



**Association of Accounting Technicians of Sri Lanka**

**January 2017 Examination - AA3 Level**

**Questions and Suggested Answers  
(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 2017**  
**(AA 31) Financial Accounting and Reporting**

**SUGGESTED ANSWERS**

**SECTION A**

Four (04) compulsory questions.

(Total Marks 20)

*Suggested Answers to Question No. 01*

(a) An asset is a resource controlled by the entity as a result of past event and from which future economic benefits are expected to flow to the entity.

(02 marks)

- (b)
1. Objective of financial reporting / Statement
  2. The qualitative characteristics of useful financial information
  3. Concept of capital and capital maintenance

(03 marks)

(Total 05 marks)

*Suggested Answers to Question No. 02*

- (a)
- 1 A statement of cash flows helps to assess the ability of an enterprise to generate cash and cash equivalent.
  - 2 It enables the company to calculate the present values of future cash flows and to compare them among different business enterprises.
  - 3 It helps to understand the ability of an enterprise to generate cash and their effective utilization for various purposes.
  - 4 It gives a good understanding on probable changes in net assets and finance structure when it is used in conjunction with the other components of the financial statements.
  - 5 Historical cash flow information could be used as an indicator for determining the amount of timing and certainty of future cash flows.
  - 6 Actual cash flows could be used as an index to plan ahead the control over the future cash flows.

(03 marks)

- (b)
1. Treasury bills
  2. Current accounts with bank

3. Saving accounts (which form part of cash and cash equivalent – day to day Cash management)
4. Bank overdraft
5. Cash in hand

(02 marks)

(Total 05 marks)

### ***Suggested Answers to Question No. 03***

1. **Not an intangible asset**

**Reason :** Recruitment of special skilled employees with a salary of Rs. 500,000/- per month on permanent basis cannot be considered as an expense relevant to the development process, as it needs to be continued even after the development is completed. Therefore, it is a recurring expenditure.

2. **An intangible asset**

**Reason :** Purchase of software at a cost of Rs. 2.5 million can be recognized as an intangible asset. Without installing software, the commercial production cannot be started, thus it means without the software future economic benefits will not be probable to flow to the entity.

3. **An intangible asset**

**Reason :** Purchase of export license can be treated as an intangible asset, thus Rs. 1 million can be capitalized. Externally acquired license satisfies the identifiability as it arises as a result of contractual or legal right even though it is not transferable.

(05 marks)

### ***Suggested Answers to Question No. 04***

**Stock Sheet (Stock Ledger)**

Date	Issue			Receipts			Balance	
	Qty.	Price	Amount	Qty.	Price	Amount	Qty.	Amount
01.04.2016							16,000	256,000
10.04.2016				5,000	16	80,000	11,000	176,000
20.04.2016	10,000	17	170,000				21,000	346,000
15.04.2016	37,000	15	555,000				58,000	901,000
25.04.2016				30,000	15.53	465,900	28,000	435,100
10.06.2016	41,000	18	738,000				69,000	1,173,100
29.06.2016				8,000	17	136,000	<b>61,000</b>	<b>1,037,100</b>

(05 marks)

***End of Section A***

Three (03) compulsory questions  
(Total 30 marks)

***Suggested Answers to Question No. 05***

Spiritual Trading PLC  
Statement of Cash Flows (Operating Activities Only)  
For the year ended 31<sup>st</sup> March 2016.

<b>Cash flows from operating activities</b>		
Net profit before taxation		<b>1,850,000</b>
<b>Adjustment For</b>		
Depreciation	300,000	
Disposal Loss	50,000	
Interest Expenses	200,000	
Provision for gratuity	450,000	1,000,000
<b>Operating profit before working capital changes</b>		<b>2,850,000</b>
Increase in Inventories	(3,400,000)	
Decrease in Trade Receivables	520,000	
Increase in Trade Payables	1,330,000	(1,550,000)
<b>Cash generated from operating activities</b>		<b>1,300,000</b>
Interest Paid	(70,000)	
Taxes Paid	(180,000)	(250,000)
<b>Net cash flows from operating activities</b>		<b>1,050,000</b>

**Workings**

**Income Tax**

Cash	180,000	B/B/F	300,000
B/C/F	570,000	P and L	450,000
	<b>750,000</b>		<b>750,000</b>

**Interest**

Cash	70,000	B/B/F	120,000
B/C/F	250,000	P and L	200,000
	<b>320,000</b>		<b>320,000</b>

(10 marks)

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### *Suggested Answers to Question No. 06*

1. **Gross Profit Ratio** =  $\text{Gross Profit} / \text{Sales} * 100$   $4,100/14,500 * 100$   
= **28.28%**
  
2. **Quick Assets Ratio** =  $\text{Current Assets} - \text{Inventories} : \text{Current Liabilities}$   
 $6,550 - 2,000 : 2,900$   
= **1.57 : 1**
  
3. **Current Ratio** =  $\text{Current Assets} : \text{Current Liabilities}$   
 $6,550 : 2,900$   
= **2.26 : 1**
  
4. **Stock Residency Period** =  $\text{Average Stock} / \text{Credit Sales} * 365$   
 $((2,000+2,100)/2) / 10,400 * 365$   
= **72 Days**
  - As an alternative, closing stock can be taken as a numerator for the calculation of the ratio, then the ratio will be 50.3 or 51 days
  
5. **Earnings per Share** =  $\frac{\text{Profit After Tax (Attributable to Share Holders)}}{\text{Weighted Avg. Number of Shares}}$   
=  $2,450/1500$   
= **1.633 Per Share**
  
6. **Return on Capital Employed (ROCE)** =  $\text{Profit before interest \& tax} / \text{Capital Employed} * 100$   
 $(2,450 / 6,700) * 100$   
= **36.56%**

*(10 marks)*

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## ***Suggested Answers to Question No. 07***

(a)

### **Extract of Statement of Financial Position**

<b><u>Non-Current Assets</u></b>		
Leased Assets – Motor Vehicle	8,500,000	
Acc. Depreciation	(1,062,500)	
Carrying Value		<b>7,437,500</b>
<b><u>Lease Creditors – Liability</u></b>		
Balance as at the Beginning		
Facility obtain during the year	5,100,000	
Repaid during the year	(646,640)	
Deposit in advance	(536,000)	
Balance as at the End		<b>3,917,360</b>
Current Portion of Lease Liability		<b>750,102.40</b>
Non-Current Portion of Lease Liability		<b>3,167,257.60</b>

Lease assets are depreciation over the 8 years, as similar to PPE (The owner is transferred)

### **Income Statement**

Depreciation of PPE Leased Assets		1,062,500
Interest expenses		730,240

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**Lease amortization schedule**

Years	Opening Bal.	Interest	Instalment	Closing Balance
1	4,564,000.00	730,240.00	(1,376,880.00)	3,917,360.00
2	3,917,360.00	626,777.60	(1,376,880.00)	3,167,257.60
3	3,167,257.60	506,761.22	(1,376,880.00)	2,297,138.82
4	2,297,138.82	367,542.21	(1,376,880.00)	1,287,801.03
5	1,287,801.03	206,048.16	(1,376,880.00)	116,969.19

- In the year one 536,000.00 was deducted from 5,100,000.00

*(06 marks)*

(b)

As per LKAS 08, changes in useful lives of assets are considered as changes in accounting estimates. The changes in estimates are accounted prospectively, that is for the current year and for the future years.

*(04 marks)*

*(Total 10 marks)*

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*End of Section B*

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

*Suggested Answers to Question No. 08*

(a) **Suhada Holdings PLC**

**Statement of Comprehensive Income**

**For the Year Ended 31<sup>st</sup> March 2016**

Description	Note	Amount	RS.'000
			Amount
Sales			77,200
Cost of Sales			(52,748)
Gross Profit			24,452
Other Income	01		1,240
			<b>25,692</b>
Selling Expenses		(7,225)	
Admin Expenses		(7,542)	
Other Expenses		(100)	
Finance Expenses	02	(958.8)	(15,825.80)
Profit before taxation	03		9,866.20
Taxation	04		(330)
Profit after taxation			9,536.20
Other Comprehensive Income			
Revaluation of Land			1500
<b>Total comprehensive income</b>			<b>11,036.20</b>

(10 marks)

(b) **Suhada Holdings PLC**  
**Statement of Financial Position**  
**As At 31<sup>st</sup> March 2016**

**RS. '000**

Description	Note	Amount	Amount
<b>Assets</b>			
<b>Non-Current Assets</b>			
Property Plant & Equipment	05	18,195	
Capital Work In Progress		3,051.20	21,246.20
<b>Current Assets</b>			
Inventories		15,040	
Trade Receivables		6,350	
Prepayment		510	
Short Term Investment		360	
Cash at Bank		390	
Cash in Hand		20	22,670
<b>Total Asset</b>			<b>43,916.20</b>
<b>Equity and Liabilities</b>			
Stated Capital	06	6,000	
Revaluation Reserve		1,500	
Retained Earnings		16,434.20	
<b>Total Equity</b>			<b>23,934.20</b>
<b>Non-Current Liabilities</b>			
Term Loan		4,000	4,000
<b>Current Liabilities</b>			
Trade Payable		3,400	
Other Short Term Loan		11,000	
Accruals		1,102	
Tax Payable		480	15,982
<b>Total Equity &amp; Liabilities</b>			<b>43,916.20</b>

(08 marks)

(c) **Suhada Holdings PLC**  
**Statement of Changes in Equity**  
**For the Year Ended 31<sup>st</sup> March 2016**

**RS. '000**

Description	Stated Capital	Revaluation	Retained Earnings
Balance As At the Beginning	6,000		7,898
Total comprehensive Income		1,500	9,536.20
Dividends			(1,000)
<b>Total</b>	<b>6,000</b>	<b>1,500</b>	<b>16,434.20</b>

(03 marks)

(d) **Note - 05 PPE**

Description	Cost				RS. '000
	Land	Buildings	Motor Vehicles	Furniture & Fittings	Total
Balance As At the Beginning	3,500	15,000	7,500	4,400	30,400
Revaluation	1,500				1,500
Disposal Of MV			(3,500)		(3,500)
<b>Total</b>	<b>5,000</b>	<b>15,000</b>	<b>4,000</b>	<b>4,400</b>	<b>28,400</b>
<b>Acc. Depreciation</b>					
Balance As At the Beginning		2,600	3,500	2,550	8,650
Charges for the Year		750	1,325	880	2,955
Removal for Disposal			(1,400)		(1,400)
<b>Total</b>	<b>-</b>	<b>3,350</b>	<b>3,425</b>	<b>3,430</b>	<b>10,205</b>
<b>Carrying Value 31st March 2016</b>	<b>5,000</b>	<b>11,650</b>	<b>575</b>	<b>970</b>	<b>18,195</b>

(04 marks)

(Total 25 marks)

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<b>Note 01 – Other Income</b>		<b>(Rs. '000)</b>
Reported form TB	=	2,740
Revaluation	=	(1,500)
<b>To PL</b>	=	<u><u>1,240</u></u>

<b>Note 02 – Finance Expense</b>		
Term Loan Interest (5,000*12*1/12)	=	50
Other Loan Interest	=	960
Adjustment for borrowing Cost	=	(51.2)
<b>To PL</b>	=	<u><u>958.80</u></u>

**Note 03 – Profit before taxation**

The profit before tax is computed after charging following

Director remuneration	=	1,000
Audit fee	=	500
Depreciation	=	2,955
Bad Debts	=	500

**Note 04 – Taxation**

Current year tax	=	480
Over Provision	=	(150)
<b>To PL</b>	=	<u><u>330</u></u>

**Note 06 – Stated Capital**

600,000 Number of Stated Capital at Rs.10 Each = 6,000,000

**Note 07- Dividends**

Company has declared a dividend of Rs.2.50 per share at the meeting held on 15th May 2016, which cumulated to Rs. 1,500,000.00. As per LKAS 10, such was not recognized as liabilities in the financial statements.

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**Working 01 – Expenses Schedules**

Description	RS.'000		
	Selling Exp.	Admin Exp.	Other Exp.
Disposal Loss			100
Depreciation	1,325	1,630	
Membership fee		170	
Bad Debts	500		
Electricity		68	
Telephone		24	
From TB	5,400	4,150	
Director Fee		1,000	
Audit Fee		500	
<b>Total</b>	<b>7,225</b>	<b>7,542</b>	<b>100</b>

**Working 02 – Borrowing Cost**

$$\begin{aligned} \text{Capitalization Rate} &= \frac{800,000+160,000}{10,000,000} \\ &= \underline{\underline{9.6\%}} \end{aligned}$$

$$\text{Amounts Capitalized} = (1,700*9.6\%*3/12) + (1,300*9.6\%*1/12) = 51.2$$

$$\begin{aligned} \text{Charged to PL} &= 960-51.2 \\ &= \underline{\underline{908.8}} \end{aligned}$$

**Working 03 - Disposal Profit or Loss**

Motor Vehicles	3,500.00
Less Depreciation	(1,400.00)
Net Book Value	2,100.00
Sales Proceed	2,000.00
Loss on Disposal	100.00

## Suggested Answers to Question No. 09

(a) (I)

### Goodwill calculation

Investment by Parent	=	100,000
Fair value of NCI	=	50,000
<b>Total</b>	=	<b>150,000</b>
Less - net assets at the date of acquisition		
Stated Capital Sub	=	100,000
General Reserve	=	5,000
Retained Earnings	=	40,000
<b>Total</b>	=	<b>145,000</b>
<b>Goodwill</b>	=	<b><u>5,000</u></b>

(II) KDL group

### Consolidated Statement of Financial Statements

As At 31<sup>st</sup> March 2016

		RS.'000
Property, Plant and Equipment (95000+19500-120+200-80-50+20)		114,470
Goodwill		5,000
<b>Current Assets</b>		
Inventories (10000+10000-1000)	19,000	
Trade Receivables (210000+212000-2000)	420,000	
Short Term Investment	35,000	
Cash (5700+1450+1500)	8650	482,650
<b>Total Assets</b>		<b>602,120</b>
<b>Capital &amp; Liabilities</b>		
Stated Capital	200,000	
General Reserve	21,500	
Retained Earnings (W 2)	135,540	
Parent's Equity		357,040
Non-Controlling Interest (W 1)		59,580
<b>Total Equity</b>		<b>416,620</b>
Current Liabilities (112000 + 74000 - 2000 + 1500)		185,500
<b>Total Equity and Liabilities</b>		<b>602,120</b>

(21 marks)

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## Workings

### 1. Non- controlling interest

Fair value as at the date of acquisition	=	50,000
Share of post profit (21,450 *40%)	=	8,580
Share of General Reserve	=	1,000
<b>Total</b>	=	<b><u>59,580</u></b>

### 2. Consolidated Retained Earnings

Reported Parent's Profit	=	123,700
Subsidiary share of profit (21,450 x 60%)	=	12,870
Over depreciation	=	20
Profit on disposal	=	80
URP on Disposal of PPE (200-120)	=	(80)
URP on Inventories [(5,000 / 125) x 25]	=	(1,000)
Depreciation	=	(50)
<b>Total</b>	=	<b><u>135,540</u></b>

(b)

1. By notice in writing require a specified business enterprise or its auditors to furnish to the board or to a person authorized by the board, within such time, as shall be specified in the notice, any information pertaining to its financial statements and it shall be the duty of such specified business enterprise or its auditors, as the case may be to comply with such requirement within the time specified in the notice.
2. Summon and question any director, officer or auditor of any specified business enterprise on any matter pertaining to the preparation or presentation of its financial statements.
3. Carry out such investigation or hold such inquiries as it may be notice in writing consider necessary or expedient for the performance of its duties under this Act, and for such purpose may summon and call upon any director, office or auditor of any specified business enterprise to appear before it at any such investigation or inquiry or to produce any such books or documents in the possession or control of such director, officer or auditor as are required for the purpose of such investigation or inquiry.

*(04 marks)*

*(Total 25 marks)*

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*End of Section C*

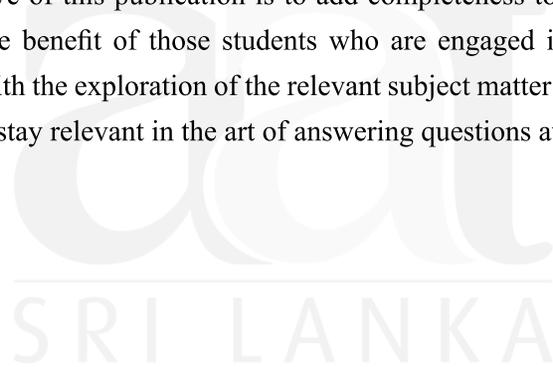
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These should be understood as Suggested Answers to question set at AAT Examinations and should not be construed as the “Only” answers, or, for that matter even as “Model Answers”.

The fundamental objective of this publication is to add completeness to its series of study texts, designs especially for the benefit of those students who are engaged in self-studies. These are intended to assist them with the exploration of the relevant subject matter and further enhance their understanding as well as stay relevant in the art of answering questions at examination level.



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