25% = **250,000**

Rs. 250,000/- shall be recognized as revenue for the year ended 31st March 2018.

(05 marks)

Suggested Answers to Question 04:

Chapter 05 - Statement of Cash Flow (LKAS 07)

Tokyo Trading

Statement of Cash Flow – Direct Method

For the year ended 31.03.2018

	(Rs.)
Cash received from Customers (W-01)	773,000
Cash paid to Suppliers (W-03)	(643,000)
Income tax paid (W-04)	(6,500)
Expenses paid (62,000 - 12,500)	(49,500)
Net cash generated from operating activities	**74,000**

(05 marks)

Workings

(W-01)

Trade Receivables (Rs.)

B/B/F	218,000	Cash	773,000
Sales	760,000	B/C/F	205,000
	978,000		**978,000**

(W-02)

Purchases

Cost of Sales	643,000
Closing stock	132,000
Opening stock	(125,000)
Purchases	**650,000**

(W-03)

Trade Payables

Cash	643,000	B/B/F	135,000
B/C/F	142,000	Purchases	650,000
	785,000		**785,000**

(W-04)

Income Tax

Cash	6,500	B/B/F	2,000
B/C/F	3,500	P & L	8,000
	10,000		**10,000**

End of Section A

Three (03) compulsory questions
(Total 30 marks)

Suggested Answers to Question 05:

Chapter 06 - Financial Statement Analysis

To – Chief Financial Officer
From – Financial Accountant
Subject – Financial Performance

I'm pleased to submit the report regarding financial performance of Eco Protect (Pvt) Ltd for the year ended 31.03.2018. This report is structured in a way to cover the profitability, efficiency and robustness of working capital management of the Company. I have used draft and audited financial statement and used the industry average ratios to assess the efficiency and effectiveness of the Company.

Eco protest has recorded a gross profit margin of 33% and it was 40% in the industry. Even though there is an increase in the cost of sales, profit margin has slightly increased by 2% over the previous year due to increase in turnover by 10.6%.

The burden on the NP Margin could be due to increased sales commission, bad debts and debt recovery cost.

It is clearly evident that Eco protect was very much efficient in managing their capital. Therefore, the company shows an increase in ROCE comparing with the industry though PBIT shows a decline.

Increase in stock tunrover comparing with industry show an improvement in stock holding. This shows the efficiency of the business to convert stock into sales.

Debtors Turnover Ratio and Debtors Collection Ratio show a similar situation in both company and industry.

After the detailed analysis, we can conclude that Eco Protect (Pvt) Ltd is focused to increase the market share through market penetration, pricing and has succeeded. Following recommendation may assist the management in securing the margins as well,

1. The management may consider market segment and price the product accordingly.
2. Control the trade discounts to permitted limits
3. If appropriate, consider factoring of debtors

I make myself available for any explanation in this regard,

Thanking You

………………..

				The Company	Industry Average
*	**Gross Profit Ratio**	=	(72,815 / 220,650) x 100	33%	**40%**
*	**Net Profit Ratio**	=	(15,620 / 220,650) x 100	7.08%	**12%**
*	**ROCE**	=	(PBIT / Capital employed)		
		=	[17,750 / (121,030 + 9,950)] x 100	13.55%	**8%**
			OR		
	ROCE	=	(15,620 / 121,030) x 100	13%	8%
*	**Stock Turnover Ratio**	=	147,835 / 11,375	**13 times**	**10 times**
*	**Debtors' Turnover Ratio**	=	220,650 / 25,350	**8.7 times**	**9 times**
*	**Debtors' Collection Period**	=	365 / 8.7	**42 Days**	**40 Days**
			OR		
	Debtors' Collection Period	=	(25,350 / 220,650) x 365	**42 days**	

(Total 10 marks)

Suggested Answers to Question 06:

Chapter 05 - Statement of Cash Flow (LKAS 07)

Siyasto Creations (Pvt) Ltd
Statement of Cash Flow - Indirect Method
For the year ended 31.03.2018

Cash Flow from Operating Activities		
Net Profit Before Taxation		2,650,000
Adjustments for:		
Profit on Disposal **(W-01)**	(200,000)	
Depreciation **(W-04)**	1,000,000	
Interest Expenses	250,000	
Provision for Gratuity	90,000	1,140,000
Operating Profit Before Working Capital Changes		3,790,000
Income Tax paid **(W-02)**		(30,000)
Changes in Working Capital		**3,760,000**
Increase in Inventories	(955,000)	
Increase in Trade Debtors	(1,914,000)	
Decrease in Trade Creditors	(91,000)	(2,960,000)
Net CashFlows Generated from Operating Activities		**800,000**
Cash Flow from Investing Activities		
Purchase of PPE **(W-03)**	(990,000)	
Disposal of PPE	400,000	
Net Cash Flows Generated from Investing Activities		**(590,000)**
Cash Flow from Financing Activities		
Obtaining a loan	1,000,000	
Interest paid	(250,000)	
Net Cash Flows Generated from Financing Activities		750,000
Net Increase in Cash and Cash Equivalents during the year		960,000
Cash and Cash Equivalents at the beginning of the year		1,320,000
Cash and Cash Equivalents at the end of the Year		**2,280,000**

(10 marks)

Workings:

(W-01)

Disposal of Asset

Cost	550	Cash	400
P & L	200	Depreciation	350
	750		**750**

(W-02)

Income Tax

Cash	400	B/B/F	1,350
B/C/F	1,770	P & L	450
	1,800		**1,800**

(W-03)

Purchases of PPE

As at 1st April 2017	4,300
Disposal	(550)
	3,750
At the end of balance	(4,740)
Additions during the year	**(990)**

(W-04)

Depreciation

Accumulated depreciation as at 01.04.2017	1,410
Depreciation on Disposal	(350)
	1,060
Balance at the end of the year	(2,060)
Depreciation for the year	**(1,000)**

Suggested Answers to Question 07:

Chapter 03 - Part II - Accounting Standards

Section A

Leased Debtors Account

Trading Account	2,500,000.00	Cash	356,409.75
		B/C/F	2,143,590.75
	2,600,000.00		**2,600,000.00**
B/B/F	2,143,590	Cash	417,000
		B/B/F	1,726,590
	2,143,590		**2,143,590**

b)

Un-earned Finance Income Account

Income	364,410	Cash	364,410
	364,410		**364,410**

(06 marks)

a) Lease Debtors = 2,143,590

b) Un-earned Finance Income = 982,047

Workings:

Lease Schedule

Years	Op.Balance (Rs.)	Annual Interest (Rs.)	Installment (Rs.)	Closing Balance (Rs.)
1	2,500,000	425,000	(781,409.75)	2,143,590
2	2,143,590	364,410	(781,409.75)	1,726,59025
3	1,726,590.25	293,320	(781,409.70)	1,238,700.50
4	1,238,700.50	210,579	(781,409.75)	667,869.75
5	667,869.75	113,537	(781,409.75)	-

Section B

Chapter 03 - Part II - Accounting Standards

1. This is an adjusting event, therefore the effect of such fraud will be adjusted in the financial year 2017/18, by adjusting the opening inventory and the retained earnings by 35.5 Mn

2. If there is a practice to pay performance incentive for employees, it is a constructive obligation. Therefore, it should be adjusted for the year ended 31st March 2018.

   If the company has no such practice, then it is a legal liability event for the year ended 31st March 2018.

(04 marks)

(Total 10 marks)

End of Section B

SECTION C

Two (02) compulsory questions.
(Total 50 marks)

Suggested Answers to Question 08:

Chapter 04 - Financial Accounts of Limited Liability Companies

(a)

Green Garden PLC

Statement of Profit or Loss and Other Comprehensive Income

For the year ended 31.03.2018

(Rs. '000)

Description	Note	Amount
Sales (262,500 - 300 - 200)		262,000
Cost of Sales (174,500 - 1,800 + 400)		(173,100)
Gross Profit		**88,900**
Other Income - Profit on Disposal of Vehicle	(W-01)	40
		88,940
Distribution Expenses	(W-04)	(32,700)
Administration Expenses	(W-05)	(21,790)
Other Expenses (260 + 1,850)		(2,110)
Finance Expenses (3,800 - 180)	(W-03)	(3,620)
Profit before taxation		28,720
Income Tax		(6,500)
Profit after taxation		**22,220**

(10 marks)

(b)

Green Garden PLC

Statement of Financial Position

As at 31st March 2018

(Rs. '000)

Assets			
Non-Current Assets			
Property, Plant and Equipment at carrying value			32,290
WIP (600 + 180)			780
Current Assets			
Inventory (25,000 - 400)		24,600	
Trade Receivables (62,000 - 2,000)	6,000		
	(3,000)	57,000	
Pre-payment		110	
Cash in hand and at bank		200	81,910
Total Assets			**114,980**
Stated Capital		40,000	
Retained earnings		23,720	63,720
Current Liabilities			
Accrued expenses (1,000 + 200)		1,260	
Income tax payable		1,700	
Trade payables		45,000	
Bank Loan		3,000	
Bank overdraft		300	51,260
			114,980

(07 marks)

(c)

Green Garden PLC

Statement of Changes in Equity

For the Year ended 31.03.2018

Description	Stated Capital	Retained Earning	Total
Balance 01.04.2017	40,000	2,500	42,500
Dividends paid	-	(1,000)	(1,000)
Profit for the year	-	22,220	22,220
Balance 31.03.2018	**40,000**	**23,720**	**63,720**

Note **:** *The Board of Directors decided to pay Rs. 1/- per share as the final dividend for ordinary shares held on 31st March 2018.*

(03 marks)

(d)

Green Garden PLC

Statement of movements of PPE

For the Year ended 31.03.2018

Note 05 PPE

Cost

Description	**Land**	**Buidings**	**Motor vehicle**	**Office Equipment**	**Software**	**Total**
Balance 01.04.2017	20,000	10,000	10,000	3,500	-	43,500
Additions	-	-	-	-	1,800	-
Disposals	-	-		(1,200)	-	(1,200)
Balance 31.03.2018	**20,000**	**10,000**	**8,800**	**3,500**	**1,800**	**44,100**
Depreciation						
Acc. Depreciation as at 01.04.2017	-	6,000	2,000	950	-	8,950
Depreciation for the year	-	500	1,900	700	500	3,600
Disposal	-	-	(740)	-	-	(740)
Balance as at 31.03.2018	**-**	**6,500**	**3,160**	**1,650**	**500**	**11,810**
Carrying Value as at 31.03.2018	**20,000**	**3,500**	**5,640**	**1,850**	**1,300**	**32,290**

(05 marks)

Workings:

(W-01)

Disposal of Vehicle

Cost	1,200	Depreciation	740
P & L	40	Cash	200
		Insurance	300
	1,240		**1,240**

(W-02)

Disposed vehicle Depreciation

As at 01.04.2017	600
During the year [(1,200 / 5) x (7/12)]	140
	740

(W-03)

Borrowing Cost

Borrowing cost to be capitalized	
3,000 x 12% x 6 / 12	180
	180

(W-04)

Distribution expenses	26,500
Depreciation M/V	1,900
Bad debt	2,000
Provision for bad debt	2,300
	32,700

(W-05)

Administration Expenses	
TB	20,200
Depreciation - Software	500
Building	500
Office Equipment	700
Insurance	(110)
	21,790

(W-06)

Income Tax Account

Cash	6,000	B/B/F	1,200
B/C/F	1,700	P & L	6,500
	7,700		**7,700**

(W-07)

Depreciation of Motor Vehicle

Disposed Vehicle	140
Balance (8,800 / 5)	1,760
For the year	**1,900**

(Total 25 marks)

Suggested Answers to Question 09:

Chapter 07 - Group Financial Statements

Section A

(a)

Goodwill Calculation

Investment		25,000
NCI		4,420
		29,420
Net Assets		
Stated Capital	20,000	
Retained Earnings	2,100	22,100
Goodwill		**7,320**

(05 marks)

(b)

ICL and TL

Consolidated Statement of Financial Position

As at 31.03.2018 **In "000"**

	ICL	TL	Adjsutment	Consolidated
Non-Current Assets				
Property, Plant & Equipment	55,000	15,000	-	70,000
Acc. Depreciation	(12,000)	(6,000)	-	(18,000)
Carring Value	**43,000**	**9,000**	**-**	**52,000**
Goodwill - **(W-01)**				7,320
Current Assets				
Inventory **(W-03)**	20,100	20,500	(500)	40,100
Trade Receivables	34,750	10,500	(2,500)	42,750
Cash and cash equivalents	6,500	4,600	1,000	12,100
Total Assets				**154,270**
Equity				
Stated Capital	82,000	20,000	(20,000)	82,000
Retained Earnings **(W-01)**				18,930
Parent Equity				100,930
Non-Controlling Int **(W-02)**				5,340
Total Equity				**106,270**

<u>Non Current Liabilities</u>				
Bank Loan	10,200			10,200
<u>Current Liabilities</u>				
Trade Payable	13,100	8,000	(1,500)	19,600
Bank Loan	5,200	-	-	5,200
Short Term Loan		5,500	(5,500)	-
Other Payables	8,600	4,400		13,000
Total Equity & Liabilites				**154,270**

(14 marks)

Workings:

(W-01)

Consolidated Retained Earnings Account

Unrealized Profit	500	B/b/f	15,750
B/C/F	18,930	TT - Profit (4,600 x 80%)	3,680
	19,430		**19,430**

(W-02)

NCI Account

Investment	4,420
Past eq. (4,600 x 20%)	920
	5,340

(W-03)

Unrealized profit = (3,000 / 120) x 20 = **500**

Section B

Chapter 06 - Financial Statement Analysis

a)

		ICL		**TL**
Current Ratio	=	Current Assets / Current Liabilities		
	=	66,850 / 26,900	=	35,600 / 17,900
	=	**2.48 : 1**	**=**	**1.99 : 1**

b)

		ICL		**TL**
Gearing Ratio	=	Loan Capital / Equity Capital		
	=	(10,200 + 5,200) / (15,750 + 82,000)	=	5,500 / 26,700
	=	**15.75%**	**=**	**20.6%**

c)

		ICL		**TL**
Creditors Turnover Ratio	=	Credit Purchases / Average Purchases		
	=	(64,000 x 80%) / (12,000 + 13,100) / 2	=	(36,000 x 80%)/(6,000 x 8,000)/2
	=	51,200 / 12,550	=	28,800 / 7,000
	=	**4.08 times**	**=**	**4.11 times**

(06 marks)

(Total 25 marks)

End of Section C

Notice :

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