

**PAPER 1: ADVANCED ACCOUNTING
NOVEMBER 2002**

Answer **all** questions.

Working notes should form part of your answer.

Wherever applicable, suitable assumptions should be made by the candidate.

Question 1

On 30th September, 1999 Beta Enterprises Ltd., was incorporated with an Authorized Capital of Rs.50 Lakhs. Its first accounts were closed on 31st March, 2000 by which time it had become a listed company with an issued subscribed and paid up Capital of Rs.40 Lakhs in 4,00,000 Equity Shares of Rs.10 each.

The company started off with two lines of business namely "Engineering Division" and "Chemical Division", with equal asset base with effect from 1st April, 2000. The "Ceramics Division" was added by the company on 1st April, 2001. The following data is gathered from the books of account of Beta Enterprises Ltd.,

(20 Marks)

Trial Balance as on 31st March, 2002

	(Rupees in 000's)	
	Dr.	Cr.
Engineering Division sales	--	6,000
Cost of engineering division sales	2,600	--
Chemicals division sales	--	8,000
Cost of sales of chemicals division	4,300	--
Ceramics division sales	--	1,500
Cost of sales of ceramics division	900	--
Administration costs	2,00	--
Distribution costs	1,500	--
Dividend - Interim	1,200	--
Fixed assets at cost	9,000	--
Depreciation on fixed assets	--	1,500
Stock on 31 st March, 2002	400	--
Trade debtors	440	--
Cash at Bank	160	--
Trade creditors	--	500
Equity share capital in shares of Rs.10 each	--	4,000
Retained profits	--	1,000
Total	22,500	22,500

Additional information:

- (i) Administration costs should be split between the Division in the ration of 5:3:2.
- (ii) Distribution costs should be spread over the Division in the ratio of 3:1:1.
- (iii) Directors have proposed a Final Dividend of Rs.8 Lakhs.
- (iv) Some of the users of Ceramics Division are unhappy with the product and have lodged claim against the company for damages of Rs.7.5 lakhs. The claim is hotly contested by the company on legal advice.
- (v) Fixed Assets worth Rs.30 lakhs were added in the Ceramics Division on 1.4.2001.
- (vi) Fixed Assets are written off over a period of 10 years on straight line basis in the books. However for Income Tax purposes depreciation at 20% on written down value of the assets is allowed by Tax Authorities.
- (vii) Income tax rate may be assumed at 35%.

- (viii) During the year Engineering Division has sold to Alpha Ltd., goods having a sales value of Rs.25 lakhs. Mr. Gamma, the Managing Director of Beta Enterprises Ltd., owns 100% of the issued Equity Shares of Alpha Ltd., The sales made to Alpha Ltd., were at normal selling price of Beta Enterprises Ltd.,

You are required to prepare Profit and Loss Account for the year ended 31st March, 2002 and the Balance Sheet as at that date. Your answer should include notes and disclosures as per Accounting Standards.

Question 2

- (a) Explain the concept of "Economic Value Added" (EVA for short) and its uses. **(6 Marks)**
- (b) The company obtained term loan during the year ended 31st March, 2002 in an extent of Rs.650 lakhs for modernization and development of its factory. Buildings worth Rs.120 lakhs were completed and plant and machinery worth Rs.350 lakhs were installed by 31st March, 2002. A sum of Rs.70 lakhs has been advanced for Assets the installation of which is expected in the following year. Rs.110 lakhs has been utilized for working capital requirements. Interest paid on the loan of Rs.650 lakhs during the year 2001-2002 amounted to Rs.58.50 lakhs. How should the interest amount be treated in the Accounts of the Company? **(6 Marks)**
- (c) For what purposes inspection of records and documents of Merchant Banker is ordered by SEBI? **(4 Marks)**

Question 3

The following are the Balance Sheet of A Ltd., and B Ltd., as on 31st December, 2001: **(16 Marks)**

Liabilities	A Ltd.,	B Ltd.,	Assets	A Ltd.,	B Ltd.,
	Rs.	Rs.		Rs.	Rs.
Share Capital			Fixed Assets	7,00,000	2,50,00
Equity shares of Rs.10 each	6,00,000	3,00,000	Investment:		
10% Pref. Shares of Rs.100 each	2,00,000	1,00,000	6,000 shares in B Ltd.,	80,000	--
Reserved and surplus	3,00,000	2,00,000	5,000 shares in A Ltd.,	--	80,000
Secured Loans:			Current Assets:		
12% Debentures	2,00,000	1,50,000	Stock	2,40,000	3,20,000
Current liabilities:			Debtors	3,60,000	1,90,000
Sundry Creditors	2,20,000	1,25,000	Bills Receivable	60,000	20,000
Bills payable	30,000	25,000	Cash at Bank	1,10,000	40,000
	15,50,000	9,00,000		15,50,000	9,00,000

Fixed Assets of both the companies are to be revalued at 15% above book value. Stock in trade and Debtors are taken over at 5 % lesser than their book value. Both the companies are to pay 10% Equity dividend. Preference dividend having been already paid.

After the above transactions are given effect to, A Ltd., will absorb B Ltd, on the following terms:

- 8 Equity shares of Rs.10 each will be issued by A Ltd., at part against 6 shares of B Ltd.,
- 10% Preference shareholders of B Ltd., will be paid at 10% discount by issue of 10% preference shares of Rs.100 each at part in A Ltd.,
- 12% Debenture holders of B Ltd., are to be paid at 8% premium by 12% Debentures in A LTD., issued at a discount of 10%
- Rs.30,00 is to be paid by A Ltd., to B Ltd., for Liquidation expenses. Sundry creditors of B L td., include Rs.10,000 due to A Ltd.,

Prepare:

- Absorption entries in the books of A Ltd.,
- Statement of consideration payable by A Ltd.,

Question 4

(a) Following are the information of two companies for the year ended 31st March, 2002 **(12 Marks)**

Particulars	Company A	Company B
Equity Shares of Rs.10 each	8,00,000	10,00,000
10% Pref. Shares of Rs.10 each	6,00,000	4,00,000
Profit after tax	3,00,000	3,00,000

Assume the Market expectation is 18% and 80% of the Profits are distributed.

- (i) What is the rate you would pay to the Equity Shares of each Company?
 (a) If you are buying a small lot.
 (b) If you are buying controlling interest shares.
- (ii) If you plan to invest only in preference shares which company's preference shares would you prefer?
- (iii) Would your rates be different for buying small lot, if the company "A" retains 30% and company "B" 10% of the Profits?
- (b) Write short notes on recommendations given in the Guidance Note on Accounting in respect of Minimum Alternate Tax (MAT) issued by Institute of Chartered Accountants of India. **(4 Marks)**

Question 5

On 31st March, 2002, the Balance Sheets of H Ltd., and S Ltd., stood as follows: **(16 Marks)**

	H Ltd., (Rs. In 000's)	S Ltd.,
Liabilities :		
Equity Share Capital – Authorized	5,000	3,000
Issued and subscribed in Equity Shares of Rs.10 each fully paid	4,000	2,400
General Reserve	928	690
Profit and Loss Account	1,305	810
Bills Payable	124	80
Sundry Creditors	487	427
Provision for Taxation	220	180
Other Provisions	65	17
Total	7,129	4,604
Assets :		
Plant and Machinery	2,541	2,450
Furniture and Fittings	615	298
Investment in the Equity Shares of S Ltd.,	1,500	--
Stock	983	786
Debtors	700	683
Bills Receivables	120	95
Cash and Bank Balances	410	102
Sundry Advances	260	190
Total	7,129	4,604

Following Additional Information is available:

- a. H Ltd., purchased 90 thousand Equity Shares in S Ltd., on 1st April, 2001 at which date the following balances stood in the books of S Ltd.,
- General Reserve Rs.1,500 thousand ; Profit and Loss Account Rs.633 thousand.
- b. On 14th July, 2001 S Ltd., declared a dividend of 20% out of pre-acquisition profits and paid corporate dividend tax (including surcharge) at 11% H Ltd., credited the dividend received to its profit and loss account.

- c. On 1st November, 2001 S Ltd., issued 3 fully paid Equity Shares of Rs.10 each, every 5 shares held as bonus shares out of pre-acquisition General Reserve.
- d. On 31st March, 2002, the stock of S Ltd., included goods purchased for Rs.50 thousand from H Ltd., which had made a profit of 25% on cost.

Prepare a consolidated Balance Sheet as on 31st March, 2002.

Question 6

In the context of relevant Accounting Standard, give you comments on any four of the following matters for the financial year ending on 31.3.2002 **(4×4=16 Marks)**

- (a) Assets and liabilities and income and expenditure items in respect of foreign branches are translated into Indian Rupees at the prevailing rate of exchange at the end of the year. The resultant exchange differences in the case of profit, is carried to other liabilities account and the loss, if any, is charged to revenue.
- (b) Leave encashment benefit is accounted for as per “Pay-as – you-go” method.
- (c) Increase in pension liability on account of wage revision in 1999-2000 is being provided for in 5 instalments commencing from that year. The remaining liability of Rs.300 lakhs as re-determined in actuarial valuation will be provided for in the next 2 years.
- (d) A Pharma Company spent Rs.33 lakhs during the accounting year ended 31st March, 2002 on a research project to develop a drug to treat “AIDS”. Experts are of the view that it may take four years to establish whether the drug will be effective or not and even if found effective it may take two to three more years to produce the medicine, which can be marketed. The company wants to treat the expenditure as deferred revenue expenditure.
- (e) While preparing its final accounts for the year ended 31st March, 2002 Rainbow Limited created a provision for Bad and Doubtful debts at 2% on trade debtors. A few weeks later the company found that payments from some of the major debtors were not forthcoming. Consequently the company decided to increase the provision by 10% on the debtors as on 31st March, 2002 as the accounts were still open awaiting approval of the Board of Directors. Is this to be considered as an extra-ordinary item or prior period item?