THE INSTITUTE OF CHARTERED ACCOUNTANTS OF SRI LANKA

Business Level

BL-25-1 Fundamentals of Financial Reporting

Pilot Paper

Instructions to candidates

1) *Time Allowed 02 Hours*
2) *Total 100 marks*
3) *50 Questions. All Questions are compulsory*
4) *All answers should be in ONE Language and the medium applied for*

Section A: Introduction to Financial Accounting (5 Questions)

01. Which of the following best describes the primary purpose of financial reporting?

A) To monitor government taxation policies
B) To provide information useful for decision-making by external users
C) To record only cash transactions of the business
D) To safeguard company assets

02. A company is planning to obtain long-term financing and presents its financial statements to several stakeholders. Which of the following users would be primarily concerned with assessing the company's solvency, gearing, and ability to meet long-term debt obligations?

A) Existing equity shareholders evaluating dividend growth potential
B) Long-term lenders assessing credit risk and repayment capacity
C) Employees reviewing job security and future wage negotiations
D) Customers assessing product quality and the reliability of supply

03. The qualitative characteristic of financial information that requires information to be free from error and bias is:

A) Relevance
B) Comparability
C) Faithful representation
D) Verifiability

04. Under the Companies Act No. 07 of 2007 (Sri Lanka), which of the following is a formal responsibility of company directors in relation to the preparation of financial statements?

A) Directors are required to outsource the preparation of financial statements to a certified public accountant
B) Directors must guarantee that the financial statements report positive profits each year
C) Directors are required to formally acknowledge responsibility for the accuracy and legal compliance of the financial statements by signing an official declaration
D) Directors must submit quarterly financial statements to the Sri Lanka Accounting and Auditing Standards Monitoring Board

05. State True or False.

"An entity shall prepare its complete set of financial statements using the accrual basis of accounting." Is this Statement true/false?

True ☐
False ☐

Section B: Understanding the Accounting Process (13 Questions)

06. Bank reconciliation prepared by Aruna as of 30th June 2025 is given below.

Balance as per the cash book	18,700
+ Unpresented cheques	2,100
	20,800
(-) Unrealized deposits	(3,400)
Balance as per the bank statement	17,400

A summary of the Bank statement for the month of July 2025 is given below.

Description	Dr.	Cr.	Balance (Rs.)
Balance			17,400
Deposits		21,400	
Payments	19,700		
Dividend		1,200	
Bank Charges	100		
Standing orders	200		
Balance			20,000

Additional Information

- A Rs. 1,800 Unpresented cheque in June has been presented and paid in July. All unrealised deposits were realised in July.
- A cheque of Rs. 2,400 issued in July is still not presented for the payments.
- Deposit made in July, Rs. 1,750, is still unrealised.

Select the correct observation:

A) Unpresented cheque amount in July reconciliation Rs. 2,700
B) Unrealised cheque amount in July reconciliation Rs. 2,700
C) Unpresented cheque amount in the July reconciliation, Rs. 1,750
D) Unrealised cheque amount in July reconciliation Rs. 1,750

07. A sole trader commenced business on 1 January 2025 with capital of Rs. 250,000 in cash. During the year, the following transactions took place.
    - Purchased equipment for Rs. 100,000 on credit.
    - Bought goods cost Rs. 200,000, of which 80% were sold for Rs. 300,000 in cash.
    - Paid Rs. 30,000 towards the amount due for equipment.
    - Owner withdrew Rs. 20,000 in cash for personal use.

    Calculate the **closing capital (equity)** as at 31 December 2025.
    Enter your final answer as a single whole number (only digits, without commas, decimals, or text)

08. After computing your company's profit for the year ended 31st March 2025, you discovered the following.
    - A fixed asset costing Rs. 50,000 has been included in the purchase account.
    - Stationery costing Rs. 10,000 has been included as closing stock of raw materials, instead of the stock of stationery.

    These two errors have the effect of;
    A) Understating gross profit by Rs. 40,000
    B) Understating both gross profit and net profit by Rs. 45,000
    C) Understating gross profit by Rs. 60,000 and understating net profit by Rs. 50,000
    D) Overstating both gross profit and net profit by Rs. 60,000

09. ABC Company had a prepaid electricity balance of Rs. 5,000 as at 1 January 2024. An electricity bill amounting to Rs. 45,000, relating to electricity consumed in December 2024, was received in January 2025 and remained unpaid at the reporting date. Explain how this transaction should be recognised and presented in the financial statements for the year ended 31 December 2024.

    A) Recognise the electricity expense of Rs. 40,000 and carry forward a prepaid expense of Rs. 5,000.
    B) Recognise the electricity expense of Rs. 45,000 and a liability (accrued expense) of Rs. 45,000.
    C) Recognise the electricity expense of Rs. 50,000 and eliminate the prepaid balance.
    D) Recognise no expense and treat the entire amount as a prepaid expense.

10. A company's trial balance does not agree, showing a debit total of Rs. 540,000 and a credit total of Rs. 530,000. Until the error is located, how should this difference be treated in the accounting records?

    A) Write off the difference directly to the income statement
    B) Transfer the difference to capital as an adjusting entry
    C) Open a suspense account to record the difference temporarily
    D) Ignore the difference and proceed to prepare financial statements

11. A business failed to record a credit purchase of Rs. 25,000 in both the purchase account and the supplier's personal account. When preparing the trial balance, how will this error affect the agreement of the trial balance?

    A) The trial balance will still agree because double-entry was omitted
    B) The trial balance will show a credit excess of Rs. 25,000
    C) The trial balance will show a debit excess of Rs. 25,000
    D) The trial balance will be impossible to prepare

12. A business purchased inventory costing Rs. 50,000 on credit. However, the accountant incorrectly debited the Equipment Account and credited the Bank Account. To correct this error, state the correct accounts and amounts.

    Debit [ ] Rs. [ ]

    Credit [ ] Rs. [ ]

    (Purchases Account/Equipment Account/Trade Payables Account) (50,000/100,000)

13. The following balances were extracted from a business as at 31st March 2025.

    Cash Rs. 80,000
    Accounts Receivable Rs. 40,000
    Inventory Rs. 60,000
    Accounts Payable Rs. 30,000
    Bank Loan Rs. 50,000.

    Additional information:

    - Expenses of Rs. 10,000 have been incurred but not yet paid.
    - The owner has withdrawn Rs. 20,000 in cash during the period.
    - Depreciation of Rs. 5,000 has not yet been recorded.

Prepare the adjusted accounting equation by filling in the blanks.

Asset = Liabilities + Equity

[ ] = [ ] + [ ]

14. A suspense account was opened due to the following errors.
    - A gas bill of Rs. 420,000 had been recorded in the gas account as Rs. 240,000.
    - A discount of Rs. 50,000 given to a customer had been credited to the discount received.
    - Interest received of Rs. 70,000 had been entered in the bank account only.

    What was the original balance of the suspense account?
    A) Rs.130,000 (Dr)
    B) Rs. 210,000 (Dr)
    C) Rs. 160,000 (Cr)
    D) Rs. 280,000 (Cr)

15. State True or False.

    When preparing a bank reconciliation statement, dishonoured cheques that were previously recorded as receipts in the cash book must be deducted from the bank statement balance if the reconciliation starts with the cash book balance.

    True ☐
    False ☐

16. Match each type of accounting error with its explanation.

Error of Principle	Trial balance will not balance
Error of Omission	Wrong account classification, amounts correct
Transposition Error	Complete transaction missing from records

17. ABC Ltd sold goods on credit with a list price of Rs. 200,000. A trade discount of 15% was allowed, and the customer was offered a cash discount of 5% if payment was made within 14 days. The customer paid within the discount period.

    The amounts to be recorded in the sales and discounts allowed accounts are:
    A) Sales: Rs. 200,000; Discount Allowed: Rs. 10,000
    B) Sales: Rs. 170,000; Discount Allowed: Rs. 0
    C) Sales: Rs. 170,000; Discount Allowed: Rs. 8,500
    D) Sales: Rs. 161,500; Discount Allowed: Rs. 8,500

18. Match each financial statement component with its primary purpose.

Statement of Financial Position	Shows performance and profitability over a period
Statement of Profit or Loss	Tracks cash movements across different activities
Statement of Cash Flows	Shows financial position at a specific point in time

Section C: Single Entity Financial Statements (7 Questions)

19. Which situation best illustrates the application of the business entity concept in Accounting?
    A) A business pays the personal electricity bill of the owner
    B) The owner records household grocery expenses as business expenses
    C) The owner withdraws cash for personal use, and it is recorded as drawings
    D) The business records profit at the end of the year

20. Which statement correctly describes the relationship between profit and cash flow?
    A) Profit and cash flow are always identical
    B) Profit measures performance, while cash flow measures liquidity
    C) Cash flow is calculated from profit before tax only
    D) Profit is irrelevant when preparing financial statements

21. Which of the following items represents a transaction or event that is appropriately presented within the Statement of Changes in Equity?

    A) Total revenue recognised during the period
    B) Share capital issued as part of equity transactions with owners
    C) Trade payables outstanding at year-end
    D) Cash at bank held for liquidity purposes

22. From the following information, calculate the Gross Profit.
    - The Cost of Sales is Rs. 320,000.
    - The company's Gross Profit Ratio is 20% on the selling price.

    Based on this information, determine the Gross Profit. [ ]

23. A company's opening equity was Rs. 400,000. During the year, it issued new shares worth Rs. 100,000 and declared dividends of Rs. 40,000. The net profit for the year was Rs. 120,000.

    Calculate the closing equity. ☐

24. State whether the following statement is TRUE or FALSE with reference to LKAS 07:

    'Cash equivalents are short-term, highly liquid investments that are readily convertible to known amounts of cash and which are subject to a significant risk of changes in value."

    True ☐
    False ☐

25. Gain or loss arising from the 1st time revaluation of land and buildings under LKAS 16 is recognized in the statement of comprehensive income under _____. *(Profit and Loss / Other Comprehensive Income/ Retained Earnings/ Statement of Financial Position).*

Section D: Application of Basic Accounting Standards (13 Questions)

26. The year-end is 30th June 2025, and the accounts are approved on 18th August 2025.

    1. Sales of year-end inventory on 2nd July 2025 at less than cost.
    2. The issue of new ordinary shares on 4th July 2025.
    3. A fire in the main warehouse occurred on 8th July 2025. A part of the building was destroyed.
    4. A major credit customer was declared bankrupt on 10th July 2025.
    5. All of the share capital of a competitor, 'Teeny Co' was acquired on 21st July 2025.
    6. On 1st August 2025, Rs. 500,000 was received in respect of an insurance claim dated 13th February 2025.

Which of the above are adjusting events for the ABC company?

A) 1,4 and 6
B) 1,2,4 and 6
C) 1,2,5 and 6
D) 1,4,5 and 6

27. The costs of inventories in line with LKAS 2 consist of
    A) Purchase price net of any discounts and rebates, transport costs, costs of conversion and storage costs.
    B) Costs of purchase, directly attributable overheads, storage costs, transport costs and other costs to bring the inventories to their present location and condition.
    C) Costs of purchase, costs of conversion and other costs to bring the inventories to their present location and condition.
    D) Costs of purchase, costs directly attributable to inventories and costs of conversion.

28. Nishantha owns a canned fish factory. The premises were purchased on 01st January 2019 for Rs. 450,000, and depreciation is charged at 2% pa on a straight-line basis. Nishantha now wishes to revalue the factory premises to Rs . 800,000 on 01st January 2025 to reflect the market value. What is the balance on the revaluation surplus after accounting for this transaction?

29. Straight-line depreciation is grounded in which fundamental assumption regarding the pattern in which an asset's economic benefits are consumed over its useful life?

    A) The asset's value decreases more in the earlier years
    B) The asset's value decreases evenly over its useful life
    C) The asset is revalued every year
    D) The residual value is ignored

30. ABC company receives a consideration of Rs. 1,000,000 for a construction contract. However, when the company assessed the revenue recognition of this consideration based on SLFRS 15 five-step model, it was noted that this contract does not meet the criteria in the five-step model. ABC company can recognise Rs. 1,000,000 as revenue only when which of the following situations?

    A) The entity has no remaining obligations to transfer goods or services to the customer, and all, or substantially all, of the consideration promised by the customer has been received by the entity and is non-refundable
    B) The contract has been terminated, and the consideration received from the customer is refundable.
    C) Both A and B are applicable
    D) Both A and B are not applicable

31. ABC Limited purchased a piece of land on 31st October 2016 for Rs. 500,000. The land was revalued for Rs. 700,000 on 31st October 2020. The latest valuation report dated 31st October 2024 values the land at Rs. 450,000. The land balance has been adjusted as of 31st October 2024 to reflect this. Which one of the following shows the correct debit entry in ABC's financial statements for the year ended 31st March 2025?

    A) Dr Revaluation Reserves Rs. 50,000
       Dr Statement of Comprehensive Income Rs. 200,000
    B) Dr Revaluation Reserves Rs. 250,000
    C) Dr Revaluation Reserves Rs. 200,000
       Dr Statement of Comprehensive Income Rs. 50,000
    D) Dr Statement of Comprehensive Income Rs. 250,000

32. On 1 January 2025, ABC Ltd purchased property consisting of land and a building for a total cost of Rs. 5,000,000. The land accounts for 40% of the total cost. The building has a residual value of Rs. 500,000 and a useful life of 10 years. The building's economic life is 20 years. The company depreciates property, plant, and equipment on a straight-line basis. Calculate the annual depreciation charge that should be recognised in the statement of profit or loss for the year ended 31 December 2025.

33. At the year-end, XYZ company has the following items of inventory. Their costs and NRVs are as follows.

Item type	Cost	NRV	No of Items
A	50	40	1000
B	65	70	1000
C	30	20	1000
D	45	55	1000
Total	**190**	**185**	

What is the amount to be disclosed for inventories in year-end statement of financial position?

34. State True or False.

'A company has a contingent liability estimated at Rs. 200,000 with a 60% probability of payment. According to Sri Lanka Accounting Standards, this should be disclosed.'

True ☐
False ☐

35. According to LKAS 8, how should a change in the estimated useful life of a machine be accounted for?

A) Prospectively, by adjusting the depreciation expense in the current and future periods.
B) Retrospectively, by restating the financial statements of all prior periods presented.
C) By recognising the full impact of the change in the current period's profit or loss.
D) As a prior period error, with a correction to the opening balance of retained earnings

36. Fill in the blanks using the most appropriate term.

As per LKAS 16, depreciation is the systematic allocation of the _____ of an asset over its useful life.

(Cost / Accumulated Depreciation / Depreciable Amount / Recoverable Amount)

37. Match the SLFRS/LKAS Standard with the subject matter.

LKAS 2	Amortization
LKAS 16	Revaluation
LKAS 38	Net Realizable Value
SLFRS 15	Performance Obligation

38. Match each depreciation method with its most suitable application.

Straight-line method	Assets with constant benefits
Reducing balance method	Assets losing more value in early years
Units of production method	Assets whose use varies with output

Section E: Analysis of Financial Statements (5 Questions)

39. Which financial ratio provides the most comprehensive assessment of a company's ability to meet its short-term obligations as they fall due?

    A) Gross Profit Margin
    B) Current Ratio
    C) Return on Equity
    D) Debt-to-Equity Ratio

40. Trend analysis in financial statements is used to:
    A) Compare performance with competitors
    B) Assess performance over several periods
    C) Identify accounting errors
    D) Determine taxation liability

41. A high inventory turnover ratio usually indicates:
    A) Slow-moving stock
    B) Efficient inventory management
    C) Excessive stock levels
    D) Understated purchases

42. XYZ Ltd reported a profit after tax of Rs. 2,500,000 for the year ended 31 December 2025. The company has 500,000 ordinary shares in issue. The current market price of one share is Rs. 25. Calculate the Price-to-Earnings (P/E) ratio for XYZ Ltd.

43. The following are extracts from the statement of financial position of XYZ Ltd as at 31st March 2025.
    - Current Assets: Rs. 600,000
    - Inventory: Rs. 200,000
    - Current Liabilities: Rs. 300,000
    - Total Equity: Rs. 1,000,000
    - Non-current Liabilities: Rs. 500,000

    Calculate the ratios below.

Current Ratio	
Debt-to-Equity Ratio	

Section F: Sustainability Reporting (2 Questions)

44. The main objective of sustainability reporting is to:

    A) Replace financial statements
    B) Provide information on environmental, social, and governance impacts
    C) Focus only on profitability measures
    D) Satisfy only regulatory authorities

45. Match each dimension of sustainability with an appropriate example disclosure.

Environmental	Carbon emissions
Social	Board diversity
Governance	Employee training hours

Section G: Digitalisation of Accounting Process (5 Questions)

46. Which of the following is not a feature of computerised accounting systems?
    A) Automation of entries
    B) Cloud storage integration
    C) Unlimited manual reconciliation
    D) Real-time reporting

47. AI-driven tools in digital accounting are primarily used for:

A) Increasing physical documentation
B) Identifying and preventing common errors
C) Eliminating the need for disclosure notes
D) Replacing all human accountants

48. Fill in the blanks using the most appropriate term.

State the *dashboard design principle* ensures a clear visual hierarchy with the most important metrics prominently displayed. _____. *(Clarity, Relevance, Timeliness, Actionability).*

49. State True or False.

'Automated accounting systems can completely eliminate the possibility of accounting errors.'

True ☐
False ☐

50. Match each digital tool/feature with its primary benefit in accounting.

Cloud Accounting	Analyses large datasets to identify complex Patterns
AI-based Audit Tools	Centralized integration of business processes
Artificial Intelligence	Real-time remote access to records
ERP Systems	Automated anomaly/error detection to records

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