



**ASSOCIATION OF ACCOUNTING TECHNICIANS OF SRI LANKA**

**AA3 EXAMINATION - JULY 2016**

**(AA31) FINANCIAL ACCOUNTING AND REPORTING**

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

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

16-07-2016  
Morning  
[8.45 – 12.00]

No. of Pages : 08  
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**

**Identify** the amount of revenue to be recognized by **B Ltd.** for the year ended 31<sup>st</sup> March 2016 in each of the following instances:

- (a) On 28<sup>th</sup> March 2016, **Anil** informed of his intention to buy 100 units of product **X** from **B Ltd.** **B Ltd.** informed **Anil** that the selling price of product **X** is Rs.500/- per unit, and there are only 75 units available in stocks at the moment and the balance 25 units will be delivered in 2 weeks' time as those are being manufactured by now. **Anil** paid the full amount of Rs.50,000/- and collected 75 units on 30<sup>th</sup> March 2016 and agreed to get the balance 25 units later. (03 marks)
- (b) **B Ltd.** publishes a particular monthly magazine and sells at Rs.1,000/- a copy. However, **B Ltd.** charges Rs.10,000/- as the annual subscription for 12 monthly issues of that magazine, payable in advance. A customer paid Rs.10,000/- on 01<sup>st</sup> September 2015 as annual subscription.

(02 marks)

(Total 05 marks)

**Question 02**

- (a) Financial statements are normally prepared on the assumption that an entity is a going concern. **Explain** the going concern assumption. (03 marks)
- (b) **State** the two(02) fundamental qualitative characteristics of useful financial information.

(02 marks)

(Total 05 marks)

### Question 03

**State** five(05) Specified Business Enterprises (SBEs) defined in Accounting and Auditing Standards Act No. 15 of 1995. (05 marks)

### Question 04

**CC Ltd.** acquired a machinery on 01<sup>st</sup> April 2012 for Rs.4 million. Economic useful life time of the machinery was estimated to be 5 years, with no residual value. A review carried out on 01<sup>st</sup> April 2015 revealed that this machinery could be used for another 3 years. The residual value at the end of 3<sup>rd</sup> year (as at 31<sup>st</sup> March 2018) was estimated at Rs.100,000 /-.

**You are required to,**

**Compute** the following:

- (a) Depreciation charge of this machinery for the year ended 31<sup>st</sup> March 2016.
- (b) Carrying value of the machinery as at 31<sup>st</sup> March 2016. (05 marks)

————— *End of Section A* —————

### **SECTION B**

Three (03) compulsory questions  
(Total 30 marks)

### Question 05

- (a) “As per the provisions of Companies Act No. 07 of 2007, companies registered under this act have to comply with certain requirements.”

**Explain** three(03) of them. (06 marks)

- (b) Given below are two profitability ratios of **PQ Ltd.** for the years ended 31<sup>st</sup> March 2015 and 31<sup>st</sup> March 2016 respectively:

	2016	2015
Gross Profit Ratio	36.5%	38.1%
Return on Capital Employed (ROCE)	30.4%	32.6%

**You are required to,**

**State** two(02) possible reasons for each of the following:

- (i) Fall in Gross Profit Ratio.
- (ii) Fall in Return on Capital Employed (ROCE). (04 marks)
- (Total 10 marks)

### Question 06

- (a) **Omega PLC** had issued 300,000 irredeemable preference shares at Rs.10/- each on 01<sup>st</sup> April 2015. During the year ended 31<sup>st</sup> March 2016, the company has paid a dividend of Rs.1/- per preference share.

**Explain** how this share capital and dividends thereof will be shown in the financial statements of **Omega PLC** as at 31<sup>st</sup> March 2016. (03 marks)

- (b) The following items have been shown in the Statement of Financial Position as at 31<sup>st</sup> March 2016 of **A Ltd.**:

- (1) Property, Plant and Equipment with a carrying value of Rs.8 million.
- (2) Trade receivable balance of Rs.50,000/- due from **Perera**.
- (3) Cash balance of Rs.325,000/-.
- (4) Trading inventory of Rs.4 million.
- (5) A fixed deposit of Rs. 1 million in Bank of Ceylon.
- (6) Prepaid expenses of Rs. 1.2 million.
- (7) Rs.5 million investment in a subsidiary company shares.

**You are required to,**

- (i) **Identify** financial assets from the above list.
  - (ii) **State** a reason for selecting each of the above items as a financial asset. (07 marks)
- (Total 10 marks)

### Question 07

On 01<sup>st</sup> April 2015, **Pero PLC** acquired 150,000 equity shares of **Sara Ltd.** for Rs.3.5 million. On that day the fair value of the identifiable net assets of **Sara Ltd.** stood at Rs.4.3 million.

Information of the two companies are given below:

	<b>Pero PLC (Rs.)</b>	<b>Sara Ltd. (Rs.)</b>
Issued share capital	20,000,000	2,100,000
Retained earnings as at 31 <sup>st</sup> March 2015	8,000,000	640,000
Retained earnings as at 31 <sup>st</sup> March 2016	9,200,000	960,000
Property, Plant and Equipment as at 31 <sup>st</sup> March 2016 (Carrying Value)	12,000,000	4,200,000

Assume that there were no other reserves belonging to **Pero PLC** and **Sara Ltd.** Any variation in the fair value of the net assets from its book value of **Sara Ltd.** on 01<sup>st</sup> April 2015 was due to variation in the fair value of land.

**Sara Ltd.** had a total of 200,000 equity shares in issue. Fair value of **Sara Ltd.'s** shares as at 01<sup>st</sup> April 2015 was Rs.20/- per share.

You are required to,

Calculate the following with supporting workings:

- Goodwill on consolidation.
- Balance of Non-controlling Interest Account as at 31<sup>st</sup> March 2016.
- Balance of Consolidated Retained Earnings Account as at 31<sup>st</sup> March 2016.
- Value of Property, Plant and Equipment to be shown in the Statement of Consolidated Financial Position as at 31<sup>st</sup> March 2016. (10 marks)

End of Section B

### **SECTION C**

Two (02) compulsory questions.

(Total 50 marks)

#### **Question 08**

Lenin PLC is a company listed in the Colombo Stock Exchange. The Trial Balance of the company as at 31<sup>st</sup> March 2016 is as follows:

<b>Lenin PLC</b>		<i>(Rs. '000)</i>	
<b>Trial Balance as at 31<sup>st</sup> March 2016</b>		<b>Dr.</b>	<b>Cr.</b>
Property, Plant and Equipment – at cost / revaluation			
Land		16,000	
Building		19,000	
Delivery Vehicles		15,000	
Furniture and Fittings		2,000	
<u>Accumulated Depreciation as at 01<sup>st</sup> April 2015</u>			
Building			5,000
Delivery Vehicles			8,000
Furniture and Fittings			500
Inventory as at 01 <sup>st</sup> April 2015		4,000	
Purchases / Sales		24,000	49,000
Trade Receivables / Trade Payables		5,000	4,000
Allowance for Trade Receivables as at 01 <sup>st</sup> April 2015			200
Investments in listed companies		4,000	
Cash at Bank		1,000	
Cash in Hand		400	
Other Payables			300
Long Term Bank Loan			8,000
Income Tax Paid		4,500	
Interim Dividend Paid		600	
Payments to IFC Institute		10,000	
Administration Expenses		5,000	
Distribution Expenses		3,000	
Finance Expenses		500	
Other Expenses		1,500	
Stated Capital - 2,000,000 Ordinary Shares			25,000
Revaluation Reserve			2,500
Retained Earnings as at 01 <sup>st</sup> April 2015			13,000
		<b>115,500</b>	<b>115,500</b>

The following additional information is also provided:

- (1) On 31<sup>st</sup> March 2016, land was revalued at Rs.18 million and relevant adjustments are yet to be incorporated in the books of accounts.
- (2) Furniture and Fittings as at 01<sup>st</sup> April 2015 included some furniture items which were fully depreciated as at that date. The cost of those furniture items was Rs.400,000/-.
- (3) One of the delivery vehicles of **Lenin PLC**, which was purchased on 01<sup>st</sup> January 2015 at a cost of Rs.2,000,000/- met with an accident on 20<sup>th</sup> March 2016 and an insurance claim of Rs.500,000/- was received on 30<sup>th</sup> March 2016. As it was damaged badly, the company has disposed it on 31<sup>st</sup> March 2016, for Rs.1,000,000/-. The sale proceeds and the insurance claim have been debited to bank account and credited to sales account. Other than that, no entries have been made in the books of accounts in this respect.
- (4) Depreciation is calculated on the straight-line basis at cost or revalued amount. The useful life of Property, Plant and Equipment is as follows:

Building	:	20 years
Delivery Vehicles	:	10 years
Furniture & Fittings	:	5 years

- (5) During the year, **Lenin PLC** has paid a research and development expenditure of Rs.10,000,000/- to **IFC Institute**, a research company in search of an alternative IT system to be used in the company. This has been recorded under payments made to **IFC institute**.
- (6) The fair value of the investments as at 31<sup>st</sup> March 2016 was Rs.4.5 million.
- (7) Accrued interest on the long term bank loan was Rs.50,000/- which is to be accounted for in the books of accounts.  $\frac{1}{4}$ <sup>th</sup> of the outstanding loan balance as at 31<sup>st</sup> March 2016 is repayable during next year.
- (8) Allowance for Trade Receivables as at 01<sup>st</sup> April 2015 was made up as follows:

	Rs.
For amount due from customer <b>Meera</b>	55,000
General Provision	145,000
	<b>200,000</b>

Now it is proved that the amount due from **Meera** is not receivable and it is to be written-off fully.

Another Trade Receivable balance of Rs.85,000/- is also to be written-off as bad debts, and a general provision of 5% of the balance Trade Receivables is to be made as at the year-end.

- (9) Closing Stock as at 31<sup>st</sup> March 2016 was valued as Rs.5,000,000/-.
- (10) Income tax for the year of assessment 2015/16 has been estimated at Rs. 5.1 million and there was an under provision of Rs.500,000/- in respect of the previous year of assessment 2014/15. Income tax paid during the year of assessment 2015/16 includes the under provided previous year's tax.
- (11) The financial statements were authorized for issue by the Board of Directors on 20<sup>th</sup> June 2016.

**You are required to:**

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

- (a) Statement of Comprehensive Income for the year ended 31<sup>st</sup> March 2016. (08 marks)
  - (b) Statement of Financial Position as at 31<sup>st</sup> March 2016. (08 marks)
  - (c) Statement of Changes in Equity for the year ended 31<sup>st</sup> March 2016. (03 marks)
  - (d) Statement showing movements of Property, Plant and Equipment for the year ended 31<sup>st</sup> March 2016. (06 marks)
- (Total 25 marks)

### Question 09

The Statements of Financial Position as at 31<sup>st</sup> March 2016 and 31<sup>st</sup> March 2015 and the Statement of Comprehensive Income for the year ended 31<sup>st</sup> March 2016 of **MCS Ltd.** are given below:

**MCS Ltd.**  
**Statements of Financial Position** (Rs.'000)

	As at 31 <sup>st</sup> March 2016	As at 31 <sup>st</sup> March 2015
<b><u>Assets</u></b>		
<b>Non-Current Assets:</b>		
Property, Plant and Equipment	12,000	7,000
<b>Current Assets:</b>		
Inventories	8,150	6,250
Trade Receivables	2,000	1,400
Prepayments	700	200
Cash and Cash Equivalents	1,800	3,450
	<b>12,650</b>	<b>11,300</b>
<b>Total Assets</b>	<b>24,650</b>	<b>18,300</b>
<b><u>Equity and Liabilities</u></b>		
<b>Equity:</b>		
Stated Capital – Ordinary Share Capital	5,000	5,000
Revaluation Reserve	2,500	2,000
Retained Earnings	6,150	3,150
<b>Total Equity</b>	<b>13,650</b>	<b>10,150</b>
<b>Non-Current Liabilities:</b>		
Interest Bearing Borrowings	7,000	5,000
<b>Current Liabilities:</b>		
Trade Payables	2,300	2,050
Income Tax Payables	400	200
Accrued Expenses	1,000	750
Bank Overdraft	300	150
	<b>4,000</b>	<b>3,150</b>
<b>Total Equity and Liabilities</b>	<b>24,650</b>	<b>18,300</b>

**MCS Ltd.**  
**Statement of Comprehensive Income**  
**for the year ended 31<sup>st</sup> March 2016**

	Rs.'000
Sales	12,000
Cost of Sales	(5,000)
<b>Gross Profit</b>	<b>7,000</b>
Distribution Expenses	(900)
Administration Expenses	(1,500)
<b>Operating Profit</b>	<b>4,600</b>
Finance Expenses	(600)
<b>Profit Before Tax</b>	<b>4,000</b>
Income Tax	(1,000)
<b>Profit for the Year</b>	<b>3,000</b>
Other Comprehensive Income	500
<b>Total Comprehensive Income for the year</b>	<b>3,500</b>

The following additional information is also provided:

- (1) Depreciation for the year ended 31<sup>st</sup> March 2016 which was included under Administration Expenses, was Rs.1,000,000/-.
- (2) Increase in Revaluation Reserve account was on account of the revaluation of land on 31<sup>st</sup> March 2016.
- (3) An office equipment with a cost of Rs.400,000/- and a carrying value of Rs.80,000/- as at the date of disposal was sold for Rs.30,000/- during the year.
- (4) Operating profit and sales for the year ended 31<sup>st</sup> March 2015 were Rs.5,200,000/- and Rs.13,500,000/- respectively.
- (5) Total assets as at 31<sup>st</sup> March 2014 were Rs.15,750,000/-.

**You are required to:**

- (a) **Prepare** the Statement of Cash Flows of **MCS Ltd.** for the year ended 31<sup>st</sup> March 2016 using the indirect method. (15 marks)
- (b) **Calculate** the following ratios of **MCS Ltd.** for the years ended 31<sup>st</sup> March 2015 and 31<sup>st</sup> March 2016:
  - (i) Gross Profit Ratio (only for the year ended 31<sup>st</sup> March 2016).
  - (ii) Net Profit Ratio (only for the year ended 31<sup>st</sup> March 2016).
  - (iii) Assets Turnover Ratio.
  - (iv) Current Ratio.
  - (v) Quick Assets Ratio. (10 marks)

(Total 25 marks)

*End of Section C*

## **ACTION VERB CHECK LIST**

<b>Knowledge Process</b>	<b>Verb List</b>	<b>Verb Definitions</b>
<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).	

<b>Knowledge Process</b>	<b>Verb List</b>	<b>Verb Definitions</b>
<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.

<b>Knowledge Process</b>	<b>Verb List</b>	<b>Verb Definitions</b>
<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.