

PAPER – 1 : ADVANCED ACCOUNTING

Answer all questions.

Working notes should form part of the answer.

Question 1

The draft Balance Sheets of 3 Companies as at 31st March, 2007 are as below:

	(In Rs.000's)		
	Morning Ltd.	Evening Ltd.	Night Ltd.
Liabilities			
Share Capital – shares of Rs.100 each	40,000	20,000	10,000
Reserves	1,800	1,000	900
P/L A/c (1.4.06)	1,500	2,000	800
Profit for 2006-07	7,000	3,800	1,800
Loan from Morning Ltd.	—	5,000	—
Creditors	<u>2,500</u>	<u>1,000</u>	<u>1,400</u>
	<u>52,800</u>	<u>32,800</u>	<u>14,900</u>
Assets			
Investments:			
1,60,000 shares in Evening	18,000	—	—
75,000 shares in Night	8,000	—	—
Loan to Evening Ltd.	5,000	—	—
Sundry assets	<u>21,800</u>	<u>32,800</u>	<u>14,900</u>
	<u>52,800</u>	<u>32,800</u>	<u>14,900</u>

Following additional information is also available:

- Dividend is proposed by each company at 10%.
- Stock transferred by Night Ltd. to Evening Ltd. fully paid for was Rs.8 lacs on which the former made a Profit of Rs.3 lacs. On 31st March, 2007, this was in the inventory of the latter.
- Loan referred to is against 8% interest. Neither Morning Ltd. nor Evening Ltd. has considered the interest.
- Reserves as on 1.4.2006 of Evening Ltd. and Night Ltd. were Rs.8,00,000 and Rs.7,50,000 respectively.
- Cash-in-transit from Evening Ltd. to Morning Ltd. was Rs.1,00,000 as on 31.3.2007.
- The shares of the subsidiaries were all acquired by Morning Ltd. on 1st April, 2006.

Prepare consolidated Balance Sheet as on 31st March, 2007. Workings should be part of the answer. (16 Marks)

Answer

Consolidated Balance Sheet of Morning Ltd. with its subsidiaries Evening Ltd. and Night Ltd.

As on 31st March, 2007

				(Rs. in thousand)			
Liabilities	Rs.	Rs.	Rs.	Assets	Rs.	Rs.	Rs.
Share Capital			40,000	Sundry Assets*			
Minority Interest				Morning Ltd.		21,800	
Evening Ltd.		4,880		Evening Ltd.	32,800		
Night Ltd.		<u>3,125</u>	8,005	Less: Unrealized profit	<u>300</u>	32,500	
Capital Reserve [Refer Note 5]			902.5	Night Ltd.		<u>14,900</u>	69,200
General Reserve							
Morning Ltd.		1,800					
Evening Ltd.		160					
Night Ltd.		<u>112.5</u>	2,072.5				
Profit & Loss A/c							
Balance on 1.04.06	1,500						
Profit during 06-07	7,000						
Add: Interest on Loan	<u>400</u>						
	8,900						
Less: Proposed dividend	<u>4,000</u>	4,900					
Add: P & L Account of Evening Ltd.		2,720					
Add: P & L Account of Night Ltd		<u>1,050</u>	8,670				
Creditors							
Morning Ltd.		2,500					
Evening Ltd.		1,000					
Night Ltd		<u>1,400</u>	4,900				

* The total of Sundry Assets of the Group mutually sets off the effect of Cash-in-transit of Rs.1 lac from Evening Ltd. to Morning Ltd. Hence, cash in transit has not been separately shown.

Proposed Dividend

Morning Ltd.	4,000		
Evening Ltd. (Minority)	400		
Night Ltd. (Minority)	<u>250</u>	<u>4,650</u>	
		<u>69,200</u>	<u>69,200</u>

Workings Notes:

- A. Morning Ltd.'s holding in Evening Ltd. is 1,60,000 shares out of 2,00,000 shares, i.e., 4/5th or 80%; Minority holding 1/5th or 20%.
- B. Morning Ltd.'s holding in Night Ltd. is 75,000 shares out of 1,00,000 shares, i.e., 3/4th or 75%; Minority holding 1/4th or 25%.

Analysis of Reserves and Profits of Subsidiary Companies

	Evening Ltd. (Rs.'000)	Night Ltd Rs.('000)	Minority interest in Evening Ltd. (1/5) Rs.('000)	Minority interest in Night Ltd. (1/4) Rs.('000)
1. Capital Reserve (pre-acquisition reserves and profits)				
Reserves on 1.04.2006	800	750		
Profit on 1.04.2006	<u>2,000</u>	<u>800</u>		
	2,800	1,550		
Less: Minority interest	<u>560</u>	<u>387.5</u>	560	387.5
	<u>2,240</u>	<u>1,162.5</u>		
2. General Reserve				
Reserves as per Balance Sheet	1,000	900		
Less: Capital Reserve [See Note A]	<u>800</u>	<u>750</u>		
	200	150		
Less: Minority interest	<u>40</u>	<u>37.5</u>	40	37.5
	<u>160</u>	<u>112.5</u>		
3. Profit and Loss Account				
Profit for the year as per Balance Sheet	3,800	1,800		
Less: Interest on Loan (5,000 x 8%)	<u>400</u>			
	3,400			

Less: Minority Interest	<u>680</u>	<u>450</u>	680	450
	2,720	1,350		
Less: Unrealised profit on stock transfer	<u> </u>	<u>300*</u>		
	<u>2,720</u>	<u>1,050</u>		
4. Share Capital				
As per Balance sheet	20,000	10,000		
Less: Minority interest	<u>4,000</u>	<u>2,500</u>	<u>4,000</u>	<u>2,500</u>
Transferred for computation of Goodwill/Capital Reserve	<u>16,000</u>	<u>7,500</u>	5,280	3,375
Less: Proposed dividend shown separately			<u>400</u>	<u>250</u>
Transferred to Consolidated Balance Sheet			<u>4,880</u>	<u>3,125</u>

5. Computation of Cost of Control i.e. Goodwill / Capital Reserve on consolidation

(Rs. In thousand)

	Evening Ltd.	Night Ltd.
Cost of Investments	18,000	8,000
Less: Paid up value of shares [Refer Note 4]	<u>16,000</u>	<u>7,500</u>
	2,000	500
Less: Capital Reserve [Refer Note 1]	<u>2,240</u>	<u>1,162.5</u>
	<u>-240</u>	<u>-662.5</u>
Total Capital Reserve (Rs.240 + Rs.662.5)	902.5	

Question 2

The Balance Sheets of Strong Ltd. and Weak Ltd. as on 31.03.2007 is as below:

Balance Sheet as on 31.03.2007

Liabilities	Strong Ltd. Rs.	Weak Ltd. Rs.	Assets	Strong Ltd. Rs.	Weak Ltd. Rs.
Equity Share Capital (Rs.100 each)	50,00,000	30,00,000	Fixed Assets other than Goodwill	30,00,000	20,00,000
Reserve	4,00,000	2,00,000	Stock	8,00,000	6,00,000
P/L A/c	6,00,000	4,00,000	Debtors	14,00,000	9,00,000

* As per para 17 of AS 21, 'Unrealised profits resulting from intragroup transactions that are included in the carrying amount of assets, such as inventory and fixed assets, are eliminated in full.

Creditors	5,00,000	3,00,000	Cash & Bank	12,00,000	3,50,000
			Preliminary Expenses	1,00,000	50,000
	<u>65,00,000</u>	<u>39,00,000</u>		<u>65,00,000</u>	<u>39,00,000</u>

Strong Ltd. takes over Weak Ltd. on 01.07.07. No Balance Sheet of Weak Ltd. is available as on that date. It is however estimated that Weak Ltd. earns estimated profit of Rs.2,00,000 after charging proportionate depreciation @ 10% p.a. on fixed assets, during April-June, 2007.

Estimated profit of Strong Ltd. during these 3 months is Rs.4,00,000 after charging proportionate depreciation @ 10% p.a. on fixed assets.

Both the companies have declared and paid 10% dividend within this 3 months' period. Goodwill of Weak Ltd. is valued at Rs.2,00,000 and Fixed Assets are valued at Rs.1,00,000 above the estimated book value. Purchase consideration is to be satisfied by Strong Ltd. by shares at par. Ignore Income-tax.

You are required to calculate the following:

- No. of shares to be issued by Strong Ltd. to Weak Ltd. against purchase consideration;
- Net Current Assets of Strong Ltd. and Weak Ltd. as on 01.07.2007;
- P/L A/c balance of the Strong Ltd. as on 01.07.2007;
- Fixed Assets as on 01.07.2007;
- Balance Sheet of Strong Ltd. as on 01.07.2007 after take over of Weak Ltd. (16 Marks)

Answer

- Number of shares to be issued by Strong Ltd. to Weak Ltd. against purchase consideration

Weak Ltd.	Rs.	Rs.
Goodwill		2,00,000
Fixed Assets	20,00,000	
Less: Depreciation	<u>50,000</u>	
	19,50,000	
Add: Appreciation	<u>1,00,000</u>	20,50,000
Stock		6,00,000
Debtors		9,00,000
Cash and Bank balances	3,50,000	
Add: Profit after depreciation	2,00,000	
Add: Depreciation (non-cash)	<u>50,000</u>	2,50,000

Less: Dividend	<u>(3,00,000)</u>	<u>3,00,000</u>
		40,50,000
Less: Creditors		<u>3,00,000</u>
Purchase Consideration		<u>37,50,000</u>

(ii) Calculation of Net Current Assets as on 01.07.2007

		Strong Ltd. Rs.		Weak Ltd. Rs.
Current assets:				
Stock		8,00,000		6,00,000
Debtors		14,00,000		9,00,000
Cash and Bank	12,00,000		3,50,000	
Less: Dividend	(5,00,000)		(3,00,000)	
Add: Profit before depreciation	<u>4,75,000</u>	<u>11,75,000</u>	<u>2,50,000</u>	<u>3,00,000</u>
		33,75,000		18,00,000
Less: Creditors		<u>5,00,000</u>		<u>3,00,000</u>
		<u>28,75,000</u>		<u>15,00,000</u>

(iii) Profit and Loss Account balance of Strong Ltd. as on 1.07.2007

	Rs.
P & L A/c balance as on 31.03.2007	6,00,000
Less: Dividend paid	<u>5,00,000</u>
	1,00,000
Add: Estimated profit for 3 months after charging depreciation	<u>4,00,000</u>
	<u>5,00,000</u>

(iv) Fixed Assets as on 01.07.2007

Fixed Assets of Strong Ltd. as on 31.03.2007		30,00,000
Less: Depreciation for 3 months		<u>75,000</u>
		29,25,000
Fixed assets taken over of Weak Ltd. as on 31.03.2007	20,00,000	
Less: Proportionate depreciation for 3 months on fixed assets	<u>50,000</u>	
	19,50,000	
Add: Appreciation above the estimated book value	<u>1,00,000</u>	<u>20,50,000</u>
		<u>49,75,000</u>

(v) Balance Sheet of Strong Ltd. as on 01.07.2007 (after Take Over)

Liabilities	Rs.	Assets	Rs.
Equity Share capital: 87500 (50,000+ 37,500) shares of Rs.100 each	87,50,000	Goodwill Fixed assets [as computed in (iv)]	2,00,000 49,75,000
Reserves	4,00,000	Stock	14,00,000
Profit and Loss Account [as computed in (iii)]	5,00,000	(8,00,000 + 6,00,000) Debtors	23,00,000
Creditors (5,00,000 + 3,00,000)	8,00,000	(14,00,000 + 9,00,000) Cash and Bank (11,75,000+ 3,00,000)	14,75,000
		Preliminary expenses	1,00,000
	<u>1,04,50,000</u>		<u>1,04,50,000</u>

Question 3

- (a) Shivaji Ltd. purchased Fixed assets worth Rs.90,00,000 on 1st April, 2002. The life of the assets is 10 years and they are to be depreciated on straight line basis. The assets were revalued on 1st April, 2004 when 50% of the assets was assessed at 10% less than the book value, and the remaining assets were revalued at 15% higher than book value. The assets were ultimately sold on 1.4.2006 for Rs.54,80,000. Excess depreciation on revaluation, if any, should be charged to Revaluation Reserve.

Show Fixed Assets A/c, Depreciation A/c and Revaluation Reserve A/c, supported by Workings wherever necessary.

- (b) The Balance Sheet of Domestic Ltd. as on 31st March, 2007 is as under:

(All figures are in lacs)

Liabilities	Rs.	Assets	Rs.
Equity Shares Rs.10 each	3,000	Goodwill	744
Reserves (including provision for taxation of Rs.300 lacs)	1,000	Premises and Land at cost	400
5% Debentures	2,000	Plant and Machinery	3,000
Secured Loans	200	Motor Vehicles	40
Sundry Creditors	300	(purchased on 1.10.06)	
Profit & Loss A/c		Raw materials at cost	920
Balance from previous B/S	Rs.32	Work-in-progress at cost	130
Profit for the year (After taxation)	<u>Rs.1,100</u>	Finished Goods at cost	180
		Book Debts	400

Investment (meant for replacement of Plant and Machinery)	1,600
Cash at Bank and Cash in hand	192
Discount on Debentures	10
Underwriting Commission	<u>16</u>
	<u>7,632</u>

The resale value of Premises and Land is Rs.1,200 lacs and that of Plant and Machinery is Rs.2,400 lacs. Depreciation @ 20% is applicable to Motor Vehicles. Applicable depreciation on Premises and Land is 2%, and that on Plant and Machinery is 10%. Market value of the Investments is Rs.1,500 lacs. 10% of book debts is bad. In a similar company the market value of equity shares of the same denomination is Rs.25 per share and in such company dividend is consistently paid during last 5 years @ 20%. Contrary to this, Domestic Ltd. is having a marked upward or downward trend in the case of dividend payment.

Past 5 years' profits of the company were as under:

2001-02	Rs.67 lacs
2002-03	(-) Rs.1,305 lacs (loss)
2003-04	Rs.469 lacs
2004-05	Rs.546 lacs
2005-06	Rs.405 lacs

The unusual negative profitability of the company during 2002-03 was due to the lock out in the major manufacturing unit of the company which happened in the beginning of the second quarter of the year 2001-02 and continued till the last quarter of 2002-03.

Value the Goodwill of the Company on the basis of 4 years' purchase of the Super Profit. (Necessary assumption for adjustment of the Company's inconsistency in regard to the dividend payment, may be made by the examinee). (8+12 = 20 Marks)

Answer

(a)		In the books of Shivaji Ltd.			
		Fixed Assets Account			
Dr.				Cr.	
		Rs.		Rs.	
1.4.2002	To Bank	90,00,000	31.3.2003	By Depreciation	9,00,000
				By Balance c/d	<u>81,00,000</u>
		<u>90,00,000</u>			<u>90,00,000</u>

1.4.2003	To	Balance b/d	81,00,000	31.3.2004	By	Depreciation	9,00,000
					By	Balance c/d	72,00,000
			<u>81,00,000</u>				<u>81,00,000</u>
1.4.2004	To	Balance b/d	72,00,000	1.4.2004	By	Revaluation Reserve (W.N.2)	3,60,000
	To	Revaluation Reserve (W.N.1)	5,40,000	31.3.2005	By	Depreciation (W.N.3)	9,22,500
					By	Balance c/d	64,57,500
			<u>77,40,000</u>				<u>77,40,000</u>
1.4.2005	To	Balance b/d	64,57,500	31.3.2006	By	Depreciation	9,22,500
					By	Balance c/d	55,35,000
			<u>64,57,500</u>				<u>64,57,500</u>
1.4.2006	To	Balance b/d	55,35,000	1.4.2006	By	Bank	54,80,000
					By	Revaluation Reserve (loss)	55,000
			<u>55,35,000</u>				<u>55,35,000</u>

Depreciation Account

			Rs.				Rs.
31.3.2003	To	Fixed assets	<u>9,00,000</u>	31.3.2003	By	P&L Account	<u>9,00,000</u>
31.3.2004	To	Fixed assets	<u>9,00,000</u>	31.3.2004	By	P&L Account	<u>9,00,000</u>
31.3.2005	To	Fixed assets	9,22,500	31.3.2005	By	P&L Account	9,00,000
					By	Revaluation Reserve Account (W.N.4)	22,500
			<u>9,22,500</u>				<u>9,22,500</u>
31.3.2006	To	Fixed assets	9,22,500	31.3.2006	By	P&L Account	9,00,000
					By	Revaluation Reserve Account	22,500
			<u>9,22,500</u>				<u>9,22,500</u>

Dr.		Revaluation Reserve Account				Cr.
		Rs.				Rs.
1.4.2004	To Fixed assets (Loss on revaluation)	3,60,000	1.4.2004	By Fixed Assets (upward revaluation)		5,40,000
31.3.2005	To Depreciation (W.N.4)	22,500				
	To Balance c/d	<u>1,57,500</u>				
		<u>5,40,000</u>				<u>5,40,000</u>
31.3.2006	To Depreciation	22,500	1.4.2005	By Balance b/d		1,57,500
	To Balance c/d	<u>1,35,000</u>				
		<u>1,57,500</u>				<u>1,57,500</u>
1.4.2006	To Fixed assets (Loss on sale of revalued assets)	55,000	1.4.2006	By Balance b/d		1,35,000
	To General Reserve	<u>80,000</u>				
		<u>1,35,000</u>				<u>1,35,000</u>

Workings Notes:

- Calculation of Revaluation amount to be shown in revaluation reserve account:
Downward revision of 50% of fixed assets = $(Rs.72,00,000 \times \frac{1}{2}) \times 10\% = Rs.3,60,000$
Upward revision of remaining 50% of fixed assets = $(Rs.72,00,000 \times \frac{1}{2}) \times 15\% = Rs.5,40,000$
- Value of Fixed assets after revaluation as on 1.4.04:
 $[(72,00,000 \times \frac{1}{2}) - 3,60,000] + \{(72,00,000 \times \frac{1}{2}) + 5,40,000\} = Rs.32,40,000 + 41,40,000 = Rs.73,80,000$
- Depreciation per annum for remaining 8 years
Value of Fixed Assets = Rs.73,80,000 (W.N.2)
Remaining life of the asset = 8 years
New Depreciation = $Rs.73,80,000 / 8 = Rs.9,22,500$
- Depreciation to be charged to Revaluation Reserve Account
 $= Rs.9,22,500 - Rs.9,00,000 = Rs.22,500$

(b) 1. Calculation of capital employed

Present value of assets:		Rs. (in lacs)
Premises and land		1,200
Plant and machinery		2,400
Motor vehicles (book value less depreciation for $\frac{1}{2}$ year)		36
Raw materials		920
Work-in-progress		130
Finished goods		180
Book debts (400 x 90%)		360
Investments		1,500
Cash at bank and in hand		<u>192</u>
		6,918
Less: Liabilities:		
Provision for taxation	300	
5% Debentures	2,000	
Secured loans	200	
Sundry creditors	<u>300</u>	<u>2,800</u>
Total capital employed on 31.3.07		<u>4,118</u>
2. Profit available for shareholders for the year 2006-07		
Profit for the year as per Balance Sheet		1,100
Less: Depreciation to be considered		
Premises and land	24*	
Plant & machinery	240*	
Motor vehicles	<u>4</u>	<u>268</u>
		832
Less: Bad debts		<u>40</u>
Profit for the year 2006-07		<u>792</u>
3. Average capital employed		
Total capital employed		4118
Less: $\frac{1}{2}$ of profit for the current year [Refer point 2]		<u>396</u>
Average capital employed		<u>3722</u>

* Depreciation on premises and land and plant and machinery have been provided on the basis of assumption that the same has not been provided for earlier.

		Rs. (in lacs)
4.	Average profit to determine Future Maintainable Profits	
	Profit for the year 2006-07	792
	Profit for the year 2005-06	405
	Profit for the year 2004-05	546
	Profit for the year 2003-04	<u>469</u>
		2212 / 4
		<u>553</u>
5.	Calculation of General Expectation:	
	Domestic Ltd. pays Rs.2 as dividend (20%) for each share of Rs.10.	
	Market value of equity shares of the same denomination is Rs.25 which fetches dividend of 20%.	
	Therefore, share of Rs.10 (Face value of shares of Domestic Ltd.) is expected to fetch $(20/25) \times 10 = 8\%$ return.	
	Since Domestic Ltd. is not having a stable record in payment of dividend, in its case the expectation may be assumed to be slightly higher, say 10%.	
6.	Calculation of super profit	Rs. (in lacs)
	Future maintainable profit [See point 4]	553
	Normal profit (10% of average capital employed as computed in point 3)	<u>372.2</u>
	Super Profit	<u>180.8</u>
7.	Valuation of Goodwill	
	Goodwill at 4 years' purchase of Super Profit	723.20

Notes:

- (1) It is evident from the Balance Sheet that depreciation was not charged to Profit & Loss Account.
- (2) It is assumed that provision for taxation already made is sufficient.
- (3) While considering past profits for determining average profit, the years 2001-02 and 2002-03 have been left out, as during these years normal business was hampered.

Question 4

- (a) Indian Engineering and Technological Institute, an autonomous body furnishes the following information:

On 1.4.2006, unutilised restricted government grant (capital) balance is Rs.40,00,000; unutilised unrestricted government grant (revenue) balance is Rs.9,00,000; Institute's own corpus fund is Rs.25,00,000. Besides, a private endowment fund of Rs.18,50,000 is there on that date. The entire endowment fund is in fixed deposit with a bank fetching interest of 9.5% p.a. half-yearly transferred on 30th September and 31st March to a current account meant for scholarship and awards. The said current account has a debit

balance of Rs.1,37,500. Apart from this, total cash and bank balance as on 1.4.06 is Rs.85,00,000.

Following transactions took place during the year 2006-07:

- (1) Salary paid out of own fund is Rs.65,00,000.
- (2) Salary to the research associates of a Government sponsored research scheme is Rs.4,00,000 paid out of unrestricted government grant.
- (3) Cost of renovation of the administrative building borne out of the Institute's own fund is Rs.4,75,000. The renovation work was completed on 21st November, 2006 which was also the date of payment. Book value of the building was Rs.38,00,000 on 1.4.06. The rate of depreciation is 5% p.a. calculated at full year's rate if the asset exists for a period exceeding 6 months, and at half-year's rate in other cases. The same principle is followed by the Institute in all cases of depreciation.
- (4) Tuition fees were received Rs.85,00,000.
- (5) Scholarships and awards of Rs.1,43,000 were given on 9th December, 2006.
- (6) A laboratory building was under construction for the last two years. Balance of capital work-in-progress on 1.4.06 was Rs.28,00,000. The work has been completed on 25th May, 2006. Final payment was made earlier on 29.4.2006. Total expenditure comes to Rs.37,00,000. Rate of depreciation on the laboratory building is 5%. The entire expenditure will be spent from the restricted government (capital) Grant on certain conditions attached by the government. The Institute follows the principles of AS 12 in the case of use of revenue and capital grant. Since certain conditionality will apply over a period of time, it is decided that deferred income method will be followed.

Show the following Ledger accounts:

- (i) Restricted Government Grant (capital) A/c.
 - (ii) Unrestricted Government Grant (revenue) A/c.
 - (iii) Current A/c of Endowment and Scholarship.
 - (iv) Cash and Bank A/c.
- (b) Value Added Ltd. furnishes the following Profit and Loss A/c:

Profit and Loss A/c for the year ended 31 st March, 2007		
Income	Notes	Rs.('000)
Turnover	1	29,872
Other Income		<u>1,042</u>
		<u>30,914</u>
Expenditure		
Operating expenses	2	26,741
Interest on 8% Debenture		987

Interest on Cash Credit	3	151
Excise duty		<u>1,952</u>
		<u>29,831</u>
Profit before depreciation		1,083
Less: Depreciation		<u>342</u>
Profit before tax		741
Provision for tax	4	<u>376</u>
Profit after tax		365
Less: Transfer to Fixed Assets Replacement Reserve		<u>65</u>
		300
Less: Dividend paid		<u>125</u>
Retained Profit		<u>175</u>

Notes:

- (1) Turnover is based on invoice value and net of sales tax.
- (2) Salaries, wages and other employee benefits amounting to Rs.14,761 ('000) are included in operating expenses.
- (3) Cash Credit represents a temporary source of finance. It has not been considered as a part of capital.
- (4) Transfer of Rs.54 ('000) to the credit of deferred tax account is included in provision for tax.

Prepare value added statement for the year ended 31st March, 2007 and reconcile total value added with profit before taxation.
(8+8 = 16 Marks)

Answer

(a) Restricted Government Grant (Capital) Account

Dr.		Rs.				Cr.
						Rs.
31.3.07	To Income and Expenditure A/c - Grant against laboratory building (recognized to the extent of amount spent)	37,00,000	1.4.06	By	Balance b/d	40,00,000
	To Balance c/d	<u>3,00,000</u>				
		<u>40,00,000</u>				<u>40,00,000</u>
			1.4.07	By	Balance b/d	3,00,000

Unrestricted Government Grant (Revenue) Account

		Rs.			Rs.
31.3.07	To Income & Expenditure A/c (salary paid to research associates)	4,00,000	1.4.06	By Balance b/d	9,00,000
	To Balance c/d	<u>5,00,000</u>			
		<u>9,00,000</u>			<u>9,00,000</u>
			1.4.07	By Balance b/d	5,00,000

Current Account of Endowment and Scholarship

		Rs.			Rs.
1.4.06	To Balance b/d	1,37,500	9.12.06	By Scholarship & awards	1,43,000
30.9.06	To Interest on fixed deposit (9.5% of Rs.18,50,000 for 6 months)	87,875	31.3.07	By Balance c/d	1,70,250
31.3.07	To Interest on fixed deposit (9.5% of Rs.18,50,000 for 6 months)	<u>87,875</u>			
		<u>3,13,250</u>			<u>3,13,250</u>
1.4.07	To Balance b/d	1,70,250			

Cash and Bank Account

		Rs.			Rs.
1.4.06	To Balance b/d	85,00,000	29.4.06	By Capital WIP (37,00,000 – 28,00,000)	9,00,000
31.3.07	To Tuition fee	85,00,000*	21.11.06	By Administrative Building A/c	4,75,000
			31.3.07	By Salary	65,00,000
			31.3.07	By Salary to research associates	4,00,000
			31.3.07	By Balance c/d	<u>87,25,000</u>
		<u>1,70,00,000</u>			<u>1,70,00,000</u>
1.4.07	To Balance b/d	87,25,000			

* Besides unrestricted government grant, tuition fee is also one of the primary source of income for unrestricted fund account. The question requires the preparation of unrestricted govt. grant account, therefore it is assumed that tuition fee has been credited to unrestricted fund account other than unrestricted government grant account.

(b)

Value Added Ltd.

Value Added Statement for the year ended 31st March, 2007

	Rs.('000)	Rs.('000)	%
Turnover		29,872	
Less: Cost of bought in materials and services:			
Operating expenses (26,741 –14,761)	11,980		
Excise duty	1,952		
Interest on Cash Credit	<u>151</u>	<u>14,083</u>	
Value added by manufacturing and trading activities		15,789	
Add: Other income		<u>1,042</u>	
Total value added		<u>16,831</u>	
Application of value added:			
To Pay to employees:			
Salaries, wages and other employee benefits		14,761	87.70
To Pay to Government:			
Corporation tax (376 – 54)		322	1.91
To Pay to providers of capital:			
Interest on 8% Debentures	987		
Dividends	<u>125</u>	1,112	6.61
To Provide for maintenance and expansion of the company:			
Depreciation	342		
Fixed Assets Replacement Reserve	65		
Deferred Tax Account	54		
Retained Profit	<u>175</u>	<u>636</u>	<u>3.78</u>
		<u>16,831</u>	<u>100</u>

Note: Deferred tax account could alternatively be shown as an item 'To pay to government'.

Reconciliation between total value added and profit before taxation

	Rs.('000)	Rs.('000)
Profit before tax		741
Add back: Depreciation	342	
Wages, salaries and other benefits	14,761	
Debenture interest	<u>987</u>	<u>16,090</u>
Total Value Added		<u>16,831</u>

Question 5

- (a) Arrange and redraft the following Cash Flow Statement in proper order keeping in mind the requirements of AS 3:

	Rs. (in lacs)	Rs.(in lacs)
Net Profit		60,000
Add: Sale of Investments		70,000
Depreciation on Assets		11,000
Issue of Preference Shares		9,000
Loan raised		4,500
Decrease in Stock		12,000
		1,66,500
Less: Purchase of Fixed Assets	65,000	
Decrease in Creditors	6,000	
Increase in Debtors	8,000	
Exchange gain	8,000	
Profit on sale of investments	12,000	
Redemption of Debenture	5,700	
Dividend paid	1,400	
Interest paid	<u>945</u>	<u>1,07,045</u>
		59,455
Add: Opening cash and cash equivalent		<u>12,341</u>
Closing cash and cash equivalent		<u>71,796</u>

- (b) P Ltd. has 60% voting right in Q Ltd. Q Ltd. has 20% voting right in R Ltd. Also, P Ltd. directly enjoys voting right of 14% in R Ltd. R Ltd. is a listed company and regularly supplies goods to P Ltd. The management of R Ltd. has not disclosed its relationship with P Ltd.

How would you assess the situation from the viewpoint of AS 18 on Related Party Disclosures?

- (c) Lessee Ltd. took a machine on lease from Lessor Ltd., the fair value being Rs.7,00,000. The economic life of the machine as well as the lease term is 3 years. At the end of each year Lessee Ltd. pays Rs.3,00,000. Guaranteed Residual Value (GRV) is Rs.22,000 on expiry of the lease. Implicit Rate of Return (IRR) is 15% p.a. and present value factors at 15% are 0.869, 0.756 and 0.657 at the end of first, second and third years respectively.

Calculate the value of machine to be considered by Lessee Ltd. and the interest (Finance charges) in each year.
(6+4+6 = 16 Marks)

Answer

(a) Cash Flow Statement		(Rs. in lacs)
Cash flows from operating activities		
Net profit		60,000
Less: Exchange gain		(8,000)
Less: Profit on sale of investments		<u>(12,000)</u>
		40,000
Add: Depreciation on assets		<u>11,000</u>
Change in current assets and current liabilities		51,000
(-) Increase in debtors	(8,000)	
(+) Decrease in stock	12,000	
(-) Decrease in creditors	<u>(6,000)</u>	<u>(2,000)</u>
Net cash from operating activities		49,000
Cash flows from investing activities		
Sale of investments	70,000	
Purchase of fixed assets	<u>(65,000)</u>	
Net cash from Investing activities		5,000
Cash flows from financing activities		
Issue of preference shares	9,000	
Loan raised	4,500	
Redemption of Debentures	(5,700)	
Interest paid	(945)	
Dividend paid	<u>(1,400)</u>	
Net cash from financing activities		<u>5,455</u>
Net increase in cash & cash equivalents		59,455
Add: Opening cash and cash equivalents		<u>12,341</u>
Closing cash and cash equivalents		<u>71,796</u>

- (b) P Ltd. has direct economic interest in R Ltd to the extent of 14%, and through Q Ltd. in which it is the majority shareholders, it has further control of 12% in R Ltd. (60% of Q Ltd's 20%). These two taken together (14% + 12%) make the total control of 26%.

Para 10 of AS 18 'Related Party Disclosures', defines related party as one that has at any time during the reporting period, the ability to control the other party or exercise significant influence over the other party in making financial and/or operating decisions.

Here, Control is defined as ownership directly or indirectly of more than one-half of the voting power of an enterprise; and Significant Influence is defined as participation in the financial and/or operating policy decisions of an enterprise but not control of those policies.

In the present case, control of P Ltd. in R Ltd. directly and through Q Ltd., does not go beyond 26%. However, as per para 12 of AS 18, significant influence may be exercised as an investing party (P Ltd.) holds, directly or indirectly through intermediaries 20% or more of the voting power of the R Ltd. As R Ltd. is a listed company and regularly supplies goods to P Ltd. therefore, related party disclosure, as per AS 18, is required.

- (c) Value of machine will be lower of the fair value or present value (PV) of Minimum Lease Payments (MLP).

Present value (PV) of Minimum Lease Payments (MLP)

Year	MLP	PV at 15% Rs.	PV Amount Rs.
1	3,00,000	0.869	2,60,700
2	3,00,000	0.756	2,26,800
3	3,22,000 (considering residual value)	0.657	<u>2,11,554</u>
			<u>6,99,054</u>

Since PV of MLP Rs. 6,99,054 being lower than the fair value Rs. 7,00,000, therefore, value of machine will be taken as Rs.6,99,054.

Calculation of interest (finance charges)

Year	Liability	Interest at 15%	Principal	Lease rental
	Rs.	Rs.	Rs.	Rs.
	6,99,054	1,04,858	1,95,142	3,00,000
1 st	Less: Principal <u>1,95,142</u>		(Rental – Interest)	
	5,03,912	75,587	2,24,413	3,00,000
2 nd	Less: Principal <u>2,24,413</u>		(Rental – Interest)	
	2,79,499	41,925	2,58,075	3,00,000
			(Rental – Interest)	
3 rd	Less: Principal <u>2,58,075</u>			
	Residual value <u>21,424*</u>			

* The difference between this figure and guaranteed residual value (Rs. 22,000) is due to approximation in computing the interest rate implicit in the lease.

Question 6

Write short notes on the following:

- (a) The concept of Materiality.
- (b) Maintenance of Books of Account by Stock Brokers.
- (c) Human Resources Accounting. (6+5+5 = 16 Marks)

Answer

- (a) Para 17 of AS 1 'Disclosure of Accounting Policies', states that financial statements should disclose all material items, i.e., items the knowledge of which might influence the decisions of the user of the financial statements. Materiality depends on the size of item or error judged in the particular circumstances of its omission or misstatement. From a positive perspective, materiality has to do with the significance of an item or event to warrant attention in the accounting process. From a negative view point, materiality is critical because otherwise a great deal of time might be spent on trivial matters in the accounting process. Individual judgements are required to assess materiality, or to decide what the appropriate minimum quantitative criteria are to be set for given situations. What is material to one organisation, may not be material for another organisation.

The relevance of information is affected by its materiality. Information is material if its misstatements (i.e., omission or erroneous statement) could influence the economic decisions of users taken on the basis of the financial information. Materiality provides a threshold or cut-off point rather than being a primary qualitative characteristic which the information must have if it is to be useful.

- (b) Every stock broker is required to maintain the following books of account and records as per Rule 15 of the Securities Contracts (Regulation) Rules, 1957 and Regulation 17 of the SEBI (Stock Brokers and Sub-Brokers) Rules, 1992:
 - (a) Register of transactions (Sauda book)/Daily transaction list;
 - (b) Clients ledger;
 - (c) General ledger;
 - (d) Journals;
 - (e) Cash book;
 - (f) Bank Pass Book;

- (g)* Documents register containing, inter-alia particulars of securities received and delivered in physical form and the statement of account and other records relating to receipt and delivery of securities provided by the depository participants (in respect of dematerialized securities);
- (h) Members' contract book showing details of all contracts entered into by him with other members of the stock exchange or counterfoils or duplicates of memos of confirmation issued to such other members;
- (i) Counterfoils or duplicates of contract notes issued to clients;
- (j) Written consent of clients in respect of contracts entered into as principals;
- (k) Margin deposit book;
- (l) Register of accounts of sub-brokers;
- (m) An agreement with a sub-broker specifying the scope of authority and responsibilities of the stock broker and such sub-broker.
- (n)**An agreement with the sub-broker and with the client of the sub-broker to establish privity of contract between the stock broker and the client of the sub-broker.

In addition to the above statutory requirements, stock brokers are also required to maintain scripwise clientwise list in respect of scripts of specified group, client upla statement, duplicate copies of self-certificates submitted on monthly basis, copies of margin statements downloaded by the stock exchange, copies of valan balance sheet (Form 31), details of spot delivery transactions, client data base and broker client agreement, copy of registration certificate of each sub-broker issued by SEBI, copies of the power of attorney/board resolution authorising directors and employees and copies of pool account statements.

- (c) Human Resource Accounting (HRA) is an attempt to identify, quantify and report investments made in human resources of an organization. Leading public sector units like OIL, BHEL, NTPC and SAIL etc. have started reporting human resources in their annual reports as additional information. Although human beings are considered as the prime mover for achieving productivity, and are placed above technology, equipment and money, the conventional accounting practice does not assign significance to the human resource. Human resources are not thus recognized as 'assets' in the Balance Sheet.

* Substituted by the SEBI (Stock Brokers of Sub-brokers) (Amendment) Regulations, 2003 w.e.f. 23.09.2003.

** Inserted by the SEBI(Stock Brokers and Sub-brokers) (Amendment) Regulations, 2003, w.e.f. 23.09.2003.

While investments in human resources are not considered as assets and not amortised over the economic service life, the result is that the income and expenditure statement comprising current revenue and expenditure gives a distorted picture of the real affairs of the organization.

Accountants have been severely criticized by the Behavioural Scientists for their failure to value human resources, as this has come out as a handicap for effective management.

Human resource accounting provides scope for planning and decision making in relation to proper manpower planning. Also, such accounting can bring out the effect of various new rules, procedures and incentives relating to work force, and in turn, can act as an eye opener for modifications of existing statutes and laws.