PAPER – 1 : ACCOUNTING

QUESTIONS

Branch Accounting

1. Concept & Co., with its Head Office at Mumbai has a branch at Nagpur. Goods are invoiced to the Branch at cost plus $33\frac{1}{3}\%$. The following information is given in respect of the branch for the year ended 31st March, 2008:

	Rs.
Goods sent to Branch (Invoice price)	4,80,000
Stock at Branch on 1.4.2007 (Invoice price)	24,000
Cash sales	1,80,000
Return of goods by customers to the Branch	6,000
Branch expenses (paid in cash)	53,500
Branch debtors balance on 1.4.2007	30,000
Discount allowed	1,000
Bad debts	1,500
Collection from Debtors	2,70,000
Branch debtors cheques returned dishonoured	5,000
Stock at Branch on 31.3.2008 (Invoice price)	48,000
Branch debtors balance on 31.3.2008	36,500

Prepare, under the Stock and Debtors system, the following Ledger Accounts in the books of the Head Office:

(i) Nagpur Branch Stock Account

(ii) Nagpur Branch Debtors Account

(iii) Nagpur Branch Adjustment Account.

Also compute shortage of Stock at Branch, if any.

Departmental Accounting

2. Department X sells goods to Department Y at a profit of 25% on cost and to Department Z at 10% profit on cost. Department Y sells goods to X and Z at a profit of 15% and 20% on sales, respectively. Department Z charges 20% and 25% profit on cost to Department X and Y, respectively.

Department Managers are entitled to 10% commission on net profit subject to unrealized profit on departmental sales being eliminated. Departmental profits after charging Managers' commission, but before adjustment of unrealized profit are as under:

	Rs.
Department X	36,000
Department Y	27,000
Department Z	18,000

Stocks lying at different departments at the end of the year are as under:

	Department X	Department Y	Department Z
	Rs.	Rs.	Rs.
Transfer from Department X	–	15,000	11,000
Transfer from Department Y	14,000	–	12,000
Transfer from Department Z	6,000	5,000	–

Find out the correct departmental profits after charging managers' commission.

Hire Purchase System

3. ABC Ltd. sells goods on Hire-purchase by adding 50% above cost. From the following particulars, prepare Hire-purchase Trading account to reveal the profit for the year ended 31.3.2009:

		Rs.
1.4.2008	Instalments due but not collected	10,000
1.4.2008	Stock at shop (at cost)	36,000
1.4.2008	Instalment not yet due	18,000
31.3.2009	Stock at shop	40,000
31.3.2009	Instalments due but not collected	18,000
Other details:		
Total instalments became due		1,32,000
Goods purchased		1,20,000
Cash received from customers		1,21,000

Goods on which due instalments could not be collected were repossessed and valued at 30% below original cost. The vendor spent Rs. 500 on getting goods overhauled and then sold for Rs. 2,800

Investment Accounts

4. On 1.4.2008, Sundar had 25,000 equity shares of 'X' Ltd.at a book value of Rs. 15 per share (Face value Rs.10). On 20.6.2008, he purchased another 5,000 shares of the company at Rs. 16 per share. The directors of 'X'Ltd. announced a bonus and rights issue. No dividend was payable on these issues. The tems of the issue are as follows:

   Bonus basis 1:6 (Date 16.8.08).

   Rights basis 3:7 (Date 31.8.08) Price Rs. 15 per share.

Due date for payment 30.9.08.

Shareholders can transfer their rights in full or in part. Accordingly Sundar sold 33.33% of his entitlement to Sekhar for a consideration of Rs. 2 per share.

Dividends: Dividends for the year ended 31.3.08 at the rate of 20% were declared by X Ltd. and received by Sundar on 31.10.08. Dividends for shares acquired by him on 20.6.08 are to be adjusted against the cost of purchase.

On 15.11.08, Sundar sold 25,000 equity shares at a premium of Rs. 5 per share.

You are required to prepare in the books of Sundar.

(i) Investment Account

(ii) Profit & Loss Account.

For your exercise, assume that the books are closed on 31.12.08 and shares are valued at average cost.

Partnership accounts

5. A, B and C carried on business in partnership, sharing Profits and Losses in the ratio of 1:2:3. They decided to form a private limited company, AB (P) Ltd. and C is not interested to take over the shares in AB (P) Ltd. The authorized share capital of the company is Rs.12,00,000 divided into 12,000 ordinary shares of Rs.100 each.

   The company was incorporated and took over goodwill as valued and certain assets of the partnership firm on 31.3.2008. The Balance Sheet of the partnership firm on that date was as follows:

Liabilities		Rs.	Assets	Rs.
Capital Accounts:			Fixed Assets:	
A		1,00,000	Machinery	1,20,000
B		2,00,000	Land	1,74,000
C		3,00,000	Motorcycles	30,000
Current Accounts:			Furniture & fittings	11,000
A		39,420	Current Assets:	
B		60,580	Stock	2,35,000
A's Loan A/c	28,000		Debtors	43,000
(+) Interest accrued	2,000	30,000	Cash in hand	87,000
Current Liability:			C's overdrawn	1,00,000
Creditors		70,000		
		8,00,000		8,00,000

   C, who retired was presented by the other partners (A and B) with one motorcycle valued in the books of the firm Rs.9,000. The remaining motorcycles were sold in the open market for Rs.13,000. C also received certain furniture for which he was charged Rs.2,000. The debtors which were all considered good, were taken over by C for Rs.40,000. A and B were charged in their profit sharing ratio for the book value of Motorcycle presented by them to C.

It was agreed that C who is not willing to take the shares in AB (P) Ltd. was discharged first by providing necessary cash. A and B should bring cash, if necessary.

AB (P) Ltd. took over the remaining furniture and fittings at a price of Rs.13,000, the machinery for Rs.1,25,000, the stock at an agreed value of Rs.2,00,000 and the land at its book value. The value of the goodwill of the partnership firm was agreed at Rs.88,000. The creditors of the firm were settled by the firm for Rs.70,000. A's loan account together with interest accrued was transferred to his capital account.

The purchase consideration was discharged by the company by the issue of equal number of fully paid up equity shares at par to A and B.

Prepare Realisation A/c, Capital A/cs of the partners and Cash A/c. Also draw the Balance Sheet of AB (P) Ltd.

Contract Accounts

6. A firm of contractors obtained a contract for construction of bridges across river Revathi. The following details are available in the records kept for the year ended 31st March, 2008.

	(Rs. in lakhs)
Total Contract Price	1,000
Work Certified	500
Work not Certified	105
Estimated further Cost to Completion	495
Progress Payment Received	400
To be Received	140

The firm seeks your advice and assistance in the presentation of accounts keeping in view the requirements of AS 7 (Revised) .

Insolvency Accounts for Non-Corporate Entities

7. Mr. A is insolvent. He supplies to you the following information as on 31.3.2008:

	Rs.
Cash in hand	10,000
Creditors for goods	10,00,000
Taxes due to Government	35,000
Bank loan secured by lien on stock	1,50,000
Furniture (expected to realize Rs 50,000)	75,000

Stock (expected to realize 50%)	6,00,000
Book debts (good)	4,50,000
Book debts (doubtful) expected to realize 40%	5,50,000
Bills discounted (Rs.40,000 bad)	1,40,000
Loan from Nathan secured by second charge on stock	2,00,000
Bills receivable (Rs.40,000 bad)	1,00,000

Mr. A started business four years ago with a capital of Rs.4,50,000. He drew Rs.75,000 each year for private purposes, but did not maintain proper books of accounts. Mrs. A gave up her jewellery valued Rs.1,00,000 to the receiver.

Prepare Statement of Affairs of Mr. A as on 31.3.2008 and Deficiency Account as on that date.

Redemption of Preference Shares

8. The balance sheet of XYZ Ltd. as at 31st December, 2008 inter alia includes the following :

		Rs.
50,000	8% Preference shares of Rs. 100 each Rs. 70 paid up	35,00,000
1,00,000	Equity shares of Rs. 100 each fully paid up	1,00,00,000
	Securities premium	5,00,000
	Capital redemption reserve	20,00,000
	General reserve	50,00,000

Under the terms of their issue, the preference shares are redeemable on March 31, 2009 at a premium of 5%. In order to finance the redemption, the company makes a right issue of 50,000 equity shares of Rs. 100 each at Rs. 20 being payable on application, Rs. 35 (including premium) on allotment and the balance on January 1, 2010. The issue was fully subscribed and allotment made on March 1, 2009. The monies due on allotment were received by March 30, 2009.

The preference shares were redeemed after fulfilling the necessary conditions of Section 80 of the Companies Act, 1956. The company decided to make the minimum utilisation of general reserve.

You are asked to pass the necessary jounal entries and show the relevant extracts from the Balance Sheet as on March 31, 2009 with the corresponding figures as on 31st December, 2008.

Underwriting of Shares

9. A joint stock company resolved to issue 10 lakh equity shares of Rs. 10 each at a premium of Re. 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. Their firm underwriting was as follows :

X 30,000 shares, Y 20,000 shares and Z 10,000 shares. 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 :

Prepare a statement calculating underwriters' liability for shares other than shares underwritten firm.

Cash Flow Statement

10. From the following Balance Sheet and information, prepare Cash Flow Statement of Ryan Ltd. for the year ended 31st March, 2009 using 'indirect method':

Balance Sheet

	31st March, 2009 Rs.	31st March, 2008 Rs.
Liabilities		
Equity Share Capital	6,00,000	5,00,000
10% Redeemable Preference Capital	–	2,00,000
Capital Redemption Reserve	1,00,000	–
Capital Reserve	1,00,000	–
General Reserve	1,00,000	2,50,000
Profit and Loss Account	70,000	50,000
9% Debentures	2,00,000	–
Sundry Creditors	95,000	80,000
Bills Payable	20,000	30,000
Liabilities for Expenses	30,000	20,000
Provision for Taxation	95,000	60,000
Proposed Dividend	90,000	60,000
	15,00,000	12,50,000

	31st March, 2009	31st March, 2008
	Rs.	Rs.
Assets		
Land and Building	1,50,000	2,00,000
Plant and Machinery	7,65,000	5,00,000
Investments	50,000	80,000
Inventory	95,000	90,000
Bills Receivable	65,000	70,000
Sundry Debtors	1,75,000	1,30,000
Cash and Bank	65,000	90,000
Preliminary Expenses	10,000	25,000
Voluntary Separation Payments	1,25,000	65,000
	15,00,000	12,50,000

Additional Information:

(i) A piece of land has been sold out for Rs. 1,50,000 (Cost – Rs. 1,20,000) and the balance land was revalued. Capital Reserve consisted of profit on sale and profit on revaluation.

(ii) On 1st April, 2008 a plant was sold for Rs. 90,000 (Original Cost – Rs. 70,000 and W.D.V. – Rs. 50,000) and Debentures worth Rs. 1 lakh was issued at par as part consideration for plant of Rs. 4.5 lakhs acquired.

(iii) Part of the investments (Cost – Rs. 50,000) was sold for Rs. 70,000.

(iv) Pre-acquisition dividend received Rs. 5,000 was adjusted against cost of investment.

(v) Directors have proposed 15% dividend for the current year.

(vi) Voluntary separation cost of Rs. 50,000 was adjusted against General Reserve.

(vii) Income-tax liability for the current year was estimated at Rs. 1,35,000.

(viii) Depreciation @ 15% has been written off from Plant account but no depreciation has been charged on Land and Building.

Accounting for Amalgamations

11. Exe Limited was wound up on 31.3.2008 and its Balance Sheet as on that date was given below:

Balance Sheet of Exe Limited as on 31.3.2008

Liabilities	Rs.	Assets	Rs.
Share capital:		Fixed assets	9,64,000
1,20,000 Equity shares of		Current assets:	

Rs. 10 each	12,00,000	Stock		7,75,000	
Reserves and surplus:		Sundry debtors	1,60,000		
Profit prior to incorporation	42,000	Less:Provision for bad and doubtful debts	8,000	1,52,000	
Contingency reserve	2,70,000				
Profit and loss A/c	2,52,000				
Current liabilities:		Bills receivable		30,000	
Bills payable	40,000	Cash at bank		3,29,000	12,86,000
Sundry creditors	2,26,000				
Provisions:					
Provision for income tax	2,20,000				
	22,50,000				22,50,000

Wye Limited took over the following assets at values shown as under:

Fixed assets Rs. 12,80,000, Stock Rs. 7,70,000 and Bills Receivable Rs. 30,000.

Purchase consideration was settled by Wye Limited as under:

Rs. 5,10,000 of the consideration was satisfied by the allotment of fully paid 10% Preference shares of Rs. 100 each. The balance was settled by issuing equity shares of Rs. 10 each at Rs. 8 per share paid up.

Sundry debtors realised Rs. 1,50,000. Bills payable was settled for Rs. 38,000. Income tax authorities fixed the taxation liability at Rs. 2,22,000.

Creditors were finally settled with the cash remaining after meeting liquidation expenses amounting to Rs. 8,000.

You are required to:

(i) Calculate the number of equity shares and preference shares to be allotted by Wye Limited in discharge of purchase consideration.

(ii) Prepare the Realisation account, Cash/Bank account, Equity shareholders account and Wye Limited account in the books of Exe Limited.

(iii) Pass journal entries in the books of Wye Limited.

Internal Reconstruction of Company

12. The following is the Balance Sheet of Rocky Ltd. as at March 31, 2008:

Liabilities	Rs. in lacs
Fully paid equity shares of Rs. 10 each	500
Capital Reserve	6
12% Debentures	400
Debenture Interest Outstanding	48
Trade Creditors	165
Directors' Remuneration Outstanding	10
Other Outstanding Expenses	11
Provisions	33
	1,173

Assets	
Goodwill	15
Land and Building	184
Plant and Machinery	286
Furniture and Fixtures	41
Stock	142
Debtors	80
Cash at Bank	27
Discount on Issue of Debentures	8
Profits and Loss Account	390
	1,173

The following scheme of internal reconstruction was framed, approved by the Court, all the concerned parties and implemented:

(i) All the equity shares be converted into the same number of fully-paid equity shares of Rs. 2.50 each.

(ii) Directors agree to forego their outstanding remuneration.

(iii) The debentureholders also agree to forego outstanding interest in return of their 12% debentures being converted into 13% debentures.

(iv) The existing shareholders agree to subscribe for cash, fully paid equity shares of Rs. 2.50 each for Rs. 125 lacs.

(v) Trade creditors are given the option of either to accept fully-paid equity shares of Rs. 2.50 each for the amount due to them or to accept 80% of the amount due in cash. Creditors for Rs. 65 lacs accept equity shares whereas those for Rs. 100 lacs accept Rs. 80 lacs in cash in full settlement.

(vi) The Assets are revalued as under :

	Rs. in lacs
Land and building	230
Plant and Machinery	220
Stock	120
Debtors	76

Pass Journal Entries for all the above mentioned transactions and draft the company's Balance Sheet immediately after the reconstruction.

Liquidation of Company

13. The following was the Balance Sheet of X Limited as on 31.3.2008 :

Balance Sheet of X Limited as at 313.2008

Liabilities	Rs.	Assets	Rs.
Share Capital		Fixed Assets	
14%, 40,000 preference shares of		Land	40,000
Rs. 100 each fully paid up	4,00,000	Buildings	1,60,000
8,000 equity shares of Rs. 100 each,		Plant and Machinery	5,40,000

Rs. 60 per share paid up	4,80,000	Patents	40,000
Reserves and Surplus	NIL	Investments	NIL
Secured Loans		Current assets, loans and advances	
1. 14% debentures	2,30,000	A. Current Assets	
(Having a floating charge on all assets)		Stock at cost	1,00,000
		Sundry debtors	2,30,000
Interest accrued on above debentures	32,200	Cash at bank	60,000
(Also having a floating charge as above)		B. Loans and Advances	NIL
		Miscellaneous expenses	
		Profit and Loss A/c	2,40,000
2. Loan on mortgage of land and building	1,50,000		
Unsecured Loan	NIL		
Current Liabilities and provisions			
A. Current liabilities			
Sundry creditors	1,17,800		
	14,10,000		14,10,000

On 31.3.2008 the company went into voluntary liquidation. The dividend on 14% preference shares was in arrears for one year. Sundry creditors include preferential creditors amounting to Rs. 30,000.

The assets realised the following sums

Land Rs. 80,000; Buildings Rs. 2,00,000; Plant and machinery Rs. 5,00,000; Patent Rs. 50,000; Stock Rs. 1,60,000; Sundry debtors Rs. 2,00,000.

The expenses of liquidation amounted to Rs. 29,434. The liquidator is entitled to a commission of 2% on all assets realised (except cash at bank) and 2% on amounts among unsecured creditors other than preferential creditors. All payments were received on 30th June, 2008. Interest on mortgage loan shall be ignored at the time of payment.

Prepare the liquidator's final statement of account.

Accounting of banking Companies

14. (a) The following is an extract from the Trial Balance of Dream Bank Ltd. as at 31st March, 2008:

Rebate on bills discounted as on 1-4-2007	68,259 (Cr.)
Discount received	1,70,156 (Cr.)

Analysis of the bills discounted reveals as follows:

Amount (Rs.)	Due date
2,80,000	June 1, 2008
8,72,000	June 8, 2008
5,64,000	June 21, 2008
8,12,000	July 1, 2008
6,00,000	July 5, 2008

You are required to find out the amount of discount to be credited to Profit and Loss account for the year ending 31st March, 2008 and pass Journal Entries. The rate of discount may be taken at 10% per annum.

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

	Rs. 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 Rs.600 lakhs)	2,000
Non-recoverable Assets	1,500

Accounting for Insurance Companies

15. The following figures have been extracted from the books of New India Insurance Company Ltd. in respect of their Marine Business for 2007-2008:

(Rs. in lakhs)

Direct Business Income received	50.00	Commission paid on Direct Business	5.00
Reserve for unexpired risks as on 1.4.2007	60.00	Expenses of Management	5.00
Claims outstanding as on 1.4.2007 (net)	20.00	Income tax deducted at source	3.00
Bad Debts	10.00	Profit and Loss Account:	
		(Cr.) balance as on 1.4.2007	10.00
Income from investment and dividends (gross)	10.00	Other expenses	1.25
Rent received from properties	5.00	Reinsurance premium receipts	5.00
Investment in government securities as on 1.4.2007	100.00	Outstanding claims as on 31.3.2008 (net)	30.00
Investment in shares as on 1.4.2007	20.00	Direct claims paid (gross)	25.00
		Reinsurance claims paid	4.00

Prepare a Revenue Account and Profit and Loss Account for the year after taking into account the following further information:

(a) All direct risks are reinsured for 20% of the risk.

(b) Claim a Commission of 25% on reinsurance ceded.

(c) Provide 25% Commission on reinsurance accepted

(d) Market value of investments as on 31st march, 2008 is as follows:

  (i) Government Securities Rs. 105 lakhs.

  (ii) Shares Rs. 18 lakhs.

  Adjust separately for each of these two categories of investments.

(e) Provide 65% for Income tax.

Accounting for Electricity Companies

16. X Electricity Company Limited decides to replace one of its old plants with a modern one in April, 2008. The plant when installed in the year 2000, costed the company Rs.26 lakhs, the components of materials and labour being in the ratio of 7:3. It is ascertained that the cost of labour and materials have risen by 30% and 25% respectively. The cost of new plant is Rs.66 lakhs and in addition old materials worth Rs.92,000 are reused. Old materials worth Rs.1,68,000 are sold. Under double account system compute the following:

(i) The amount to be written off to Revenue A/c.

(ii) The amount to be capitalized.

(iii) Draw up the necessary Journal entries.

(iv) Draw up the Replacement Account.

Accounting from Incomplete Records

17. Shri Rashid furnishes you with the following information relating to his business :

(a) Assets and liabilities as on	1.1.2007	31.12.2007
	Rs.	Rs.
Furniture (w.d.v)	6,000	6,350
Stock at cost	8,000	7,000
Sundry Debtors	16,000	?
Sundry Creditors	11,000	15,000
Prepaid expenses	600	700
Unpaid expenses	2,000	1,800
Cash in hand and at bank	1,200	625

(b) Receipts and payments during 2007 :

Collections from debtors, after allowing discount of Rs. 1,500 amounted to Rs. 58,500.

Collections on discounting of bills of exchange, after deduction of discount of Rs. 125 by the bank, totalled to Rs. 6,125.

Creditors of Rs. 40,000 were paid Rs. 39,200 in full settlement of their dues.

Payment for freight inwards Rs. 3,000.

Amounts withdrawn for personal use Rs. 7,000.

Payment for office furniture Rs. 1,000.

Investment carrying annual interest of 4% were purchased at Rs. 96 on 1st July, 2007 and payment made therefor.

Expenses including salaries paid Rs. 14,500.

Miscellaneous receipts Rs. 500.

(c) Bills of exchange drawn on and accepted by customers during the year amounted to Rs. 10,000. Of these, bills of exchange of Rs. 2,000 were endorsed in favour of creditors. An endorsed bill of exchange of Rs. 400 was dishonoured.

(d) Goods costing Rs. 900 were used as advertising materials.

(e) Goods are invariably sold to show a gross profit of $33^1/_3$% on sales.

(f) Difference in cash book, if any, is to be treated as further drawing or introduction by Shri Rashid.

(g) Provide at 2.5% for doubtful debts on closing debtors.

Rashid asks you to prepare trading and profit and loss a/c for the year ended 31st December, 2007 and the balance sheet as on that date.

Theory Questions

18. (a) Whether government accounting is totally different from commercial accounting ? State your opinion with reasons.

(b) Write short note on Common costs incurred in agricultural farm and the basis of their apportionment.

19. Write short notes on:

(a) Basis of common expenditure among departments.

(b) Preferential creditors.

(c) Co-insurance.

(d) Fluctuating capital method in partnership accounts.

(e) Accounting in case of over subscription of shares.

(f) Dividend on partly paid up shares.

(g) Reserve for unexpired risks in an insurance company.

20. (a) What are the implications of Garner vs Murray rule in partnership accounting? Explain in brief.

(b) State the conditions to be fulfilled by a joint stock company to buy-back its equity.

Theory Questions based on Accounting Standards

21. (a) What information are required to be disclosed in the financial statements as per AS 7?

(b) When can a company change its accounting policy?

(c) Explain the treatment of borrowing costs in brief.

(d) How will you calculate diluted earnings for a particular period?

(e) What are the conditions that are to be satisfied for 'Amalgamation in the nature of merger'?

(f) Explain the 'Accounting for Revaluation of fixed assets' with reference to AS 10.

(g) What do you mean by 'events occurring after the balance sheet date'? Describe disclosure requirements required for such events.

(h) Write short note on Sale and Lease Back Transactions as per Accounting Standard 19.

22. (a) What are the main considerations in selection and application of accounting policies?

(b) What are the components of costs of inventories? Explain in brief.

(c) Define the following terms for the purpose of AS 5:

(i) Ordinary activities.

(ii) Extraordinary Activities.

(d) What are the two approaches for accounting of government grants? Explain in brief.

(e) Explain the disclosure requirements as regards the investor ,where the associate has contingent liabilities.

(f) Describe "theoretical ex-right value per share" in context of AS 20.

Practical Problems based on Accounting Standards

23. (a) X and Y entered into an agreement on 20.12.2008 which provided for the sale of an asset (book value Rs. 2,50,000) for Rs. 3,70,000 to Y. The sale deed was to be registered and other formalities completed on 15.1.2009. Y has paid an advance money of Rs. 50,000 to X on 20.12.2008. Both X and Y prepare final accounts on December 31 every year and present in April next. How the transaction be shown in the books of X and for the year 2008?

(b) A Ltd. Company finds that the stock sheets as on 31.3.2007 had included twice an item the cost of which was Rs. 20,000. You are asked to suggest, how the error would be dealt within the accounts of the year ended 31.3.2008.

(c) P Ltd. owns 70 per cent of the voting power of Q Ltd. Q Ltd. in turn owns 50 per cent of the voting interest in R Ltd. Further, P Ltd. also directly owns 15 per cent of the voting interest in R Ltd. Would P Ltd. be deemed to have control over R Ltd. or would it only be considered as exercising significant influence?

(d) Bharat Ltd. wants to re-classify its investments in accordance with AS 13. Decide on the amount of transfer, based on the following information:

1. A portion of Current Investments purchased for Rs. 20 lakhs, to be re-classified as Long Term Investments, as the Company has decided to retain them. The market value as on the date of Balance Sheet was Rs. 25 lakhs.

2. Another portion of current investments purchased for Rs. 15 lakhs, to be re-classified as long term investments. The market value of these investments as on the date of balance sheet was Rs. 6.5 lakhs.

3. Certain long term investments no longer considered for holding purposes, to be reclassified as current investments. The original cost of these were Rs. 18 lakhs but had been written down to Rs. 12 lakhs to recognise permanent decline, as per AS 13.

24. (a) During the current year 2007–2008, X Limited made the following expenditure relating to its plant building:

	Rs. in lakhs
Routine Repairs	4
Repairing	1
Partial replacement of roof tiles	0.5
Substantial improvements to the electrical wiring system which will increase efficiency	10

What amount should be capitalized?

(b) How would you deal with the following in the annual accounts of a company for the year ended 31st March, 2008 ?

The company has obtained Institutional Term Loan of Rs. 580 lakhs for modernisation and renovation of its Plant & Machinery. Plant & Machinery acquired under the modernisation scheme and installation completed on 31st March, 2008 amounted to Rs. 406 lakhs, Rs. 58 lakhs has been advanced to suppliers for additional assets and the balance loan of Rs. 116 lakhs has been utilised for working capital purpose. The Accountant is on a dilemma as to how to account for the total interest of Rs. 52.20 lakhs incurred during 2007-2008 on the entire Institutional Term Loan of Rs. 580 lakhs.

(c) X Co. Ltd. supplied the following information. You are required to compute the basic earning per share:

(Accounting year 1.1.2007 – 31.12.2007)

Net Profit	:	Year 2007 : Rs. 20,00,000
	:	Year 2008 : Rs. 30,00,000
No. of shares outstanding prior to Right Issue	:	10,00,000 shares
Right Issue	:	One new share for each four Outstanding i.e., 2,50,000 shares. Right Issue price – Rs. 20 Last date of exercise rights – 31.3.2007.
Fair rate of one Equity share immediately prior to exercise of rights on 31.3.2008	:	Rs. 25

(d) At the end of the financial year ending on 31st December, 2008, 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 (Rs.)
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.

25. (a) A Ltd. had acquired 80% share in the B Ltd. for Rs. 15 lacs. The net assets of B Ltd. on the day are Rs. 22 lacs. During the year A Ltd. sold the investment for Rs. 30 lacs and net assets of B Ltd. on the date of disposal was Rs. 35 lacs. Calculate the profit or loss on disposal of this investment to be recognised in consolidated financial statement.

(b) X Ltd. is having a plant (asset) carrying amount of which is Rs. 100 lakhs on 31.3.2004. Its balance useful life is 5 years and residual value at the end of 5 years is Rs. 5 lakhs. Estimated future cash flow from using the plant in next 5 years are:-

For the year ended on	Estimated cash flow (Rs. in lakhs)
31.3.2005	50
31.3.2006	30
31.3.2007	30
31.3.2008	20
31.3.2009	20

Calculate "value in use" for plant if the discount rate is 10% and also calculate the recoverable amount if net selling price of plant on 31.3.2004 is Rs. 60 lakhs.

(c) Global Ltd. has initiated a lease for three years in respect of an equipment costing Rs.1,50,000 with expected useful life of 4 years. The asset would revert to Global Limited under the lease agreement. The other information available in respect of lease agreement is:

(i) The unguaranteed residual value of the equipment after the expiry of the lease term is estimated at Rs.20,000.

(ii) The implicit rate of interest is 10%.

(iii) The annual payments have been determined in such a way that the present value of the lease payment plus the residual value is equal to the cost of asset.

Ascertain in the hands of Global Ltd.

(i) The annual lease payment.

(ii) The unearned finance income.

(iii) The segregation of finance income, and also,

(iv) Show how necessary items will appear in its profit and loss account and balance sheet for the various years.

SUGGESTED ANSWERS/HINTS

1. In the books of head office

Nagpur Branch Stock Account

		Rs.				Rs.
1.4.2007	To Balance b/d	24,000	31.3.08	By Bank A/c (Cash Sales)		1,80,000
31.3.2008	To Goods sent to Branch A/c	4,80,000		By Branch Debtors (Credit Sales)		2,80,000
	To Branch Debtors	6,000		By Stock shortage: Branch P&L A/c	1,500*	

		Branch Adjustment A/c		2,000
		(Loading)	500	
		By Balance c/d		48,000
	5,10,000			5,10,000

Nagpur Branch Debtors Account

1.4.2007	To Balance b/d	30,000	31.3.2008	By Bank A/c (Collection)	2,70,000
31.3.2008	To Bank A/c (dishonour of cheques)	5,000		By Branch Stock A/c	6,000
	To Branch Stock A/c	2,80,000*		By Bad debts	1,500
				By Discount allowed	1,000
				By Balance c/d	36,500
		3,15,000			3,15,000

Nagpur Branch Adjustment Account

To Branch Stock A/c (loading of loss)	500*	By Stock Reserve A/c	6,000
To Stock Reserve	12,000	By Goods sent to Branch A/c	1,20,000
To Gross Profit c/d	1,13,500		
	1,26,000		1,26,000
To Branch Stock A/c (Cost of loss)	1,500	By Gross Profit b/d	1,13,500
To Branch Expenses	56,000		
To Net Profit (Transferred to General P & L A/c)	56,000		
	1,13,500		1,13,500

*Balancing figure.

Working Notes:

1. Credit Sales have not been given in the problem. So, the balancing figure of Branch Debtors Account is taken as credit sales
2. Loading is 33 $\frac{1}{3}$ % of Cost; i.e. 25% of invoice value

   Loading on opening stock = 24,000 × 25% = 6,000
3. Loading on goods sent = 4,80,000 × 25% = Rs.1,20,000
4. Loading on Closing Stock = Rs.48,000 × 25% = Rs.12,000
5. Total Branch Expenses = Cash expenses + Bad debt + Discount allowed

   = Rs.53,500 + Rs.1,500 + Rs.1,000 = Rs.56,000

6. Gross Profit

Total sales (at invoice price)- Goods returned by customers (at invoice price) x $\frac{33.33}{100+33.33}$

{(Rs. 1,80,000+ Rs. 2,80,000)- Rs. 6,000} x $\frac{33.33}{133.33}$ = Rs. 1,13,500 (approx.)

2. Statement showing calculation of correct departmental profit

	Department X	Department Y	Department Z
	Rs.	Rs.	Rs.
Profit after charging managers' commission	36,000	27,000	18,000
Add: Managers' commission (1/9)	4,000	3,000	2,000
	40,000	30,000	20,000
Less: Unrealised profit on stock (Refer working note)	4,000	4,500	2,000
Profit before Managers' commission	36,000	25,500	18,000
Less: Commission for Department Managers @ 10%	3,600	2,550	1,800
Actual departmental profit	32,400	22,950	16,200

Working Note:

Stock lying with

	Department X	Department Y	Department Z	Total
	Rs.	Rs.	Rs.	Rs.
Unrealised Profit of:				
Department X		$1/5 \times 15,000 = 3,000$	$1/11 \times 11,000 = 1,000$	4,000
Department Y	$0.15 \times 14,000 = 2,100$		$0.20 \times 12,000 = 2,400$	4,500
Department Z	$1/6 \times 6,000 = 1,000$	$1/5 \times 5,000 = 1,000$		2,000

3. In the Books of ABC Ltd.

Hire Purchase Trading Account

for the year ended 31st March, 2009

Dr.							Cr.
			Rs.				Rs.
1.1.2008	To	Hire purchase stock	18,000	1.1.2008	By	Stock reserve	
1.1.2008	To	Goods sold on hire				(1/3 of Rs. 18,000)	6,000

to 31.3.2009		Purchase	1,74,000	1.1.2008 to 31.3.2009	By	Hire purchase sales	1,32,000
	To	Loss on repossession of goods (W.N. 5)	1,600		By	Goods sold on hire purchase (1/3 of Rs. 1,74,000)	58,000
31.3.2009	To	Stock reserve	20,000		By	Profit on sale of repossessed goods (W.N. 4)	900
	To	Profit and loss account (Transfer of profit)	43,300	31.3.2009	By	Hire purchase stock (W.N. 3)	60,000
			2,56,900				2,56,900

Alternatively, Hire Purchase Trading Account can be prepared in the following manner:

Hire Purchase Trading Account

for the year ended 31st March, 2009

Dr.							Cr.
			Rs.				Rs.
1.1.2008	To	Hire purchase stock	18,000	1.1.2008	By	Stock reserve (1/3 of Rs. 18,000)	6,000
1.1.2008	To	Hire purchase debtors	10,000				
to 31.3.2009	To	Goods sold on hire purchase	1,74,000	1.1.2008 to 31.3.2009	By	Cash (Rs. 1,21,000 + Rs. 2,800)	1,23,800
	To	Cash (Overhauling charges)	500		By	Goods sold on hire purchase (1/3 of Rs. 1,74,000)	58,000
31.3.2009	To	Stock reserve	20,000				
	To	Profit and loss account (Transfer of profit)	43,300	31.3.2009	By	Hire purchase stock	60,000
					By	Hire purchase debtors	18,000
			2,65,800				2,65,800

Working Notes:

1. Memorandum Instalment due but not collected (hire purchase debtors) account

Dr.					Cr.
		Rs.			Rs.
To	Balance b/d	10,000	By	Cash	1,21,000
To	Hire purchase sales	1,32,000	By	Repossessed stock (Balancing figure)	3,000
			By	Balance c/d	18,000
		1,42,000			1,42,000

2. Memorandum shop stock account

Dr.		Rs.			Cr. Rs.
To	Balance b/d	36,000	By	Goods sold on hire purchase (Balancing figure)	1,16,000
To	Purchases	1,20,000			
			By	Balance c/d	40,000
		1,56,000			1,56,000

3. Memorandum Instalment not yet due (hire purchase stock) account

Dr.		Rs.			Cr. Rs.
To	Balance b/d	18,000	By	Hire purchase Sales	1,32,000
To	Goods sold on hire purchase [1,16,000 + (1,16,000 × 50%)]	1,74,000	By	Balance c/d (Balancing figure)	60,000
		1,92,000			1,92,000

4. Goods Repossessed account

Dr.		Rs.			Cr. Rs.
To	Hire purchase debtors	3,000	By	Hire purchase trading account (W.N. 5)	1,600
		3,000	By	Balance c/d (W.N. 5)	1,400
					3,000
To	Balance b/d	1,400			
To	Cach account (expenses)	500	By	Cash account	2,800
To	Profit on sale	900			
		2,800			2,800

5.

	Rs.
Original cost of goods repossessed $\left(\text{Rs.}\,3{,}000 \times \frac{100}{150}\right)$	2,000
Instalments due but not received	3,000
Valuation of repossessed goods (70% of Rs. 2,000)	1,400
Loss on repossession	1,600

4. Books of Sundar

Investment Account

Equity Shares in X Ltd.

		No.	Amount Rs.			No.	Amount Rs.
1.4.08	To Bal b/d	25,000	3,75,000	30.9.08	By Bank (Sale of Rights)		10,000
20.6.08	To Bank	5,000	80,000				
16.8.08	To Bonus	5,000	—	31.10.08	By Bank (dividend on shares acquired on 20/6/08)		10,000
30.9.08	To Bank (Rights Shares)	10,000	1,50,000				
				15.11.08	By Bank (Sale of shares)	25,000	3,75,000
15.11.08	To Profit transferred		50,000	31.12.08	By Bal. c/d	20,000	2,60,000
		45,000	6,55,000			45,000	6,55,000

Profit & Loss A/c

To Balance c/d	1,00,000	By Profit transferred	50,000
		By Dividend	50,000
	1,00,000		1,00,000

Working Notes:

(i) Bonus Shares = $\frac{(25{,}000 + 5{,}000)}{6} = 5{,}000$ shares

(ii) Right Shares = $\frac{25{,}000 + 5{,}000 + 5{,}000}{7} \times 3$ = 15,000 shares

(iii) Rights shares renounced = 15,000×1/3 = 5,000 shares

(iv) Dividend received = 25,000×10×20% = Rs. 50,000

Dividend on shares purchased on 20.6.08 = 5,000×10×20% = Rs.10,000 is adjusted to Investment A/c

(v) Cost of shares on 31.12.2008

$$\frac{(3{,}75{,}000 + 80{,}000 + 1{,}50{,}000 - 10{,}000 - 10{,}000)}{45{,}000} \times 20{,}000 = \text{Rs.}2{,}60{,}000$$

5. **Realization Account**

Dr.		Rs.		Cr.	Rs.
To	Machinery	1,20,000	By	Creditors	70,000
To	Land	1,74,000	By	AB (P) Ltd. – Purchase consideration (Refer Working Note)	6,00,000
To	Motor Cycles	30,000			
To	Furniture & Fittings	11,000			
To	Stock	2,35,000	By	A's Capital A/c	3,000
To	Debtors	43,000	By	B's Capital A/c	6,000
To	Cash (payment to creditors)	70,000	By	C's Capital A/c (2,000 + 40,000)	42,000
			By	Cash A/c (Sale of Motor Cycle)	13,000
To	Profit transferred to				
	A's Capital A/c	8,500			
	B's Capital A/c	17,000			
	C's Capital A/c	25,500			
		7,34,000			7,34,000

Partners' Capital Accounts

Dr		A	B	C		Cr.	A	B	C
		Rs.	Rs.	Rs.			Rs.	Rs.	Rs.
To	Current A/c	-	-	1,00,000	By	Balance b/d	1,00,000	2,00,000	3,00,000
To	Realisation A/c (Assets taken over)	3,000	6,000	42,000	By	Current A/c	39,420	60,580	-
To	Equity shares in AB (P) Ltd.	3,00,000	3,00,000	-	By	A's Loan A/c	30,000	-	-
To	Cash A/c	-	-	1,83,500	By	Realization A/c (Profit)	8,500	17,000	25,500
					By	Cash A/c	1,25,080	28,420	
		3,03,000	3,06,000	3,25,500			3,03,000	3,06,000	3,25,500

Cash Account

Dr.		Rs.		Cr.	Rs.
To	Balance b/d	87,000	By	Realisation A/c	70,000
To	Realisation A/c	13,000	By	C's Capital A/c	1,83,500
To	A's Capital A/c	1,25,080			
To	B's Capital A/c	28,420			
		2,53,500			2,53,500

Balance Sheet of AB (P) Ltd.

Liabilities	Rs.	Assets	Rs.
Authorised Share Capital:		Fixed Assets:	
12,000 Equity Shares of Rs.100 each	12,00,000	Goodwill	88,000
Issued, Subscribed & Paid up:		Land	1,74,000
6,000 equity shares of Rs.100 each fully paid up (shares were issued for consideration otherwise than for cash)		Machinery	1,25,000
		Furniture & Fittings	13,000
	6,00,000	Current Assets:	
		Stock	2,00,000
	6,00,000		6,00,000

Working Note:

Calculation of Purchase Consideration

Assets taken over by AB (P) Ltd.	Rs.
Machinery	1,25,000
Furniture & Fittings	13,000
Land	1,74,000
Stock	2,00,000
Goodwill	88,000
Purchase Consideration	6,00,000

Purchase consideration is discharged by the issue of equal number of equity shares of Rs.100 each (3,000 shares) at par to A & B.

6. (a) Amount of foreseeable loss

	(Rs in lakhs)
Total cost of construction (500 + 105 + 495)	1,100
Less: Total contract price	1,000
Total foreseeable loss to be recognized as expense	100

According to para 35 of AS 7 (Revised 2002), when it is probable that total contract costs will exceed total contract revenue, the expected loss should be recognized as an expense immediately.

(b) Contract work-in-progress i.e. cost incurred to date are Rs. 605 lakhs

	(Rs in lakhs)
Work certified	500
Work not certified	105
	605

This is 55% (605/1,100 × 100) of total costs of construction.

(c) Proportion of total contract value recognised as revenue as per para 21 of AS 7 (Revised).

55% of Rs. 1,000 lakhs = Rs. 550 lakhs

(d) Amount due from/to customers = Contract costs + Recognised profits – Recognised losses – (Progress payments received + Progress payments to be received)

= [605 + Nil – 100 – (400 + 140)] Rs. in lakhs

= [605 – 100 – 540] Rs. in lakhs

Amount due to customers = Rs. 35 lakhs

The amount of Rs. 35 lakhs will be shown in the balance sheet as liability.

(e) The relevant disclosures under AS 7 (Revised) are given below:

	Rs. in lakhs
Contract revenue	550
Contract expenses	605
Recognised profits less recognized losses	(100)
Progress billings (400 + 140)	540
Retentions (billed but not received from contractee)	140
Gross amount due to customers	35

7. Statement of Affairs of Mr. 'A' as on 31.3.2008

Gross Liabilities Rs.	Liabilities	Rs.	Expected to Rank	Property & Assets	Book Value Rs.	Expected to produce Rs.
11,40,000	Unsecured creditors as per list A		10,40,000	Properties as per list E :		
1,50,000	Fully Secured Creditors as per List B (Bank Loan)	1,50,000		Cash in Hand	10,000	10,000
				Furniture	75,000	50,000
	Less: Estimated value of stock	3,00,000		Jewellery from wife	-	1,00,000
		1,50,000		Book debts as per List F:		
	Surplus transferred to List C	1,50,000	-			
2,00,000	Partly secured creditors as per List C (Loan from Nathan)	2,00,000		Good	4,50,000	4,50,000
	Surplus transferred from List B	1,50,000	50,000	Doubtful	5,50,000	2,20,000
35,000	Preferential creditors as per list D (Taxes due to Government)	35,000		Bills Receivable as per List G	1,00,000	60,000
	Deducted as per contra	35,000	-		11,85,000	8,90,000
				Less: Preferential creditors as per contra		35,000
						8,55,000
				Deficiency as explained in List H		2,35,000
15,25,000			10,90,000			10,90,000

Deficiency Account (List H)

	Rs.		Rs.	Rs.
Excess of Assets over Liabilities	4,50,000	Bad debts as per List F		3,30,000
Accumulated Profit up to 31st March, 2008 (Refer Working Note 2)	2,50,000	Drawings (75,000x4)		3,00,000
		Other Losses:		
Profit from other sources: Jewellery from wife	1,00,000	Loss on realization of Furniture	25,000	
Deficiency as per Statement of Affairs	2,35,000	Stock	3,00,000	
		Bills receivable	40,000	3,65,000
		Loss on Bills Discounted		40,000
	10,35,000			10,35,000

Working Notes:

1. Calculation of unsecured creditors as per List A

	Gross	Expected to Rank
	Rs.	Rs.
Creditors for Goods	10,00,000	10,00,000
Liabilities for Bills Discounted	1,40,000	40,000
	11,40,000	10,40,000

2. Calculation of Accumulated Profit/Loss

Trial Balance

Debit	Rs.	Credit	Rs.
Cash	10,000	Creditors	10,00,000
Furniture	75,000	Taxes due to Government	35,000
Stock	6,00,000	Bank Loan	1,50,000
Debtors (4,50,000 + 5,50,000)	10,00,000	Loan from Nathan	2,00,000
Bills Receivable	1,00,000	Capital	4,50,000
Drawings (75,000 x 4)	3,00,000	Accumulated Profit (b/f)	2,50,000
	20,85,000		20,85,000

8. XYZ Ltd.

Journal Entries

		Dr. Rs. '000	Cr. Rs. '000
8% Preference Share Final Call Account	Dr.	15,00	
To 8% Preference Share Capital Account			15,00
(Being the final call made on 50,000 preference shares @ Rs. 30 each to make them fully paid up)			
Bank Account	Dr.	15,00	
To 8% Preference Share Final Call Account			15,00
(Being the final call amount received on 50,000 preference shares @ Rs. 30 each)			
Bank Account	Dr.	10,00	
To Equity Share Application Account			10,00
(Being the application money received on 50,000 equity shares @ Rs. 20 per share)			
Equity Share Application Account	Dr.	10,00	
To Equity Share Capital Account			10,00
(Being the application money on 50,000 equity shares transferred to equity share capital account vide Board's resolution dated...)			
Equity Share Allotment Account	Dr.	17,50	
To Equity Share Capital Account			12,50
To Securities Premium Account			5,00
(Being the amount due on 50,000 equity shares @ Rs. 35 per share [including premium Rs.] 10 vide Board's resolution dated...)			
Bank Account	Dr.	17,50	
To Equity Share Allotment Account			17,50
(Being the allotment money received on 50,000 equity shares @ Rs. 35 per share)			
8% Preference Share Capital Account	Dr.	50,00	
Premium on Redemption of Preference Shares Account	Dr.	2,50	
To Preference Shareholders Account			52,50
(Being the amount payable to preference share holders on redemption)			

Preference Shareholders Account	Dr.	52,50	
To Bank Account			52,50
(Being the payment made to preference shareholders)			
Securities Premium Account	Dr.	2,50	
To Premium on Redemption of Preference Shares Account			2,50
(Being the premium payable on redemption of preference shares charged to share premium account)			
General Reserve	Dr.	27,50	
To Capital Redemption Reserve			27,50
(Being the amount transferred to capital redemption reserve on redemption of preference shares for the balance not covered by proceeds of fresh issue of shares)			

Balance Sheet of XYZ Limited
As at 31st March, 2009 (after redemption of preference shares)
(Relevant extracts)

	Amount Rs. ('000) As on 31.3.09	Amount Rs. ('000) As on 31.12.08
1. Sources of funds		
Shareholders' funds :		
(a) Share Capital		
Issued, subscribed and paid-up		
1,00,000 equity shares of Rs. 100 each, fully paid up	1,00,00	1,00,00
50,000 equity shares of Rs. 100 each, Rs. 45 called up and paid up	22,50	—
50,000, 8% Redeemable preference shares of Rs. 100 each, Rs. 70 called-up and paid-up (redeemed on 31st March, 2009)	—	35,00
	1,22,50	1,35,00
(b) Reserves and Surplus :		
Capital redemption reserve	47,50	20,00
Securities premium account	7,50	5,00
General reserve	22,50	50,00
	77,50	75,00

The cash and bank balance will be decreased by Rs. 10,00,000 on 31.3.09 as compared to the balance on 31.12.08.

Working Notes :

		Rs. '000
(i)	Transfer to capital redemption reserve	
	Nominal value of preference shares redeemed (Rs. 100 × 50,000)	50,00
	Less : Proceeds of fresh equity issue [(Rs. 20 + 25) × 50,000)]	22,50
	Transfer to capital redemption reserve	27,50
(ii)	Capital redemption reserve as on 31.3.09	
	Balance as on 31.12.08	20,00
	Add : Transfer from general reserve	27,50
	Balance as on 31.3.09	47,50
(iii)	General reserve as on 31.3.09	
	Balance as on 31.12.08	50,00
	Less : Transfer to capital redemption reserve	27,50
	Balance as on 31.3.09	22,50
(iv)	Securities premium as on 31.3.09	
	Balance as on 31.12.08	5,00
	Add : Amount received @ Rs. 10 per share on fresh issue of 50,000 equity shares	5,00
		10,00
	Less : Premium on redemption of preference shares	2,50
	Balance as on 31.3.09	7,50
(v)	Change in cash and bank balance	
	Receipts : (31.12.08 - 31.3.09)	
	Application money on 50,000 equity shares @ Rs. 20 per share	10,00
	Allotment money on 50,000 equity shares @ Rs. 35 per share	17,50
	Final call on 50,000, 8% Preference shares @ Rs. 30 per share	15,00
		42,50
	Payments :	
	Amount paid to preference shareholders on redemption	52,50
	Reduction in cash and bank balance	10,00

9. Statement showing underwriters' liability for shares other than shares underwritten firm

	X	Y	Z	Total
Gross liability	5,85,000	2,25,000	90,000	9,00,000
(9,00,000 shares in the ratio of 65 : 25 : 10)				
Less : Marked applications	1,19,500	57,500	10,500	1,87,500
	4,65,500	1,67,500	79,500	7,12,500
Less : Allocation of unmarked applications (including firm underwriting i.e. 7,00,000) in the ratio 65 : 25 : 10	4,55,000	1,75,000	70,000	7,00,000
	10,500	(7,500)	9,500	12,500
Surplus of Y allocated to X and Z in the ratio 65 : 10	(6,500)	7,500	(1,000)	–
	4,000	–	8,500	12,500
	Rs.	Rs.	Rs.	
Liability amount @ Rs. 11	44,000	–	93,500	
Underwriting commission payable (Gross liability × Rs. 11 × 2%)	1,28,700	49,500	19,800	
Net Amount payable	84,700	49,500		
Net Amount receivable			73,700	

10.

Cash Flow Statement of Ryan Limited

For the year ended 31st March, 2009

Cash flow from operating activities	Rs.	Rs.
Net Profit before taxation	2,45,000	
Adjustment for		
Depreciation	1,35,000	
Preliminary expenses	15,000	
Profit on sale of plant	(40,000)	
Profit on sale of investments	(20,000)	
Interest on debentures	18,000	
Operating profit before working capital changes	3,53,000	

Increase in inventory	(5,000)	
Decrease in bills receivable	5,000	
Increase in debtors	(45,000)	
Increase in creditors	15,000	
Decrease in bills payable	(10,000)	
Increase in accrued liabilities	10,000	
Cash generated from operations	3,23,000	
Income taxes paid	(1,00,000)	
	2,23,000	
Voluntary separation payments	(1,10,000)	
Net cash from operating activities		1,13,000
Cash flow from investing activities		
Proceeds from sale of land	1,50,000	
Proceeds from sale of plant	90,000	
Proceeds from sale of investments	70,000	
Purchase of plant	(3,50,000)	
Purchase of investments	(25,000)	
Pre-acquisition dividend received	5,000	
Net cash used in investing activities		(60,000)
Cash flow from financing activities		
Proceeds from issue of equity shares	1,00,000	
Proceeds from issue of debentures	1,00,000	
Redemption of preference shares	(2,00,000)	
Dividends paid	(60,000)	
Interest paid on debentures	(18,000)	
Net cash used in financing activities		(78,000)
Net decrease in cash and cash equivalents		(25,000)
Cash and cash equivalents at the beginning of the year		90,000
Cash and Cash equivalents at the end of the year		65,000

Working Notes:

1.	Rs.
Net profit before taxation	
Retained profit	70,000
Less: Balance as on 31.3.2008	(50,000)

	20,000
Provision for taxation	1,35,000
Proposed dividend	90,000
	2,45,000

2. Land and Building Account

		Rs.			Rs.
To	Balance b/d	2,00,000	By	Cash (Sale)	1,50,000
To	Capital reserve (Profit on sale)	30,000	By	Balance c/d	1,50,000
To	Capital reserve (Revaluation profit)	70,000			
		3,00,000			3,00,000

3. Plant and Machinery Account

		Rs.			Rs.
To	Balance b/d	5,00,000	By	Cash (Sale)	90,000
To	Profit and loss account	40,000	By	Depreciation	1,35,000
To	Debentures	1,00,000	By	Balance c/d	7,65,000
To	Bank	3,50,000			
		9,90,000			9,90,000

4. Investments Account

		Rs.			Rs.
To	Balance b/d	80,000	By	Cash (Sale)	70,000
To	Profit and loss account	20,000	By	Dividend	
To	Bank (Balancing figure)	25,000		(Pre-acquisition)	5,000
			By	Balance c/d	50,000
		1,25,000			1,25,000

5. Capital Reserve Account

		Rs.			Rs.
To	Balance c/d	1,00,000	By	Profit on sale of land	30,000
			By	Profit on revaluation of land	70,000
		1,00,000			1,00,000

6. General Reserve Account

		Rs.			Rs.
To	Voluntary separation cost	50,000	By	Balance b/d	2,50,000
To	Capital redemption reserve	1,00,000			
To	Balance c/d	1,00,000			
		2,50,000			2,50,000

7. Proposed Dividend Account

		Rs.			Rs.
To	Bank (Balancing figure)	60,000	By	Balance b/d	60,000
To	Balance c/d	90,000	By	Profit and loss account	90,000
		1,50,000			1,50,000

8. Provision for Taxation Account

		Rs.			Rs.
To	Bank (Balancing figure)	1,00,000	By	Balance b/d	60,000
To	Balance c/d	95,000	By	Profit and loss account	1,35,000
		1,95,000			1,95,000

9. Voluntary Separation Payments Account

		Rs.			Rs.
To	Balance b/d	65,000	By	General reserve	50,000
To	Bank (Balancing figure)	1,10,000	By	Balance c/d	1,25,000
		1,75,000			1,75,000

11. (i) Purchase consideration

	Rs.
Fixed assets	12,80,000
Stock	7,70,000
Bills receivable	30,000
Purchase consideration	20,80,000

Amount discharged by issue of preference shares = Rs. 5,10,000

No. of preference shares to be allotted $= \frac{\text{Rs. } 5{,}10{,}000}{100} = 5{,}100$ shares

Amount discharged by allotment of equity shares = Rs. 20,80,000 – Rs. 5,10,000

= Rs. 15,70,000

Paid up value of equity share = Rs. 8

Hence, number of equity shares to be issued $= \frac{\text{Rs. } 15{,}70{,}000}{8}$

= 1,96,250 shares

(ii) Realisation Account

In the books of Exe Ltd.

Dr.					Cr.
		Rs.			Rs.
To	Fixed assets	9,64,000	By	Provision for bad and doubtful debts	8,000
To	Stock	7,75,000	By	Bills payable	40,000
To	Sundry debtors	1,60,000	By	Sundry creditors	2,26,000
To	Bills receivable	30,000	By	Provision for taxation	2,20,000
To	Bank account:		By	Wye Ltd. account	
	Liquidation expenses	8,000		(Purchase consideration)	20,80,000
	Bills payable	38,000	By	Bank account: Sundry debtors	1,50,000
	Tax liability	2,22,000			
	Sundry creditors	2,11,000			
To	Equity shareholders (profit transferred)	3,16,000			
		27,24,000			27,24,000

Cash/Bank Account

Dr.					Cr.
		Rs.			Rs.
To	Balance b/d	3,29,000	By	Realisation account:	
To	Realisation account:			Liquidation expenses	8,000
	Sundry debtors	1,50,000		Bills payable	38,000
				Tax liability	2,22,000
				Sundry creditors (Balancing figure)	2,11,000
		4,79,000			4,79,000

Equity Shareholders Account

Dr.					Cr.
		Rs.			Rs.
To	10% Preference shares in Wye Ltd.	5,10,000	By	Equity share capital account	12,00,000
To	Equity shares in Wye Ltd.	15,70,000	By	Profit prior to incorporation	42,000
			By	Contingency reserve	2,70,000
			By	Profit and loss account	2,52,000

		By	Realisation account (Profit)	3,16,000
	20,80,000			20,80,000

Wye Limited Account

Dr.					Cr.
		Rs.			Rs.
To	Realisation account	20,80,000	By	10% Preference shares in Wye Ltd.	5,10,000
			By	Equity shares in Wye Ltd.	15,70,000
		20,80,000			20,80,000

(iii) Journal Entries

in the books of Wye Ltd.

Particulars		Dr. Amount Rs.	Cr. Amount Rs.
Business purchase account	Dr.	20,80,000	
To Liquidator of Exe Ltd. account			20,80,000
(Being the amount of purchase consideration payable to liquidator of Exe Ltd. for assets taken over)			
Fixed assets account	Dr.	12,80,000	
Stock account	Dr.	7,70,000	
Bills receivable account	Dr.	30,000	
To Business purchase account			20,80,000
(Being assets taken over)			
Liquidator of the Exe Ltd. account	Dr.	20,80,000	
To 10% Preference share capital account			5,10,000
To Equity share capital account			15,70,000
(Being the allotment of 10% fully paid up preference shares and equity shares of Rs 10 each, Rs. 8 each paid up as per agreement for discharge of purchase consideration)			

12. Journal Entries

		Rs. in lacs	
		Dr.	Cr.
Equity Share Capital (Rs. 10 each) A/c	Dr.	500	
To Equity Share Capital (Rs. 2.50 each) A/c			125
To Reconstruction A/c			375

(Conversion of all the equity shares into the same number of fully paid equity shares of Rs. 2.50 each as per scheme of reconstruction)			
Director's Remuneration Outstanding A/c	Dr.	10	
To Reconstruction A/c			10
(Outstanding remuneration foregone by the directors as per scheme of reconstruction)			
12% Debentures A/c	Dr.	400	
Debenture Interest Outstanding A/c	Dr.	48	
To 13% Debentures A/c			400
To Reconstruction A/c			48
(Conversion of 12% debentures into 13% debentures, Debentureholders forgoing outstanding debenture interest)			
Bank	Dr.	125	
To Equity Share Application A/c			125
(Application money received for equity shares)			
Equity Share Application A/c	Dr.	125	
To Equity Share Capital (Rs. 2.50 each) A/c			125
(Application money transferred to share cpital)			
Trade Creditors	Dr.	165	
To Equity Share Capital (Rs. 2.50 each) A/c			65
To Bank A/c			80
To Reconstruction A/c			20
(Trade creditors for Rs. 64 lakhs accepting shares for full amount and those for Rs. 100 lakhs accepting cash equal to 80% of claim in full settlement)			
Capital Reserve	Dr.	6	
To Reconstruction A/c			6
(Capital Reserve being used for purpose of reconstruction)			
Land and Building	Dr.	46	
To Reconstruction A/c			46
(Appreciation made in the value of land and building as per scheme of reconstruction)			
Reconstruction A/c	Dr.	505	
To Goodwill			15
To Plant and Machinery			66
To Stock			22
To Debtors			4
To Discount on issue of Debentures			8

To Profit and Loss Account	390
(Writing off losses and reduction in the values of assets as per scheme of reconstruction—W.N. 1)	

Balance Sheet of Rocky Ltd. (and Reduced) as on 31st March, 2008

Liabilities		Rs. in lacs
1,26,000 Fully paid equity shares of Rs. 2.50 each (W.N. 2)		315
(26,000 shares have been issued for consideration other than cash)		
13% Debentures		400
Outstanding Expenses		11
Provisions		33
		759
Assets	Rs. in lack	Rs. in lacs
Goodwill	15	
Less : Amount written off under scheme of reconstruction dated...........	15	Nil
Land and Building	184	
Add : Amount of appreciation made under scheme of reconstruction dated..........	46	230
Plant and Machinery	286	
Less: Amount written off under scheme of reconstruction dated.........	66	220
Furniture and Fixtures		41
Stock		120
Debtors	80	
Less: Provision for Bad Debts	4	76
Cash at bank		72
		759

Note : Goodwill has been written off under reconstruction scheme in the solution given above.

Working Notes:

1. Reconstruction Account

(Rs. in lacs)

		Rs.			Rs.
To	Goodwill	15	By	Equity Share Capital A/c	375
To	Plant and Machinery	66	By	Director's Remuneration Outstanding A/c	10
To	Stock	22	By	Debenture Interest Outstanding A/c	48
To	Debtors	4	By	Trade Creditors	20
To	Discount on issue of		By	Capital Reserve	6

	Debentures	8	By	Land and Building	46
To	Profit and Loss A/c	390			
		505			505

2. Equity share capital as on 31st March, 2008 (after reconstruction)

	Rs.
Equity Share Capital (Rs. 2.50 each)	125
Add: Fresh issue	125
Add: Equity shares issued to creditors	65
	315

3. Cash at bank as on 31st March, 2008 (after reconstruction)

Cash at bank (before reconstruction)	27
Add: Proceeds from issue of equity shares	125
	152
Less: Payment made to creditors	80
	72

13. X Ltd.

Liquidator's Final Statement of Account

Receipts	Value Realised	Payments Rs.		Payment Rs.
Assets Realised :				
Cash at Bank	60,000	Liquidator's Remuneration (W.N. 1)		25,556
Sundry Debtors	2,00,000	Liquidation Expenses		29,434
Stock	1,60,000	Debentureholders :		
Plant and Machinery	5,00,000	14% Debentures	2,30,000	
Patents	50,000	Interest Accrued (W.N. 2)	40,250	2,70,250
Surplus from Securities		Creditors :		
(W.N. 3)	1,30,000	Preferential	30,000	
		Unsecured	87,800	1,17,800
		Preference Shareholders :		
		Preference Share Capital	4,00,000	
		Arrears of Dividend	56,000	4,56,000
		Equity Shareholders (W.N.4) :		
		Rs. 25.12 per share on 8,000 shares		2,00,960
	11,00,000			11,00,000

Working Notes :

	Rs.
1. Liquidator's remuneration :	
2% on assets realised (2% of Rs. 11,90,000)	23,800
2% on payments to unsecured creditors (2% on Rs. 87,800)	1,756
	25,556
2. Interest accrued on 14% Debentures :	
Interest accrued as on 31.3.2008	32,200

	Interest accrued upto the date of payment i.e. 30.6.2008	8,050
		40,250
3.	Surplus from Securities :	
	Amount realised from Land and Buildings (Rs. 80,000 + Rs. 2,00,000)	2,80,000
	Less : Mortgage Loan	1,50,000
		1,30,000
4.	Amount payable to Equity Shareholders :	
	Equity share capital (paid up)	4,80,000
	Less : Amount available for equity shareholders	2,00,960
	Loss to be born by equity shareholders	2,79,040
	Loss per equity share (Rs. 2,79,040/8,000)	34.88
	Amount payable to equity shareholders for each equity share (60-34.88)	25.12

Notes : (1) Commission due to the liquidator has been calculated on the total realisation on the supposition that the securities (land and buildings) are realised by the liquidator on behalf of the lender.

(2) Preference shares have been taken as cumulative.

14. (a) The amount of rebate on bills discounted as on 31st March, 2008 the period which has not been expired upto that day will be calculated as follows:

Discount on Rs.2,80,000 for 62 days @ 10%	4,756
Discount on Rs.8,72,000 for 69 days @ 10%	16,484
Discount on Rs.5,64,000 for 82 days @ 10%	12,671
Discount on Rs.8,12,000 for 92 days @ 10%	20,467
Discount on Rs.6,00,000 for 96 days @ 10%	15,781
Total	70,159

The amount of discount to be credited to the profit and loss account will be:

	Rs.
Transfer from rebate on bills discounted as on 31.03.2007	68,259
Add: Discount received during the year	1,70,156
	2,38,415
Less: Rebate on bills discounted as on 31.03.2008 (as above)	70,159
	1,68,256

Journal Entries

		Rs.	Rs.
Rebate on bills discounted A/c	Dr.	68,259	
To Discount on bills A/c			68,259
(Transfer of unexpired discount on 31.03.2007)			

Discount on bills A/c	Dr.	70,159	
To Rebate on bills discounted			70,159
(Unexpired discount on 31.03.2008 taken into account)			
Discount on Bills A/c	Dr.	1,68,256	
To P & L A/c			1,68,526
(Discount earned in the year, transferred to P&L A/c)			

(b) Calculation of amount of provision to be made in the Profit and Loss Account

Classification of Assets	Amount of advances (Rs. in lakhs)	% age of provision %	Amount of provision (Rs. in lakhs)
Standard assets	20,000	0.40	80
Sub-standard assets	16,000	10*	1,600
Doubtful assets:			
For one year (secured)	6,000	20	1,200
For two to three years (secured)	4,000	30	1,200
For more than three years (unsecured)	1,400	100	1,400
(secured)	600	100	600
Non-recoverable assets (Loss assets)	1,500	100	1,500
Total provision required			7,580

15. Form B - RA

Name of the Insurer: New India Insurance Company Ltd.
Registration No. and date of registration with the IRDA: …………….

Revenue Account for the year ended 31st March, 2008

	Particulars	Schedule	Current Year (Rs. in Lakhs)	Previous Year (Rs. in Lakhs)
.	Premium earned (net)	1	60.00	
2.	Profit/Loss on sale/redemption of investments			
	Others		-	
3.	Interest, Dividend & Rent-Gross (10+5-3)		-	
4.	Total (A)		12.00	
			72.00	
1.	Claims Incurred (Net)	2	34.00	
2.	Commission	3	3.75	
3.	Operating expenses related to insurance business	4		
	Total (B)		16.25	
			54.00	

* Sub-standards assets have been assumed as fully secured.

Operating Profit/(Loss) from Marine Business = (A-B)	(C)	18.00
Appropriations		
Transfer to Shareholder's Account		–
Transfer to Catastrophe Reserve		–
Transfer to other Reserves (to be specified)		–
Total (C)		18.00

Form B – PL

Name of the Insurer: New India Insurance Company Ltd.

Registration No. and date of registration with the IRDA: ……………..

Profit & Loss Account

for the year ended 31st March, 2008

	Particulars		Schedule	Current Year (Rs. In Lakhs)	Previous Year (Rs. In Lakhs)
1.	Operating Profit from marine insurance			18.00	
2.	Income from investments			-	
3.	Other Income			-	
	Total (A)			18.00	
4.	Provision (other than taxation)				
	Diminution in the value of investment in shares	2.00			
	Less: increment in the value of investment in govt. securities	(5.00)		(3.00)	
5.	Other expenses			-	
	Total (B)			(3.00)	
	Profit before tax A-B [i.e. 18 – (-3)]			21.00	
	Less: Provision for taxation			(10.65)	
	Total			10.35	
	Appropriations			Nil	
	Balance of profit/loss bought forward from last year			10.00	
	Balance carried forward to Balance Sheet			20.35	

Schedule 1

Premium Earned (Net)

Particulars	Current Year (Rs. in Lakhs)	Previous Year (Rs. in Lakhs)
Premium from direct business	50.00	
Add: Premium on re-insurance accepted	5.00	
	55.00	
Less: Premium on re-insurance ceded	10.00	
Net Premium	45.00	
Adjustment for change in reserve for unexpired risk [(opening) 60 – (Closing) 45]	15.00	
	60.00	

Schedule 2

Claims incurred (Net)

Particulars	Current Year (Rs. in Lakhs)	Previous Year (Rs. in Lakhs)
Claims paid		
Direct	25.00	
Add: Reinsurance accepted	4.00	
	29.00	
Less: Reinsurance ceded	5.00	
Net Claims paid	24.00	
Add: Claims outstanding at the end of the year	30.00	
	54.00	
Less: Claims outstanding at the beginning of the year	20.00	
Total claims incurred	34.00	

Schedule 3

Commission

Particulars	Current Year (Rs. in Lakhs)	Previous Year (Rs. in Lakhs)
Commission paid		
Direct	5.00	
Add: Re-insurance accepted	1.25	
	6.25	
Less: Commission on reinsurance ceded	2.50	
Net Commission	3.75	

Schedule 4

Operating Expenses

Particulars	Current Year (Rs.in Lakhs)	Previous Year (Rs.in Lakhs)
Expenses of Management	5.00	
Bad Debts	10.00	
Other expenses	1.25	
	16.25	

Working Note:

Provision for income tax:	Rs. in lakhs
Income (excluding revaluation)	18.00
Add: Tax deducted at source	3.00
	21.00
Provision @ 65% of Rs. 21.00 lakhs	13.65
Less: Tax deducted at source	(3.00)
	10.65

16. (i) Statement showing amount to be written off to Revenue Account

			Rs.
Cost of old plant			26,00,000
Add:. Increase in cost of material	$26,00,000 \text{x} \frac{7}{10} \times \frac{25}{100}$		4,55,000
Increase in cost of Labour	$26,00,000 \text{ x } \frac{3}{10} \times \frac{30}{100}$		2,34,000
Current cost of old plant			32,89,000
Less: Cost of Material used		92,000	
Cost of Material sold		1,68,000	(-) 2,60,000
Amount to be written off to Revenue A/c			30,29,000

(ii) Statement showing amount to be capitalised

Cost of new plant excluding the value of old materials used	66,00,000
Less: Current cost of old plant	32,89,000
Current cost to be capitalized	33,11,000
Add: Value of old material used	92,000
Total amount to be capitalized	34,03,000

(iii) Journal Entries in the Books of X Electricity Company Ltd.

			Rs.	Rs.
(a)	Replacement Account	Dr.	32,89,000	
	To Bank Account			32,89,000
	(Being the replacement of old plant by a new plant; the current cost of replacement Rs.32,89,000)			
(b)	Plant Account	Dr.	34,03,000	
	To Replacement Account			92,000
	To Bank Account			33,11,000
	(Being additional cost of new plant capitalized and also old materials used in construction of new plant)			
(c)	Bank Account	Dr.	1,68,000	
	To Replacement A/c			1,68,000
	(Being the sale of old materials for Rs.1,68,000)			
(d)	Revenue A/c	Dr.	30,29,000	
	To Replacement Account			30,29,000
	(Being the balance of replacement account transferred to revenue account)			

(iv) Replacement Account

Dr.					Cr.
		Rs.			Rs.
To	Bank A/c	32,89,000	By	New Plant A/c	92,000
			By	Bank A/c	1,68,000
			By	Revenue A/c (Balancing figure)	30,29,000
		32,89,000			32,89,000

17. Trading and Profit and Loss Account of Shri Rashid for the year ended 31st December, 2007

		Rs.			Rs.
To Opening Stock		8,000	By	Sales	73,050
To Purchases	45,600		By	Closing stock	7,000

Less : For advertising	900	44,700			
To Freight inwards		3,000			
To Gross profit c/d		24,350			
		80,050			80,050
To Sundry expenses		14,200	By	Gross profit b/d	24,350
To Advertisement		900	By	Interest on investment	2
To Discount allowed –				$\left(\text{Rs.}100\times\frac{4}{100}\times\frac{1}{2}\right)$	
Debtors	1,500		By	Discount received	800
Bills Receivable	125	1,625	By	Miscellaneous income	500
To Depreciation on furniture		650			
To Provision for doubtful debts		486			
To Net Profit		7,791			
		25,652			25,652

Balance Sheet as on 31st December, 2007

Liabilities		Amount	Assets		Amount
		Rs.			Rs.
Capital as on 1st January, 2007			Furniture (w.d.v.)	6,000	
	18,800		Additions during the year	1,000	
Less : Drawings	7,904			7,000	
	10,896		Less : Depreciation	650	6,350
Add : Net Profit	7,791	18,687	Investment		96
Sundry creditors		15,000	Interest accrued		2
Outstanding expenses		1,800	Closing Stock		7,000
			Sundry debtors	19,450	
			Less : Provision for		
			doubtful debts	486	18,964
			Bills receivable		1,750
			Cash in hand and at bank		625
			Prepaid expenses		700
		35,487			35,487

Working Notes :

(1) Capital on 1st January, 2007

Balance Sheet as on 1st January, 2007

Liabilities	Rs.	Assets	Rs.
Capital (Balancing figure)	18,800	Furniture (w.d.v.)	6,000
Creditors	11,000	Stock at cost	8,000

Outstanding expenses	2,000	Sundry debtors	16,000
		Cash in hand and at bank	1,200
		Prepaid expenses	600
	31,800		31,800

(2) Purchases made during the year

Sundry Creditors Account

	Rs.		Rs.
To Cash and bank A/c	39,200	By Balance b/d	11,000
To Discount received A/c	800	By Sundry debtors A/c	400
To Bills Receivable A/c	2,000	By Purchases A/c	45,600
To Balance c/d	15,000	(Balancing figure)	
	57,000		57,000

(3) Sales made during the year

		Rs.
Opening stock		8,000
Purchases	45,600	
Less : For advertising	900	44,700
Freight inwards		3,000
		55,700
Less : Closing stock		7,000
Cost of goods sold		48,700
Add : Gross profit (@ 50% on cost)		24,350
		73,050

(4) Debtors on 31.12.2007

Sundry Debtors Account

	Rs.		Rs.
To Balance b/d	16,000	By Cash and bank A/c	58,500
To Sales A/c	73,050	By Discount allowed A/c	1,500
To Sundry creditors A/c		By Bills receivable A/c	10,000
(bill dishonoured)	400	By Balance c/d (Balancing figure)	19,450
	89,450		89,450

(5) Additional drawings by Mr. Rashid

Cash and Bank Account

	Rs.		Rs.
To Balance b/d	1,200	By Freight inwards A/c	3,000
To Sundry debtors A/c	58,500	By Furniture A/c	1,000
To Bills Receivable A/c	6,125	By Investment A/c	96

To Miscellaneous income A/c	500	By Expenses A/c	14,500
		By Creditors A/c	39,200
		By Drawings A/c [Rs. 7,000 + Rs. 904 (Additional drawings)]	7,904
		By Balance c/d	625
	66,325		66,325

(6) Amount of expenses debited to Profit and Loss A/c

Expenses Account

	Rs.		Rs.
To Prepaid expenses A/c (on 1.1.2007)	600	By Outstanding expenses A/c (on 1.1.2007)	2,000
To Bank A/c	14,500	By Profit and Loss A/c (Balancing figure)	14,200
To Outstanding expenses A/c (on 31.12.2007)	1,800	By Prepaid expenses A/c (on 31.12.2007)	700
	16,900		16,900

(7) Bills Receivable on 31.12.2007

Bills Receivable Account

	Rs.		Rs.
To Debtors A/c	10,000	By Creditors A/c	2,000
		By Bank A/c	6,125
		By Discount on bills receivable A/c	125
		By Balance c/d (Balancing figure)	1,750
	10,000		10,000

Note : As regards investment, it has been assumed that investment purchased for Rs. 96 was of the face value Rs. 100.

18. (a) The primary objective of commercial accounting is to ascertain the gain or loss of an enterprise for a given period and to find out the position of assets and liabilities at the end of the accounting period. Against this, government accounts are designed to enable government to determine how much money it needs to mobilize in order to maintain its necessary activities at the proper standard of efficiency. It is thus clear that the purpose of government accounting is totally different from that of commercial accounting. The other broad differences between government accounting and commercial accounting can be enumerated as follows :

1. Financial Statements : Every commercial enterprise prepares a profit and loss account and a Balance Sheet. But in case of government accounting, following two statements are generally prepared:

(i) Government account — to show the net result of all incomes and expenditure including expenditure on capital account ;

(ii) Statement of balancing accounts — to show whether the government owes or has to receive money.

2. Method of accounting : Government accounts are maintained on cash basis as against commercial accounting in which accounts are normally maintained on mercantile basis.

3. System of accounting : In commercial accounting, double entry system of book keeping is followed. On the other hand, mass of the government accounts are kept on single entry. There is, however, a portion of accounts which is maintained on double entry basis.

4. Classification of accounts : In commercial accounting, accounts are broadly classified into (i) personal (ii) real, and (iii) nominal accounts. Government accounts are kept in three parts : Part I – Consolidated fund ; Part II – Contingency fund ; and Part III – Public account.

5. Classification of financial transactions : One of the most distinctive features of the system of government accounts in India is the minute elaboration with which the financial transactions of government under both receipts and payments, are differentiated and classified. Government expenditure in India is classified into a five tier system : Sectors, Major heads, Minor heads, Sub-heads and Detailed heads of accounts. In case of commercial accounting, no such elaborate details are provided.

(b) Seed, fertilizer, manure, pesticides, direct wages—notional and actual, land rental—notional and actual can be identified crop-wise. But other costs like irrigation, services of agricultural machinery, implements or animal power, depreciation, interest etc. cannot be classified simply by nomenclature. These costs which can't be identified cropwise are common costs of the agricultural farms. Common costs should be apportioned among the crop enterprises on the basis of usage, wherever use of assets can be quantified. In other cases length of crop season can be used. An illustrative list of the common costs and apportionment bases is given below:

Apportionment bases of common costs in agriculture

Cost element	Apportionment basis
Maintenance of Draught Animal and Depreciation	Animal Base
Maintenance of Agricultural Machinery, Implements and Depreciation	Machine Hours
Maintenance of Farm Shed and Depreciation	Length of crop season
Interest on Fixed Capital	Length of crop season
Interest on Working Capital	Working Capital Investment for various crops

19. (a) While preparing department accounts, expenses should be allocated among the different departments on the basis of the following principles :

1. Expenses incurred specially for each department are charged directly thereto e.g., insurance charges of stock held by a department.

2. Common expenses, the benefit of which is shared by all the dpeartments and which are capable of precise allocation, (e.g., rent, lighting expenses etc.) are distributed among the departments concerned on some equitable basis considered suitable in the circumstances of the case. Rent is charged to different departments according to the floor area occupied by each department, having regard to any favourable location specially allocated to a department. Lighting and heating expenses are distributed on the basis of consumption of energy by each department and so on.

3. Common expenses which are not capable of accurate measurement are dealt with as follows:

   (i) Selling expenses, e.g., discount, bad debts, selling commission, etc. are charged on the basis of sales.

   (ii) Administrative and other expenses, e.g., salaries of managers, directors, common advertisement expenses, depreciation on assets, etc., are allocated equally among all the departments that have benefited thereby. Alternatively, no allocation may be made and such expenses may be charged to the combined profit and loss account.

(b) Preferential Creditors: Section 530 specifies the creditors that have to be paid in priority to unsecured creditors or creditor having a floating charge. Such creditors are known as Preferential Creditors. These are the following:

(a) All revenues, taxes, cesses and rates, becoming due and payable by the company within 12 months next before the commencement of the winding up.

(b) All wages or salaries (including wages payable for time or piece work and salary earned wholly or in part by way of commission) of any employee due for the period not

exceeding 4 months within the twelve months next before commencement of winding up provided the amount payable to one claimant will not exceed Rs. 20,000.

(c) All accrued holiday remuneration becoming payable to any employee on account of winding up.

Note: Persons who advance money for the purpose of making preferential payments under (b) and (c) above will be treated as preferential creditors, provided the money is actually so used.

(d) Unless the company is being wound up voluntarily for the purpose of reconstruction, all contributions payable during the 12 months next under the

Employees State Insurance Act, 1948, or any other law for the time being in force.

(e) All sums due as compensation to employees under the Workmen's Compensation Act, 1923.

(f) All sums due to any employee from a provident fund, pension fund, gratuity fund or any other fund, for the welfare of the employees maintained by the company.

(g) The expenses of any investigation held under section 235 or 237 in so far as they are payable by the company.

(c) Co-Insurance: In cases of large risks the business is shared between more than one insurer under co-insurance arrangements at agreed percentages. The leading insurer issues the documents, collects premium and settles claims. Statements of Account are rendered by the leading insurer to the other co-insurers. Accounting for premium, claims etc. under co-insurance is done in the same manner as that of the direct business except in respect of the following peculiar features.

Incoming co-insurance

(i) Premium: The co-insurer books the premium based on the statement received from the leading insurer usually by issuing dummy documents. Entries are made in the Premium Register from which the Premium Account is credited and the Leading Insurer Company's Account debited. In case the statement is not received, the premium is accounted for on the basis of advices to ensure that all premium in respect of risk assumed in any year is booked in the same year; share of premium relatable to further extension/endorsements on policies by the leading insurer are also accounted for on the basis of subsequent advices. Reference to the relevant communications should be made from the concerned companies to ensure that premium collected by them and attributable to the company is recorded.

(ii) Claims Paid: Normally, on the basis of claims paid, advices received from the leading insurer, the Claims Paid Account is debited with a credit to the co-insurer. All such advices are entered into the Claims Paid Register. It is a practice to treat all claims paid advices relating to the accounting year received upto 31st January of the subsequent year from leading insurer as claims paid.

Outgoing co-insurance: The share of the insurer only for both premium and claims has to be accounted under respective accounts. The share of other co-insurers is credited or debited, as the case may be, to their personal accounts and not routed through revenue accounts.

(d) Under fluctuating capital method, no current account is maintained. All such transactions and events are passed through capital accounts. Naturally, capital account balance of the partners fluctuates everytime. So in fixed capital method a fixed capital balance is maintained over a period of time while in fluctuating capital method, capital account balances fluctuate all the time.

(e) In actual practice, issue of shares are either under-or-over subscribed. When an issue is under-subscribed, entries are made on the basis of the shares applied for, provided the minimum subscription has been raised and the company can proceed to allotment. On the other hand, if an issue is over-subscribed, some applications may be rejected and application money refunded and in respect of others, only a part of the shares applied for may be allotted and the excess amount received can be utilized towards allotment or call money which has fallen or will soon fall due for payment. The entries are:

(1) On refund of application money to applicants to whom shares have not been allotted:

Share Application A/c	Dr.	
To Bank A/c		

(2) When only a part of shares applied for are allowed:

Share Application A/c	Dr.	(With the amount received in advance for allotment)
To Share Allotment A/c		
To Share Calls-in-Advance Account		

(f) In the case of partly paid-up shares, the dividend is payable either on the nominal, called-up or the paid-up amount of shares, depending on the provisions in this regard that there may be in the articles of the company. In the absence of any such provisions, Table A would be applicable. In such a case the amount of dividend payable will be calculated on the amount paid-up on the shares, and while doing so, the dates on which the amounts were paid must be taken into account. Calls paid in advance do not rank for payment of dividend. Instead, interest may be paid on such calls, the rate of interest is 6% p.a. according to Table A; Articles of a company may prescribe different rate. A company may if so authorised by its articles, pay a dividend in proportion to the amount paid on each share, where a larger amount is paid on some shares than on others (Section 93 of the Companies Act, 1956). But where the articles are silent and Table A has been excluded, the amount of dividend payable will have to be calculated on the nominal amount of shares. It should, however, be noted that according to Clause 88 of Table A dividends are to be declared and paid according to the amounts paid or credited as paid on the shares in respect whereof the dividend is paid, but if and so long as nothing is paid upon any of the shares of the company, dividends may be declared and paid according to the nominal amounts of the shares.

(g) In most cases policies are renewed annually except in some cases where policies are issued for a shorter period. Since insurers close their accounts on a particular date, not all risks under policies expire on that date. Many policies extend into the following year during which the risk continues. Therefore on the closing date, there is unexpired liability under various policies which may occur during the remaining term of the policy beyond the year and therefore, a provision for unexpired risks is made at normally 50% in case of Fire Insurance and 100% of in case of Marine Insurance. This Reserve is based on the net premium income earned by the insurance company during the year.

20. (a) When a partner is unable to pay his debts due to the firm, he is said to be insolvent and the share of loss is to be borne by other solvent partners in accordance with the decision in the English case of Garner vs Murray. According to this decision, the normal loss on realization of assets has to be borne by all partners (including insolvent partner) in the profit sharing ratio but a loss due to insolvency of a partner has to be borne by the solvent partners in the capital ratio.

The implications of this decision are that:

(1) the solvent partners in the first instance would bring in cash equal to the loss on realization debited to their respective capital accounts. Such a procedure would restore their capital accounts to the figures that stood prior to dissolution;

(2) the deficiency on the capital account of the insolvent partner (i.e. irrecoverable debit balance) should be divided between solvent partners in proportion to their capitals.

The fact of capital being fixed or fluctuating assumes great significance in such a situation. If they are maintaining capital at fixed amounts, insolvency loss is distributed in the ratio of fixed capitals. But if the capitals are not fixed and all transactions relating to drawings, profits, interest, etc., are passed through capital accounts, then capital ratio will be determined after adjusting all the reserves and accumulated profits to the date of dissolution, all drawings to the date of dissolution, interest on capital and on drawings to the date of dissolution but before adjusting profit or loss on realization account. If some partner is having a debit balance in his capital account and is not insolvent then he cannot be called upon to bear the loss on account of the insolvency of other partner.

(b) As per section 77A of the Companies Act, 1956 a joint stock company has to fulfill the following conditions to buy-back its own equity shares:

(a) The buy-back is authorised by its articles.

(b) A special resolution[*] has been passed in general meeting of the company authorising the buy-back.

(c) The buy-back does not exceed 25% of the total paid up capital and free reserves of the company. Provided the buy–back must not exceed 25% of its total paid up equity capital in that financial year.

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[*] If the buy-back by the company is or less than 10% of the total paid-up equity capital and free reserves of the company then it can be authorised by the Board by means of resolution passed at its meeting and no special resolution will be required.

(d) The ratio of the debt owed by the company is not more than twice the capital and its free reserves after such buy-back.

(e) All the shares for buy-back are fully paid up.

(f) The buy-back is made out of the free reserves (which include securities premium) or out of the proceeds of a fresh issue of any shares or other specified securities.

(g) The buy-back is completed within 12 months of the passing of the special resolution or a resolution passed by the Board.

(h) The buy-back of the shares listed on any recognised stock exchange is in accordance with the regulations made by the SEBI in this behalf.

(i) Before making such buy-back, a listed company has to file with the Registrar and the SEBI a declaration of solvency in the prescribed form.

21. (a) According to paragraph 38, 39 and 41 of AS 7, an enterprise should disclose in its financial statements:

(a) the amount of contract revenue recognised as revenue in the period;

(b) the methods used to determine the contract revenue recognised in the period; and

(c) the methods used to determine the stage of completion of contracts in progress.

An enterprise should also disclose the following for contracts in progress at the reporting date:

(a) the aggregate amount of costs incurred and recognised profits (less recognised losses) upto the reporting date;

(b) the amount of advances received; and

(c) the amount of retentions.

An enterprise should present:

(a) the gross amount due from customers for contract work as an asset; and

(b) the gross amount due to customers for contract work as a liability.

(b) A change in accounting policy is made only if the adoption of a different accounting policy is required by statute or for compliance with an accounting standard or if it is considered that the change would result in a more appropriate preparation or presentation of the financial statements of the enterprise. A more appropriate presentation of events or transactions in the financial statements occurs when the new accounting policy results in more relevant or reliable information about the financial position, performance or cash flows of the enterprise.

(c) Borrowing costs are interest and other costs incurred by an enterprise in connection with the borrowing of funds in the course of business. These costs normally include

(i) interest and commitment changes on bank borrowing and other short-term and long-term borrowings. (ii) Amortisation of discounts or premium relating to borrowing costs; (iii) Amortisation of ancillary cost incurred in connection with the arrangement of borrowings; (iv) Finance charges in respect of assets acquired under a finance lease or under other similar arrangements and; (v) Exchange differences arising from foreign currency borrowing to the extent they are regarded as an adjustment to interest costs.

Borrowing costs that are directly attributable to the acquisition, construction or particular of a qualifying asset have to be capitalized as part of cost of asset as per AS 16.

(d) For the purpose of calculating diluted earnings per share, the amount of net profit or loss for the period attributable to equity shareholders, as calculated in accordance with paragraph 11, should be adjusted by the following, after taking into account any attributable change in tax expense for the period:

(a) any dividends on dilutive potential equity shares which have been deducted in arriving at the net profit attributable to equity shareholders as calculated in accordance with paragraph 11;

(b) interest recognized in the period for the dilutive potential equity shares; and

(c) any other changes in expenses or income that would result from the conversion of the dilutive potential equity shares.

(e) For 'amalgamation in the nature of merger', all the following conditions should be satisfied:

(i) All the assets and liabilities of the transferor company become, after amalgamation, the assets and liabilities of the transferee company.

(ii) Shareholders holding not less than 90% of the face value of the equity shares of the transferor company (other than the equity shares already held therein, immediately before the amalgamation, by the transferee company or its subsidiaries or their nominees) become equity shareholders of the transferee company by virtue of the amalgamation.

(iii) The consideration for the amalgamation receivable by those equity shareholders of the transferor company who agree to become equity shareholders of the transferee company is discharged by the transferee company wholly by the issue of equity shares in the transferee company, except that cash may be paid in respect of any fractional shares.

(iv) The business of the transferor company is intended to be carried on, after the amalgamation, by the transferee company.

(v) No adjustment is intended to be made to the book values of the assets and liabilities of the transferor company when they are incorporated in the financial statements of the transferee company except to ensure uniformity of accounting policies.

(f) An increase in net book value arising on revaluation of fixed assets is normally credited directly to owner's interests under the heading of revaluation reserves and is regarded as not available for distribution. A decrease in net book value arising on revaluation of fixed assets is charged to profit and loss statement except that, to the extent that such a decrease is considered to be related to a previous increase on revaluation that is included in revaluation reserve, it is sometimes charged against that earlier increase. It sometimes happens that an increase to be recorded is a reversal of a previous decrease arising on revaluation which has been charged to profit and loss statement in which case the increase is credited to profit and loss statement to the extent that it offsets the previously recorded decrease.

(g) Events occurring after the balance sheet date are those significant events, both favourable and unfavourable, that occur between the balance sheet date and the date on which the financial statements are approved by the Board of Directors in the case of a company and in the case of any other entity by the corresponding approving authority.

   (i) Assets and liabilities should be adjusted for events occurring after the balance sheet date that provide additional evidence to assist the estimation of amounts relating to conditions existing at the balance sheet date or that indicate that the fundamental accounting assumption of going concern (i.e., the continuance of existence or substratum of the enterprise) is not appropriate. However, assets and liabilities should not be adjusted for but disclosure should be made in the report of the approving authority of events occurring after the balance sheet date that represent material changes and commitments affecting the financial position of the enterprise.

   (ii) Disclosure regarding events occurring after the balance sheet date :

      (a) The nature of the event;

      (b) An estimate of the financial effect, or a statement that such an estimate cannot be made.

(h) As per AS 19 on 'Leases', a sale and leaseback transaction involves the sale of an asset by the vendor and the leasing of the asset back to the vendor. The lease payments and the sale price are usually interdependent, as they are negotiated as a package. The accounting treatment of a sale and lease back transaction depends upon the type of lease involved.

   If a sale and leaseback transaction results in a finance lease, any excess or deficiency of sale proceeds over the carrying amount should be deferred and amortised over the lease term in proportion to the depreciation of the leased asset.

   If sale and leaseback transaction results in a operating lease, and it is clear that the transaction is established at fair value, any profit or loss should be recognised immediately. If the sale price is below fair value any profit or loss should be recognised immediately except that, if the loss is compensated by future lease payments at below market price, it should be deferred and amortised in proportion to the lease payments over the period for which the asset is expected to be used. If the sale price is above fair value, the excess over fair value should be deferred and amortised over the period for which the asset is expected to be used.

22. (a) The main considerations in selection of accounting policies is the presentation of true and fair picture. The financial picture presented by Balance Sheet and the net result shown by Profit & Loss Account should be true and fair. To ensure the true and fair consideration this statement issues following guidelines:

Prudence: As defined in the statement, prudence means recognising all losses immediately but ignoring anticipated profits. Business environment is highly dynamic, therefore, enterprises has to keep anticipate the future and take managerial decisions accordingly. This statement suggests that accounting policies should be such that no profit is recognised on the basis of anticipation but all anticipated losses are provided for.

For Example: If valuation of stock is always done at cost, consider a situation where market price of the relevant goods has reduced below the cost price, then valuing stock at cost price means ignoring anticipated losses. Similarly if stock is always valued at market price, then take a situation where cost price is below market price, indirectly we are recognising the anticipated gross profit on stock in the books. Therefore, accounting policy should be cost price or market price whichever is less, in this case we are ignoring anticipated profits (if any) but any anticipated losses would be taken care of.

Substance over form: While recording a transaction one should look into the substance of the transaction and not only the legal form of it.

For Example: The ownership of an asset purchased on hire purchase is not transferred till the payment of the last instalment is made but the asset is shown in the books of the hire purchaser. Similarly, in the case of the amalgamation, the entry for amalgamation in the books of the amalgamated company is recorded on the basis of the status of the shareholders of amalgamating company after amalgamation i.e. if all or almost all the shareholders of the amalgamated company has become shareholder of the amalgamating company by virtue of amalgamation, we record all the transactions as Amalgamation in nature of Merger otherwise it is recorded as Amalgamation in nature of Purchase.

Materiality: All the items which are material should be recorded. The materiality of an item is decided on the basis that whether non-disclosure of the item will effect the decision making of the user of accounts. If the answer is positive then the item is material and should be disclosed, in case answer is negative, item is immaterial. By this statement does not mean that immaterial item should not be disclosed, disclosure or non-disclosure of an immaterial item is left at the discretion of the accountant but disclosure of material item is been made mandatory.

For Example, Any penalty paid by the enterprise should be disclosed separately even though the amount paid is negligible, payment of any tax also should be disclosed separately and not to be merged with office expenses or miscellaneous expense.

(b) Inventories should be valued at the lower of cost and net realisable value. Cost of goods is the summation of:

(a) Cost of Purchase.

(b) Cost of Conversion.

(c) Other cost necessary to bring the inventory in present location and condition.

Finished goods should be valued at cost or market price whichever is lower, in other words, finished goods are valued at the lower of cost or net realisable value.

Cost has three elements as discussed below:

Cost of Purchase: Cost of purchase includes the purchase price plus all other necessary expenses directly attributable to purchase of stock like, taxes, duties, carriage inward, loading/unloading excluding expenses recoverable from the supplier. From the above sum, following items are deducted, duty drawback, CENVAT, VAT, trade discount, rebates.

Cost of Conversion: For a trading company cost of purchase along with other cost (discussed below) constitutes cost of inventory, but for a manufacturer cost of inventory also includes cost of conversion. Readers can recollect the calculation of factory cost calculated in Cost Accounting:

Direct Material + Direct Labour = Prime Cost

Prime Cost + Factory Variable Overhead + Factory Fixed Overhead = Factory Cost.

Direct material is included in cost of purchase and the rest items i.e. direct labour and overheads are termed as cost of conversion. Direct labour is cost of workers in the unit who are directly associated with the production process, in other words we can say that direct labour is the cost of labour which can be directly attributed to the units of production.

Overheads are indirect expenses. Variable overheads are indirect expenses which is directly related to production i.e., it changes with the change in production in the same proportion. Fixed overheads generally remains constant, it varies only there is some major shift in production.

Other Costs: Other costs are included in the cost of inventories only to the extent that they are incurred in bringing the inventories to their present location and condition. For example, it may be appropriate to include overheads other than production overheads or the costs of designing products for specific customers in the cost of inventories.

In determining the cost of inventories, it is appropriate to exclude the following costs and recognise them as expenses in the period in which they are incurred:

(a) Abnormal amounts of wasted materials, labour, or other production costs.

(b) Storage costs, unless those costs are necessary in the production process prior to a further production stage.

(c) Administrative overheads that do not contribute to bringing the inventories to their present location and condition and

(d) Selling and distribution costs.

(c) (i) Ordinary activities: Any activities which are undertaken by an enterprise as part of its business and such related activities in which the enterprise engages in furtherance of, incidental to, or arising from, these activities. For example profit on sale of merchandise, loss on sale of unsold stock at the end of the season.

(ii) Extraordinary items: Income or expenses that arise from events or transactions that are clearly distinct from the ordinary activities of the enterprise and, therefore, are not expected to recur frequently or regularly. For example, profit on sale of furniture or heavy loss of goods due to fire.

(d) Two broad approaches may be followed for the accounting treatment of government grants: the 'capital approach', under which a grant is treated as part of shareholders' funds, and the 'income approach', under which a grant is taken to income over one or more periods.

Those in support of the 'capital approach' argue as follows:

(i) Many government grants are in the nature of promoters' contribution, i.e., they are given by way of contribution towards its total capital outlay and no repayment is ordinarily expected in the case of such grants.

(ii) They are not earned but represent an incentive provided by government without related costs.

Arguments in support of the 'income approach' are as follows:

(i) The enterprise earns grants through compliance with their conditions and meeting the envisaged obligations. They should therefore be taken to income and matched with the associated costs which the grant is intended to compensate.

(ii) As income tax and other taxes are charges against income, it is logical to deal also with government grants, which are an extension of fiscal policies, in the profit and loss statement.

(iii) In case grants are credited to shareholders' funds, no correlation is done between the accounting treatment of the grant and the accounting treatment of the expenditure to which the grant relates.

It is generally considered appropriate that accounting for government grant should be based on the nature of the relevant grant. Grants which have the characteristics similar to those of promoters' contribution should be treated as part of shareholders' funds. Income approach may be more appropriate in the case of other grants.

(e) Paragraph 21 of Accounting Standard 23 on Accounting for Investments in Associates says that where the associate has a contingent liability , the investor has to disclose the following in the consolidated financial statements in accordance with AS 4:-

- Its share of the contingencies and capital commitments of an associate for which it is also contingently liable; and

- those contingencies that arise because the investor is severally liable for the liabilities of the associate.

(f) As per paragraph 25 of Accounting Standard 20 on Earnings Per Share:

"The theoretical ex-rights fair value per share is calculated by adding the aggregate fair value of the shares immediately prior to the exercise of the rights to the proceeds from the exercise of the rights, and dividing by the number of shares outstanding after the exercise of the rights. Where the rights themselves are to be publicly traded separately from the shares prior to the exercise date, fair value for the purposes of this calculation is established at the close of the last day on which the shares are traded together with the rights."

23. (a) Books of X: Agreement to sell has been entered on 20.12.2008 and he has received an advance of Rs. 50,000 on the same date. But the actual sale has taken place only on 15.1.2009 (next year). Though, the sale has taken place before approval of accounts, yet the profit of Rs. 1,20,000 (i.e. Rs. 3,70,000 – Rs. 2,50,000) need not be recognised in the financial statements for the year 2008. The amount received as advance shall be shown as a liability in the balance sheet and there should be an disclosure in Notes to Accounts about the agreement to sell. The profit should be recognized only in the year 2009, when it is actually realized.

Books of Y: He has paid an advance of Rs. 50,000 and it should be shown in the balance sheet. There should be a disclosure in the Notes to Accounts for the year 2008, that agreement for purchase of an asset at a price of Rs. 3,70,000 has been entered and an advance of Rs. 50,000 has been paid.

(b) It is prior period item. The error in the recoding of closing stock of the year ended 31.3.2007 have also resulted in overstatement of profits of the previous year, brought forward to the current year (2007-08). Hence, Rs. 20,000 should be deducted from opening stock in the profit and loss account and also charged as a prior-period item in the profit and loss account of the current year (2007-08) in accordance with AS 5 (Revised) which requires that the nature and amount of prior period items should be separately disclosed in the statement of profit and loss in a manner that their impact on the current profit or loss can be perceived.

(c) P Ltd. would be considered to control R Ltd. The definition of control, as per paragraph 10 of AS 18, includes ownership, directly or indirectly, of more than one-half of the voting power of another enterprise. As P Ltd. is a majority shareholder in Q Ltd., it has control over it. Further, as P Ltd. and Q Ltd. together are majority shareholders (i.e. 15% + 50%) in R Ltd. P Ltd. has indirect control over it.

Accordingly, P Ltd. has the ability to control R Ltd. indirectly, via the share ownership in Q Ltd. apart from its individual shareholding in R Ltd.

(d) The transfers should be made at lower of (a) Cost, and (b) Fair value at the date of transfer.

1. In this case, the transfer should be made at cost (being lower of Rs. 20 lakhs and Rs. 25 lakhs) and hence the long term investments should be carried at Rs. 20 lakhs.

2. In the second case, the transfer should be made at Market Value (being lower of Rs. 15 lakhs and Rs. 6.5 lakhs) and hence the long term investments should be carried at Rs. 6.50 lakhs. The loss of Rs. 15 – Rs. 6.5 = Rs. 8.5 lakhs should be provided for in the profit and loss account.

3. Here, the transfer should be made at carrying amount (being lower of Rs. 18 lakhs and Rs. 12 lakhs) and hence these reclassified current investments should be carried at Rs. 12 lakhs.

24. (a) As per para 12.1 of AS 10 on Accounting for Fixed Assets, expenditure that increases the future benefits from the existing asset beyond its previously assessed standard of performance is included in the gross book value, e.g., an increase in capacity. Hence, in the given case, Repairs amounting Rs. 5 lakhs and Partial replacement of roof tiles should be charged to profit and loss statement. Rs. 10 lakhs incurred for substantial improvement to the electrical writing system which will increase efficiency should be capitalized

(b) As per para 6 of AS 16 'Borrowing Costs', borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset should be capitalized as part of the cost of that asset. Other borrowing costs should be recognized as an expense in the period in which they are incurred. Borrowing costs should be expensed except where they are directly attributable to acquisition, construction or production of qualifying asset.

A qualifying asset is an asset that necessary takes a substantial period of time* to get ready for its intended use or sale.

The treatment for total interest amount of Rs. 52.20 lakhs can be given as:

Purpose	Nature	Interest to be charged to profit and loss account	Interest to be charged to profit and loss account
		Rs. in lakhs	Rs. in lakhs
Modernisation and renovation of plant and machinery	Qualifying asset	$**52.20 \times \frac{406}{580} = 36.54$	

Advance to supplies for additional assets	Qualifying asset	$^{**}52.20 \times \frac{58}{580} = 5.22$	
Working Capital	Not a qualifying asset		$52.20 \times \frac{116}{580} = 10.44$
		41.76	10.44

*Accounting Standards Interpretation (ASI) 1 deals with the meaning of expression 'substantial period of time'. A substantial period of time primarily depends on the facts and circumstances of each case. However, ordinarily, a period of twelve months is considered as substantial period of time unless a shorter or longer period can be justified on the basis of the facts and circumstances of the case.

** It is assumed in the above solution that the modernization and renovation of plant and machinery will take substantial period of time (i.e. more than twelve months). Regarding purchase of additional assets, the nature of additional assets has also been considered as qualifying assts. Alternatively, the plant and machinery and additional assets may be assumed to be non-qualifying assts on the basis that the renovation and installation of additional assets will not take substantial period of time. In that case, the entire amount of interest, Rs. 52.20 lakhs will be recognized as expense in the profit and loss account for year ended 31st March, 2008.

(c) Computation of Basic Earnings Per Share

(as per paragraphs 10 and 26 of AS 20 on Earnings Per Share)

	Year 2007 Rs.	Year 2008 Rs.
EPS for the year 2007 as originally reported		
$= \dfrac{\text{Net profit of the year attributable to equity shareholders}}{\text{Weighted average number of equity shares outstanding during the year}}$		
= (Rs. 20,00,000 / 10,00,000 shares)	2.00	
EPS for the year 2007 restated for rights issue		
= [Rs. 20,00,000 / (10,00,000 shares × 1.04*)]	1.92 (approx.)	

* Refer working note 2.

EPS for the year 2008 including effects of rights issue

$$\frac{\text{Rs. }30,00,000}{(10,00,000\text{ shares}\times 1.04\times 3/12)+(12,50,000\text{ shares}\times 9/12)}$$

$$\frac{\text{Rs. }30,00,000}{11,97,500\text{ shares}}$$ 2.51 (approx.)

Working Notes:

1. Computation of theoretical ex-rights fair value per share

$$\frac{\text{Fair value of all outstanding shares immediately prior to exercise of rights}+\text{Total amount received from exercise}}{\text{Number of shares outstanding prior to exercise}+\text{Number of shares issued in the exercise}}$$

$$=\frac{(\text{Rs. }25\times 10,00,000\text{ shares})+(\text{Rs. }20\times 2,50,000\text{ shares})}{10,00,000\text{ shares}+2,50,000\text{ shares}}$$

$$=\frac{\text{Rs. }3,00,00,000}{12,50,000\text{ shares}}=\text{Rs. }24$$

2. Computation of adjustment factor

$$=\frac{\text{Fair value per share prior to exercise of rights}}{\text{Theoretical ex - rights value per share}}$$

$$=\frac{\text{Rs. }25}{\text{Rs. }24\text{ (Refer Working Note 1)}}=1.04\text{ (approx.)}$$

(d) According to AS 29 'Provisions, Contingent Liabilities and Contingent Assets', contingent liability should be disclosed in the financial statements if following conditions are satisfied:

(i) There is a present obligation arising out of past events but not recognized as provision.

(ii) It is not probable that an outflow of resources embodying economic benefits will be required to settle the obligation.

(iii) The possibility of an outflow of resources embodying economic benefits is also remote.

(iv) The amount of the obligation cannot be measured with sufficient reliability to be recognized as provision.

In this case, the probability of winning of first five cases is 100% and hence, question of providing for contingent loss does not arise. The probability of winning of next ten cases is 60% and for remaining five cases is 50%. As per AS 29, we make a provision if the loss is probable. As the loss does not appear to be probable and the possibility of an outflow of resources embodying economic benefits is not remote rather there is reasonable possibility of loss, therefore disclosure by way of note should be made. For the purpose of the disclosure of contingent liability by way of note, amount may be calculated as under:

Expected loss in next ten cases = 30% of Rs. 1,20,000 + 10% of Rs. 2,00,000

= Rs. 36,000 + Rs. 20,000

= Rs. 56,000

Expected loss in remaining five cases = 30% of Rs. 1,00,000 + 20% of Rs. 2,10,000

= Rs. 30,000 + Rs. 42,000

= Rs. 72,000

To disclose contingent liability on the basis of maximum loss will be highly unrealistic. Therefore, the better approach will be to disclose the overall expected loss of Rs. 9,20,000 (Rs. 56,000 × 10 + Rs. 72,000 × 5) as contingent liability.

25. (a) Calculation of Profit/Loss on disposal of investment in subsidiary

Particulars	Rs.	Rs.
Net Assets of B Ltd. on the date of disposal		35,00,000
Less: Minority Interest (35 lacs x 20%)		7,00,000
A Ltd.'s Share in Net Assets		28,00,000
Proceeds from the sale of Investment		30,00,000
Less: A Ltd.'s share in net assets		28,00,000
		2,00,000
Less: Capital Reserve in the Consolidated Financial Statement		
A Ltd.'s Share in net asset on the date (22 lacs x 80%)	17,60,000	
Less: Cost of investment	15,00,000	2,60,000
Profit on sale of investment		4,60,000

(b) Present value of future cash flow

Year ended	Future Cash Flow	Discount @ 10% Rate	Discounted cash flow
31.3.2005	50	0.909	45.45
31.3.2006	30	0.826	24.78
31.3.2007	30	0.751	22.53
31.3.2008	20	0.683	13.66
31.3.2009	20	0.620	12.40
			118.82
Present value of residual price on 31.3.2009 = 5 × 0.620			3.10
Present value of estimated cash flow by use of an asset and residual value, which is called "value in use".			121.92

If net selling price of plant on 31.3.2004 is Rs. 60 lakhs, the recoverable amount will be higher of Rs. 121.92 lakhs (value in use) and Rs.60 lakhs (net selling price), hence recoverable amount is Rs.121.92 lakhs

(c) (i) Calculation of Annual Lease Payment*

	Rs.
Cost of the equipment	1,50,000
Unguaranteed Residual Value	20,000
PV of residual value for 3 years @ 10% (Rs.20,000 x 0.751)	15,020
Fair value to be recovered from Lease Payment (Rs.1,50,000 – Rs.15,020)	1,34,980
PV Factor for 3 years @ 10%	2.487
Annual Lease Payment (Rs. 1,34,980 / PV Factor for 3 years @ 10% i.e. 2.487)	54,275

(ii) Unearned Financial Income

Total lease payments [Rs. 54,275 x 3]	1,62,825
Add: Residual value	20,000
Gross Investments	1,82,825
Less: Present value of Investments (Rs.1,34,980 + Rs.15,020)	1,50,000
Unearned Financial Income	32,825

(iii) Segregation of Finance Income

Year	Lease Rentals Rs.	Finance Charges @ 10% on outstanding amount of the year Rs.	Repayment Rs.	Outstanding Amount Rs.
0	-	-	-	1,50,000
I	54,275	15,000	39,275	1,10,725
II	54,275	11,073	43,202	67,523
III	74,275**	6,752	67,523	--
	1,82,825	32,825	1,50,000	

(iv) Profit and Loss Account (Relevant Extracts)

Credit side		Rs.
I Year	By Finance Income	15,000
II year	By Finance Income	11,073
III year	By Finance Income	6,752

* Annual lease payments are considered to be made at the end of each accounting year.

** Rs. 74,275 includes unguaranteed residual value of equipment amounting Rs. 20,000.

Balance Sheet (Relevant Extracts)

Assets side	Rs.	Rs.
I year Lease Receivable	1,50,000	
Less: Amount Received	39,275	1,10,725
II year Lease Receivable	1,10,725	
Less: Received	43,202	67,523
III year :Lease Amount Receivable	67,523	
Less: Amount received	47,523	
Residual value	20,000	NIL

Notes to Balance Sheet

Year 1	Rs.
Minimum Lease Payments (54,275 + 54,275)	1,08,550
Residual Value	20,000
	1,28,550
Unearned Finance Income(11,073+ 6,752)	17,825
Lease Receivables	1,10,725
Classification:	
Not later than 1 year	43,202
Later than 1 year but not more than 5 years	67,523
Total	1,10,725
Year II:	
Minimum Lease Payments	54,275
Residual Value (Estimated)	20,000
	74,275
Unearned Finance Income	6,752
Lease Receivables (not later than 1year)	67,523
III Year:	
Lease Receivables (including residual value)	67,523
Amount Received	67,523
	NIL

Note: AS 1 to AS 29 are applicable for June, 2009 Examination

APPENDIX

Announcement

Withdrawal of the Announcement issued by the Council on ‘Treatment of exchange differences under Accounting Standard (AS) 11 (revised 2003), The Effects of Changes in Foreign Exchange Rates vis-à-vis Schedule VI to the Companies Act, 1956’

1. The Council of the Institute of Chartered Accountants of India had issued an Announcement on ‘Treatment of exchange differences under Accounting Standard (AS) 11 (revised 2003), The Effects of Changes in Foreign Exchange Rates vis-à-vis Schedule VI to the Companies Act, 1956’, which was published in the November 2003 issue of ‘The Chartered Accountant’ (pp. 497)[1]

2. Subsequent to the issuance of the above Announcement, the Ministry of Company Affairs (now known as the Ministry of Corporate Affairs) issued the Companies (Accounting Standards) Rules, 2006, by way of Notification in the Official Gazette dated 7th December, 2006. As per Rule 3(2) of the said Rules, the Accounting Standards shall come into effect in respect of accounting periods commencing on or after the publication of these accounting standards under the said Notification.

3. AS 11, as published in the above Government Notification, carries a footnote that “it may be noted that the accounting treatment of exchange differences contained in this Standard is required to be followed irrespective of the relevant provisions of Schedule VI to the Companies Act, 1956”.

4. In view of the above footnote to AS 11, the Council of the Institute of Chartered Accountants of India has decided at its 269th meeting held on July 18, 2007, to withdraw the Announcement on ‘Treatment of exchange differences under Accounting Standard (AS) 11 (revised 2003), The Effects of Changes in Foreign Exchange Rates vis-à-vis Schedule VI to the Companies Act, 1956’, published in ‘The Chartered Accountant’ of November 2003. Accordingly, the accounting treatment of exchange differences contained in AS 11 notified as above is applicable and not the requirements of Schedule VI to the Act, in respect of accounting periods commencing on or after 7th December, 2006.

Students are advised to refer the following rates of Non-Performing Assets in case of Banking Companies

Provisions

Taking into account the time lag between an account becoming doubtful of recovery, its recognition as such, the realisation of the security and the erosion over time in the value of security charged to the banks, it has been decided that banks should make provision against sub-standard assets, doubtful assets and loss assets on the following basis:

(a) Loss assets : The entire amount should be written off or full provision should be made for the amount outstanding.

(b) Doubtful assets : (i) Full provision to the extent of the unsecured portion should be made. In doing so, the realisable value of the security available to the bank should be determined on a realistic basis. DICGC/ECGC cover is also taken into account (this aspect is discussed later in this chapter). In case the advance covered by CGTSI guarantee becomes non-performing, no provision need be made towards the guaranteed portion. The amount outstanding in excess of the guaranteed portion should be provided for as per the extant guidelines on provisioning for non-performing advances.

(ii) Additionally, 20% - 100% of the secured portion should be provided for, depending upon the period for which the advance has been considered as a doubtful asset, as follows:

Period for which the advance has been considered as doubtful	% of provision on secured portion
Upto 1 year	20%
More than 1 year and upto 3 years	30%
More than three years	
i. Outstanding stock of NPA's as on 31.03.2004	60% w.e.f. 31.03.2005
	75% w.e.f. 31.03.2006
	100% w.e.f. 31.03.2007
ii. Advances classified as doubtful for more than three years on or after 01.04.2004	100% w.e.f. 31.03.2005

(iii) Banks are permitted to phase the additional provisioning consequent upon the reduction in the transition period from substandard to doubtful asset from 18 to 12 months over a four year period commencing from the year ending March 31, 2005, with a minimum of 20% each year.

(c) Sub-standard assets : A general provision of 10% on total outstanding should be made without making any allowance for DICGC/ECGC cover and securities available. An additional provision of 10% (i.e., total 20% of total outstanding) is required to be made on 'unsecured exposure' ab initio sanction of loan. Generally such a situation may arise in case of personal and education loans etc. Unsecured exposure is defined as 'an exposure where the realizable value of security is not more than 10% of the outstanding exposure (fund based and non-fund based). Security should not include guarantees, comfort letters etc

(d) Standard assets : A general provision of a minimum of 0.40% of total standard assets should be made. It has been clarified that the provision should be made on global loan portfolio basis and not on domestic advances alone.