Test Series: March, 2012

MOCK TEST PAPER – 2

IPCC: GROUP – II

PAPER – 5 : ADVANCED ACCOUNTING

Question No. 1 is compulsory.

*Answer any **five** questions from the remaining **six** questions.*

Working notes should form part of the answer.

Time Allowed – 3 Hours | Maximum Marks – 100

1. (a) At the end of the financial year ending on 31st December, 2011, a company finds that there are twenty law suits outstanding which have not been settled till the date of approval of accounts by the Board of Directors. The possible outcome as estimated by the Board is as follows:

	Probability	*Loss (₹)*
In respect of five cases (Win)	100%	-
Next ten cases (Win)	60%	-
Lose (Low damages)	30%	1,20,000
Lose (High damages)	10%	2,00,000
Remaining five cases		
Win	50%	-
Lose (Low damages)	30%	1,00,000
Lose (High damages)	20%	2,10,000

Outcome of each case is to be taken as a separate entity. Ascertain the amount of contingent loss and the accounting treatment in respect thereof.

(b) Paras Ltd. had the following borrowings during a year in respect of capital expansion.

Plant	Cost of Asset	Remarks
	₹	
Plant P	100 lakhs	No specific borrowings
Plant Q	125 lakhs	Bank loan of ₹ 65 lakhs at 10%
Plant R	175 lakhs	9% Debentures of ₹ 125 lakhs were issued.

In addition to the specific borrowings stated above, the Company had obtained term loans from two banks (1) ₹ 100 lakhs at 10% from Corporation Bank and (2) ₹ 110 lakhs at 11.50% from State Bank of India, to meet its capital expansion requirements. Determine the amount of borrowing costs to be capitalized in each of the above Plants, as per AS-16.

(c) Bharat Ltd. grants 1,000 employees stock options on 1.4.2008 at ₹ 40, when the market price is ₹ 160. The vesting period is 2½ years and the maximum exercise period is one year. 300 unvested options lapse on 1.5.2010. 600 options are exercised on 30.6.2011. 100 vested options lapse at the end of the exercise period.

Pass Journal Entries giving suitable narrations.

(d) A limited company created a provision for bad and doubtful debts at 2.5% on debtors in preparing the financial statements for the year 2011-12.

Subsequently on a review of the credit period allowed and financial capacity of the customers, the company decided to increase the provision to 8% on debtors as on 31.3.2012. The accounts were not approved by the Board of Directors till the date of decision. While applying the relevant accounting standard can this revision be considered as an extraordinary item or prior period item? *(5 Marks each)*

2. 'S' and 'T' were carrying on business as equal partners. Their Balance Sheet as on 31st March, 2011 stood as follows:

Liabilities		₹	Assets	₹
Capital accounts:			Stock	2,70,000
S	6,40,000		Debtors	3,65,000
T	6,60,000	13,00,000	Furniture	75,000
Creditors		3,27,500	Joint life policy	47,500
Bank overdraft		1,50,000	Plant	1,72,500
Bills payable		62,500	Building	9,10,000
		18,40,000		18,40,000

The operations of the business were carried on till 30th September, 2011. S and T both withdrew in equal amounts, half the amount of profits made during the current period of 6 months after 10% per annum had been written off on building and plant and 5% per annum written off on furniture. During the current period of 6 months, creditors were reduced by ₹ 50,000, Bills payable by ₹ 11,500 and Bank overdraft by ₹ 75,000. The Joint Life policy was surrendered for ₹ 47,500 on 30th September, 2011. Stock was valued at ₹ 3,17,000 and debtors at ₹ 3,25,000 on 30th September, 2011. The other items remained the same as on 31st March, 2011.

On 30th September, 2011 the firm sold its business to ST Ltd. The value of goodwill was estimated at ₹ 5,40,000 and the remaining assets were valued on the basis of the Balance Sheet as on 30th September, 2011. The ST Ltd. paid the purchase consideration in equity shares of ₹ 10 each. You are required to prepare a Realization Account and Capital accounts of the partners. *(16 Marks)*

3. Success Ltd. issued ₹ 10,00,000, 6% Debenture Stock at par on 21.1.2002. Interest was payable on 30th June and 31st December, in each year.

   Under the terms of the Debentures Trust the owned stock is redeemable at par. The trust deed obliges the Company to pay to the trustees on 31st December, 2009 and annually thereafter the sum of ₹ 1,00,000 to be utilized for the redemption and cancellation of an equivalent amount of stock, which is to be selected by drawing lots.

   Alternatively, the Company is empowered as from 1st January, 2009 to purchase its own debentures from the open market. These Debentures must be surrendered to the Trustees for cancellation and any adjustments for accrued interest recorded in the books of account. If in any year the nominal amount of the stock surrendered under this alternative does not amount to ₹ 1,00,000 then the shortfall is to be paid by the Company to the Trustees in cash on 31st December.

   The following purchases of stock were made by the Company:

	Nominal value of stock purchased ₹	Purchase price per ₹ 100 of stock ₹
(1) 30th September, 2009	1,20,000	98
(2) 31st May, 2010	75,000	95 (Ex-interest)
(3) 31st July, 2011	1,15,000	92

   The Company fulfilled all its obligations under the trust deed.

   Prepare the Ledger Accounts : (a) Debenture Stock A/c (b) Debenture Redemption A/c (c) Debenture Interest A/c.

   Note: Ignore costs and taxation *(16 Marks)*

4. Prepare Revenue Account in proper form for the year ended 31st March, 2012, from the following particulars related to Saviour General Insurance Co. for the year ended 2011-12:

	Related to Direct business (₹)	Related to Reinsurance (₹)
Premiums:		
Amount received	30,00,000	2,40,000

Receivable at the beginning	1,80,000	24,000
Receivable at the end	2,40,000	36,000
Amount paid	--	3,60,000
Payable at the beginning	--	30,000
Payable at the end	--	42,000
Claims:		
Amount paid	18,00,000	1,80,000
Payable at the beginning	60,000	12,000
Payable at the end	1,20,000	18,000
Amount recovered	--	1,20,000
Receivable at the beginning	--	18,000
Receivable at the end	--	12,000
Commission:		
Amount paid	72,000	10,800
Amount received	--	14,400

Additional information:

(i) Interest, dividend and rent received 30,000

Income-tax in respect of above 6,000

(ii) Management expenses including ₹ 12,000 related to legal expenses regarding claims 1,32,000.

(iii) Provision for income tax existing at the beginning of the year was ₹ 1,95,000, the income-tax actually paid during the year ₹ 1,68,000 and the provision necessary at the year end ₹ 2,07,000.

(iv) The net premium income of the company during the year 2010-2011 was ₹ 24,00,000 on which reserve for unexpired risk @ 50% and additional reserve @ 7 ½ % was created. This year, the balance to be carried forward is 50% of net premium on reserve for unexpired risk and 5% on additional reserve. *(16 Marks)*

5. (a) Here and There and Co. of Mumbai started a branch at Bangalore on 1.4.2011 to which goods were sent at 20% above cost. The branch makes both cash sales and credit sales. Branch expenses are met from branch cash and balance money remitted to H.O. The branch does not maintain double entry books of account and necessary accounts relating to branch are maintained in H.O. Following further details are given for the year ending on 31.3.2012:

	₹
Cost of goods sent to branch	1,00,000
Goods received by branch till 31.3.2012 at Invoice price	1,08,000
Credit sales for the year	1,16,000
Closing debtors on 31.3.2012	41,600
Bad debts written off during the year	400
Cash remitted to H.O.	86,000
Closing cash on hand at branch on 31.3.2012	4,000
Cash remitted by H.O. to branch during the year	6,000
Closing stock in hand at branch at invoice price	12,000
Expenses incurred at branch	24,000

Draw up the necessary Ledger Accounts like Branch Debtors Account, Branch Stock Account, Goods sent to Branch Account, Branch Cash Account, Branch Expenses Account and Branch Adjustment Account for ascertaining gross profit and Branch Profit and Loss Account for ascertaining Branch profit. *(8 Marks)*

(b) A joint stock company resolved to issue 10 lakh equity shares of ₹ 10 each at a premium of ₹ 1 per share. One lakh of these shares were taken up by the directors of the company, their relatives, associates and friends, the entire amount being received forthwith. The remaining shares were offered to the public, the entire amount being asked for with applications. The issue was underwritten by X, Y and Z for a commission @ 2% of the issue price. 65% of the issue was underwritten by X, while Y's and Z's shares were 25% and 10% respectively.

The underwriters were to submit unmarked applications for shares underwritten firm with full application money along with members of the general public.

Marked applications were as follows: X - 1,19,500 shares; Y - 57,500 shares and Z – 10,500 shares.

Unmarked applications totalled 7,00,000 shares.

Accounts with the underwriters were promptly settled.

You are required to:

(i) Prepare a statement calculating underwriter's liability for shares.

(ii) Pass journal entries for all transactions including cash transactions. *(8 Marks)*

6. (a) Bright Electricity Company earned a profit of ₹ 1,20,00,000 (after tax) for the year ended 31st March, 2011 on which date it had a capital base of ₹ 8,74,00,000 and the bank rate was 8%. The following additional information about the company is

also provided to you:

	₹
Reserve Fund Investment, invested in 8% Government securities at par	1,20,00,000
Contingencies Reserve Fund Investments @ 7% per annum	50,00,000
Loan from State Electricity Board	1,00,00,000
11% Debentures	8,00,000
Development Reserve	32,00,000

Show how the surplus of the company will be disposed of under the provisions of the Electricity Act. . *(8 Marks)*

(b) The following balances were extracted from the books of M/s Part & Parcel. You are required to prepare Departmental Trading Account and Profit and Loss account for the year ended 31st December, 2011 after adjusting the unrealized department profits if any.

	Deptt. A ₹	Deptt. B ₹
Opening Stock	50,000	40,000
Purchases	6,50,000	9,10,000
Sales	10,00,000	15,00,000

General expenses incurred for both the departments were ₹ 1,25,000 and you are also supplied with the following information: (a) Closing stock of Department A ₹ 1,00,000 including goods from Department B for ₹ 20,000 at cost of Department A. (b) Closing stock of Department B ₹ 2,00,000 including goods from Department A for ₹ 30,000 at cost to Department B. (c) Opening stock of Department A and Department B include goods of the value of ₹ 10,000 and ₹ 15,000 taken form Department B and Department A respectively at cost to transferee departments. (d) The gross profit is uniform from year to year. *(8 Marks)*

7. Answer any **four** out of five:

(a) From the following information of Honour Bank Limited, compute the provisions to be made in the Profit and Loss account:

	₹ in lakhs
Assets	
Standard	20,000
Substandard	16,000

Doubtful	
For one year (secured)	6,000
For two years and three years (secured)	4,000
For more than three years (secured by mortgage of plant and machinery ₹ 600 lakhs)	2,000
Non-recoverable Assets	1,500

(b) A Limited Company closed its accounting year on 30.6.11 and the accounts for that period were considered and approved by the board of directors on 20th August, 2011. The company was engaged in laying pipe line for an oil company deep beneath the earth. While doing the boring work on 1.9.2011 it had met a rocky surface for which it was estimated that there would be an extra cost to the tune of ₹ 80 lakhs. You are required to state with reasons, how the event would be dealt with in the financial statements for the year ended 30.6.11.

(c) S Ltd. purchased fixed assets costing ₹ 3,000 lakhs on 1.1.2011 and the same was fully financed by foreign currency loan (U.S. Dollars) payable in three annual equal instalments. Exchange rates were 1 Dollar = ₹ 40.00 and ₹ 42.50 as on 1.1.2011 and 31.12.2011 respectively. First instalment was paid on 31.12.2011. The entire difference in foreign exchange has been capitalized.

You are required to state, how these transactions would be accounted for.

(d) Should appropriation to mandatory reserves be excluded from net profit attributable to equity shareholders?

Kraft Ltd. is engaged in manufacturing industrial packaging equipment. As per the terms of an agreement entered into with its debentureholders, the company is required to appropriate adequate portion of its profits to a specific reserve over the period of maturity of the debentures such that, at the redemption date, the Reserve constitutes at least half the value of such debentures. As such, appropriations are not available for distribution to the equity shareholders. Kraft Ltd. has excluded this from the numerator in the computation of basis EPS. Is this treatment correct?

(e) Rishi Limited has set up its business in a designated backward area which entitles the company to receive from the Government of India a subsidy of 20% of the cost of investment. Having fulfilled all the conditions under the scheme, the company on its investment of ₹ 50 crore in capital assets, received ₹ 10 crore from the Government in January, 2012 (accounting period being 2011-2012). The company wants to treat this receipt as an item of revenue and thereby reduce the losses on profit and loss account for the year ended 31st March, 2012.

Keeping in view the relevant Accounting Standard, discuss whether this action is justified or not. *(5 Marks each)*