

## PAPER – 1 : ADVANCED ACCOUNTING

Answer **all** questions.

Working notes should form part of the answer.

### Question 1

On 31st March, 2004 Bee Ltd. became the holding company of Cee Ltd. and Dee Ltd. by acquiring 450 lakhs fully paid shares in Cee Ltd. for Rs. 6,750 lakhs and 240 lakhs fully paid shares in Dee Ltd. for Rs. 2,160 lakhs. On that date, Cee Ltd. showed a balance of Rs. 2,550 lakhs in General Reserve and a credit balance of Rs. 900 lakhs in Profit and Loss Account. On the same date, Dee Ltd. showed a debit balance of Rs. 360 lakhs in Profit and Loss Account while its Preliminary Expenses Account showed a balance of Rs. 30 lakhs.

After one year, on 31st March, 2005 the Balance Sheets of three companies stood as follows:

|                                         | (All amounts in lakhs of Rupees) |               |              |
|-----------------------------------------|----------------------------------|---------------|--------------|
| Liabilities                             | Bee Ltd.                         | Cee Ltd.      | Dee Ltd.     |
| Fully paid equity shares of Rs. 10 each | 27,000                           | 7,500         | 3,000        |
| General Reserve                         | 33,000                           | 3,150         | —            |
| Profit and Loss Account                 | 9,000                            | 1,200         | 750          |
| 15 lakh fully paid 9.5%                 |                                  |               |              |
| Debentures of Rs. 100 each              | —                                | —             | 1,500        |
| Loan from Cee Ltd.                      | —                                | —             | 75           |
| Bills Payable                           | —                                | —             | 150          |
| Sundry Creditors                        | <u>14,100</u>                    | <u>2,700</u>  | <u>930</u>   |
|                                         | <u>83,100</u>                    | <u>14,550</u> | <u>6,405</u> |

|                                | (All amounts in lakhs of Rupees) |          |          |
|--------------------------------|----------------------------------|----------|----------|
| Assets                         | Bee Ltd.                         | Cee Ltd. | Dee Ltd. |
| Machinery                      | 39,000                           | 7,500    | 2,100    |
| Furniture and Fixtures         | 6,000                            | 1,500    | 600      |
| Investments:                   |                                  |          |          |
| 450 lakhs shares in Cee Ltd.   | 6,750                            | —        | —        |
| 240 lakhs shares in Dee Ltd.   | 2,160                            | —        | —        |
| 3 lakhs debentures in Dee Ltd. | 294                              | —        | —        |
| Stocks                         | 16,500                           | 3,000    | 1,500    |
| Sundry Debtors                 | 9,000                            | 1,350    | 1,290    |

|                        |               |               |              |
|------------------------|---------------|---------------|--------------|
| Cash and Bank balances | 3,201         | 1,050         | 900          |
| Loan to Dee Ltd.       | —             | 90            | —            |
| Bills Receivable       | 195           | 60            | —            |
| Preliminary Expenses   | —             | —             | 15           |
|                        | <u>83,100</u> | <u>14,550</u> | <u>6,405</u> |

The following points relating to the above mentioned Balance Sheets are to be noted:

- (i) All the bills payable appearing in Dee Ltd.'s Balance Sheet were accepted in favour of Cee Ltd. out of which bills amounting to Rs. 75 lakhs were endorsed by Cee Ltd. in favour of Bee Ltd. and bills amounting to Rs. 45 lakhs had been discounted by Cee Ltd. with its bank.
- (ii) On 29th March, 2005 Dee Ltd. remitted Rs. 15 lakhs by means of a cheque to Cee Ltd. to return part of the loan; Cee Ltd. received the cheque only after 31st March, 2005.
- (iii) Stocks with Cee Ltd. includes goods purchased from Bee Ltd. for Rs. 200 lakhs. Bee Ltd. invoiced the goods at cost plus 25%.
- (iv) In August, 2004 Cee Ltd. declared and distributed dividend @ 10% for the year ended 31st March, 2004. Bee Ltd. credited the dividend received to its Profit and Loss Account.

You are required to prepare a Consolidated Balance Sheet of Bee Ltd. and its subsidiaries Cee Ltd. and Dee Ltd. as at 31st March, 2005. (16 Marks)

### Answer

#### Consolidated Balance Sheet of Bee Ltd. and its subsidiaries Cee Ltd. and Dee Ltd. as at 31st March, 2005

| Liabilities                             | Rs. in lakhs | Assets                                 | Rs. in lakhs     |
|-----------------------------------------|--------------|----------------------------------------|------------------|
| Share Capital                           |              | Fixed Assets                           |                  |
| Authorised                              | ?            | Goodwill (W.N. 3)                      | 246              |
| Issued and subscribed                   |              | Machinery                              | 48,600           |
| Fully paid equity shares of Rs. 10 each | 27,000       | Furniture and Fixtures                 | 8,100            |
| Minority interest (W.N. 2)              | 5,487        | Current Assets, Loans<br>and Advances: |                  |
| Reserves and Surplus                    |              | (A) Current Assets                     |                  |
| General Reserve (W.N. 4)                | 33,360       | Stock                                  | 21,000           |
| Profit and Loss A/c (W.N. 4)            | 10,040       | Less: Unrealised profit                | <u>40</u> 20,960 |
| Secured Loans                           |              | Sundry debtors                         | 11,640           |
| Debentures                              | 1,200        | Cash and bank balances                 | 5,151            |

|                            |            |               |                              |               |
|----------------------------|------------|---------------|------------------------------|---------------|
| <i>Current Liabilities</i> |            |               | Cash in transit              | 15            |
| Acceptances                | 150        |               | (B) <i>Loan and Advances</i> |               |
| Less: Mutual owing         | <u>105</u> | 45            | Bills receivable             | 255           |
| Sundry creditors           |            | <u>17,730</u> | Less: Mutual owing (W.N. 5)  | <u>105</u>    |
|                            |            | <u>94,862</u> |                              | <u>94,862</u> |

**Working Notes:**1. *Analysis of reserves and profits of subsidiaries:*

|                                      |            | <i>Pre-acquisition<br/>capital profit</i> | <i>Post-acquisition<br/>General<br/>Reserve</i> | <i>Rs. in lakhs<br/>Profit and Loss<br/>Account</i> |
|--------------------------------------|------------|-------------------------------------------|-------------------------------------------------|-----------------------------------------------------|
| <b>Cee Ltd.</b>                      |            |                                           |                                                 |                                                     |
| General reserve                      |            | 2,550                                     | 600                                             |                                                     |
| Profit and loss account on 31.3.2004 | 900        |                                           |                                                 |                                                     |
| Less: Dividend                       | <u>750</u> | <u>150</u>                                | <u>—</u>                                        | <u>1,050</u>                                        |
|                                      |            | <u>2,700</u>                              | <u>600</u>                                      | <u>1,050</u>                                        |
| Share of Bee Ltd. (60%)              |            | 1,620                                     | 360                                             | 630                                                 |
| Minority interest (40%)              |            | 1,080                                     | 240                                             | 420                                                 |

|                         |  | <i>Pre-acquisition<br/>capital profit</i> | <i>Post-acquisition<br/>Preliminary<br/>Expenses<br/>written off</i> | <i>Rs. in lakhs<br/>Profit and Loss<br/>Account</i> |
|-------------------------|--|-------------------------------------------|----------------------------------------------------------------------|-----------------------------------------------------|
| <b>Dee Ltd.</b>         |  |                                           |                                                                      |                                                     |
| Profit and loss account |  | (360)                                     |                                                                      | 1,110                                               |
| Preliminary expenses    |  | <u>(30)</u>                               | <u>15</u>                                                            | <u>—</u>                                            |
| Less: Dividend          |  | <u>(390)</u>                              | <u>15</u>                                                            | <u>1,110</u>                                        |
| Share of Bee Ltd. (80%) |  | (312)                                     | 12                                                                   | 888                                                 |
| Minority interest (20%) |  | (78)                                      | 3                                                                    | 222                                                 |

2 . *Minority Interest**(Rs. in lakhs)***Cee Ltd.**

|                                     |            |              |       |
|-------------------------------------|------------|--------------|-------|
| Share capital                       |            | 3,000        |       |
| Capital (pre-acquisition) profits   | 1,080      |              |       |
| Revenue (post-acquisition) profits: |            |              |       |
| General reserve                     | 240        |              |       |
| Profit and loss account             | <u>420</u> | <u>1,740</u> | 4,740 |

**Dee Ltd.**

|                                            |          |            |              |
|--------------------------------------------|----------|------------|--------------|
| Share capital                              |          | 600        |              |
| Capital (pre-acquisition) profits/(losses) | (78)     |            |              |
| Revenue (post-acquisition) profits         | 222      |            |              |
| Add: Preliminary expenses written off      | <u>3</u> | <u>225</u> | <u>147</u>   |
|                                            |          |            | <u>747</u>   |
|                                            |          |            | <u>5,487</u> |

3. *Cost of Control**(Rs. in lakhs)***Cee Ltd.**

|                                                                            |              |              |     |
|----------------------------------------------------------------------------|--------------|--------------|-----|
| Investment                                                                 | 6,750        |              |     |
| Less: Dividend received and wrongly credited to<br>profit and loss account | <u>450</u>   | 6,300        |     |
| Less: Paid-up share capital (60%)                                          | 4,500        |              |     |
| Capital profits                                                            | <u>1,620</u> | <u>6,120</u> | 180 |

**Dee Ltd.**

|                                   |              |              |            |
|-----------------------------------|--------------|--------------|------------|
| Investment in shares              | 2,160        |              |            |
| in debentures                     | <u>294</u>   | 2,454        |            |
| Less: Paid-up share capital (80%) | 2,400        |              |            |
| Nominal value of debentures       | 300          |              |            |
| Capital profits                   | <u>(312)</u> | <u>2,388</u> | <u>66</u>  |
| Cost of control - Goodwill        |              |              | <u>246</u> |

## 4. Consolidated general reserve and profit and loss account

|                                  | General reserve | Profit and loss account |
|----------------------------------|-----------------|-------------------------|
| Bee Ltd.                         | 33,000          | 9,000                   |
| Less: Wrong dividend credited    | <u>—</u>        | <u>450</u>              |
|                                  | 33,000          | 8,550                   |
| Cee Ltd.                         | 360             | 630                     |
| Dee Ltd. (888 + 12)              | <u>—</u>        | <u>900</u>              |
|                                  | 33,360          | 10,080                  |
| Less: Unrealised profit on stock | <u>—</u>        | <u>40</u>               |
|                                  | <u>33,360</u>   | <u>10,040</u>           |

## 5. Mutual owing regarding bills

Rs. (150 – 45) lakhs = Rs. 105 lakhs.

## 6. Unrealised profit

$$\left( \text{Rs. } 200 \times \frac{25}{125} \right) \text{ lakhs} = \text{Rs. } 40 \text{ lakhs}$$

## 7. Amount of dividend wrongly credited to profit and loss account by Bee Ltd.

60% of Rs. 750 lakhs = Rs. 450 lakhs.

**Question 2**

- (a) On the basis of the following Profit and Loss Account of Zed Limited and the supplementary information provided thereafter, prepare Gross Value Added Statement of the company for the year ended 31st March, 2005. Also prepare another statement showing reconciliation of Gross Value Added with Profit before Taxation.

Profit and Loss Account of Zed Limited for the year ended 31st March, 2005.

|                                     | Amount<br>(Rs. in lakhs) | Amount<br>(Rs. in lakhs) |
|-------------------------------------|--------------------------|--------------------------|
| <b>Income</b>                       |                          |                          |
| Sales                               |                          | 5,010                    |
| Other Income                        |                          | <u>130</u>               |
|                                     |                          | 5,140                    |
| <b>Expenditure</b>                  |                          |                          |
| Production and Operational Expenses | 3,550                    |                          |
| Administrative Expenses             | 185                      |                          |
| Interest                            | 235                      |                          |
| Depreciation                        | <u>370</u>               | <u>4,340</u>             |

|                                                 |            |
|-------------------------------------------------|------------|
| <i>Profit before Taxation</i>                   | 800        |
| <i>Provision for Taxation</i>                   | <u>280</u> |
| <i>Profit after Taxation</i>                    | 520        |
| <i>Credit Balance as per last Balance Sheet</i> | <u>40</u>  |
|                                                 | <u>560</u> |

**Appropriations**

|                                             |            |
|---------------------------------------------|------------|
| <i>Transfer to General Reserve</i>          | 100        |
| <i>Preference Dividend (Interim) paid</i>   | 50         |
| <i>Proposed Preference Dividend (Final)</i> | 50         |
| <i>Proposed Equity Dividend</i>             | 300        |
| <i>Balance carried to Balance Sheet</i>     | <u>60</u>  |
|                                             | <u>560</u> |

**Supplementary Information**

*Production and Operational Expenses consist of:*

|                                          |              |
|------------------------------------------|--------------|
| <i>Raw Materials and Stores consumed</i> | 1,900        |
| <i>Wages, Salaries and Bonus</i>         | 610          |
| <i>Local Taxes including Cess</i>        | 220          |
| <i>Other Manufacturing Expenses</i>      | <u>820</u>   |
|                                          | <u>3,550</u> |

**Administrative Expenses consist of:**

|                                             |            |
|---------------------------------------------|------------|
| <i>Salaries and Commission to Directors</i> | 60         |
| <i>Audit Fee</i>                            | 24         |
| <i>Provision for Bad and Doubtful Debts</i> | 20         |
| <i>Other Administrative Expenses</i>        | <u>81</u>  |
|                                             | <u>185</u> |

**Interest is on:**

|                                           |            |
|-------------------------------------------|------------|
| <i>Loan from Bank for Working Capital</i> | 35         |
| <i>Debentures</i>                         | <u>200</u> |
|                                           | <u>235</u> |

- (b) The Institute for Global Management Research maintains a combined Development Fund in respect of which the following information is available for the year ended 31st March, 2005:

|                                                                      |                 |
|----------------------------------------------------------------------|-----------------|
|                                                                      | Rs.             |
| <i>Government. Grants received for acquisition of land</i>           | 60,00,000       |
| <i>Private Grants received for construction of buildings</i>         | 30,00,000       |
| <i>Foreign Private Grant for purchase of computing equipment USD</i> | <u>5,00,000</u> |
| <i>Transfer from unrestricted fund for purchase of furniture</i>     | 10,00,000       |
| <i>Cost of assets so far acquired:</i>                               |                 |

|                                                 |           |
|-------------------------------------------------|-----------|
| Land                                            | 59,00,000 |
| Buildings in progress (payments to Contractors) | 15,00,000 |
| Furniture                                       | 3,00,000  |

The USD grant has been received into a bank account in USA on 29.3.2005 and is expected to be utilized therefrom for purchases to be made abroad. The rate of exchange on 31.3.2005 is 1 USD = Rs. 44.

You are required to prepare

- A Statement showing changes in the Development Fund for the year; and
- Balance Sheet of the Development Fund as at 31.3.2005. (12 + 8 = 20 Marks)

**Answer**

**(a) Gross Value Added Statement of Zed Ltd.  
for the year ended 31st March, 2005**

|                                                                               | Rs. in lakhs | Rs. in lakhs |
|-------------------------------------------------------------------------------|--------------|--------------|
| Sales                                                                         |              | 5,010        |
| Less: Cost of raw materials, stores and other services consumed (1,900 + 820) | 2,720        |              |
| Administrative expenses (185 – 60)                                            | 125          |              |
| Interest on loan from bank for working capital                                | <u>35</u>    | <u>2,880</u> |
| Value added by manufacturing and trading activities                           |              | 2,130        |
| Add: Other income                                                             |              | <u>130</u>   |
| Total value added                                                             |              | <u>2,260</u> |

**Application of Value Added**

|                                      | Rs.in lakhs | Rs. in lakhs | %     |
|--------------------------------------|-------------|--------------|-------|
| To pay employees                     |             |              |       |
| Wages, salaries and bonus            |             | 610          | 26.99 |
| To pay directors                     |             |              |       |
| Salaries and commission to Directors |             | 60           | 2.66  |
| To pay Government                    |             |              |       |
| Local taxes including cess           | 220         |              |       |
| Income tax                           | <u>280</u>  | 500          | 22.12 |
| To pay providers of capital          |             |              |       |
| Interest on debentures               | 200         |              |       |
| Preference dividend                  | 100         |              |       |
| Equity dividend                      | <u>300</u>  | 600          | 26.55 |

To provide for the maintenance and expansion of the company:

|                                     |           |              |              |
|-------------------------------------|-----------|--------------|--------------|
| Depreciation                        | 370       |              |              |
| Transfer to general reserve         | 100       |              |              |
| Retained profits Rs.(60 – 40) lakhs | <u>20</u> | <u>490</u>   | <u>21.68</u> |
|                                     |           | <u>2,260</u> | <u>100</u>   |

**Statement showing Reconciliation between  
Gross Value Added with Profit before Taxation**

|                                      | <i>Rs. in lakhs</i> | <i>Rs. in lakhs</i> |
|--------------------------------------|---------------------|---------------------|
| Profit before taxation               |                     | 800                 |
| <i>Add back:</i>                     |                     |                     |
| Wages, salaries and bonus            | 610                 |                     |
| Salaries and commission to Directors | 60                  |                     |
| Local taxes including cess           | 220                 |                     |
| Interest on debentures               | 200                 |                     |
| Depreciation                         | <u>370</u>          | <u>1,460</u>        |
| Gross Value Added                    |                     | <u>2,260</u>        |

**(b) The Institute for Global Management Research  
Statement of Changes in Development Fund**

|                                         | <i>Rs.</i>       | <i>Rs.</i>         |
|-----------------------------------------|------------------|--------------------|
| <i>Receipts</i>                         |                  |                    |
| Government grants                       | 60,00,000        |                    |
| Private grants                          | 30,00,000        |                    |
| Foreign private grant (in USD 5,00,000) | 2,20,00,000      |                    |
| Transfer from unrestricted fund         | <u>10,00,000</u> | 3,20,00,000        |
| <i>Deductions/Transfers</i>             |                  |                    |
| Cost of land acquired                   | 59,00,000        |                    |
| Furniture purchased                     | <u>3,00,000</u>  | <u>62,00,000</u>   |
| Balance as at 31.3.2005                 |                  | <u>2,58,00,000</u> |



**Development Fund**  
**Balance Sheet as at 31.3.2005**

| <i>Liabilities</i> | <i>Rs.</i>         | <i>Assets</i>         | <i>Rs.</i>         |
|--------------------|--------------------|-----------------------|--------------------|
| Fund balance       | 2,58,00,000        | Buildings in progress | 15,00,000          |
|                    |                    | Bank balances         |                    |
|                    |                    | in India              | 23,00,000          |
|                    |                    | outside India         | <u>2,20,00,000</u> |
|                    | <u>2,58,00,000</u> |                       | <u>2,43,00,000</u> |
|                    |                    |                       | <u>2,58,00,000</u> |

**Working Note:****Bank Account (in India)**

|                     | <i>Rs.</i>         |                                          | <i>Rs.</i>         |
|---------------------|--------------------|------------------------------------------|--------------------|
| To Government grant | 60,00,000          | By Land                                  | 59,00,000          |
| To Private grant    | 30,00,000          | By Furniture                             | 3,00,000           |
| To Transfer         | 10,00,000          | By Payments to contractors for buildings | 15,00,000          |
|                     |                    | By Balance c/d                           | <u>23,00,000</u>   |
|                     | <u>1,00,00,000</u> |                                          | <u>1,00,00,000</u> |

**Question 3**

*The following abridged Balance Sheet as at 31st March, 2005 pertains to Glorious Ltd.*

| <i>Liabilities</i>                                   | <i>Rs. in lakhs</i> | <i>Assets</i>                    | <i>Rs. in lakhs</i> |
|------------------------------------------------------|---------------------|----------------------------------|---------------------|
| <i>Share Capital:</i>                                |                     | <i>Goodwill, at cost</i>         | 420                 |
| 180 lakh Equity shares of Rs. 10 each, fully paid up | 1,800               | <i>Other Fixed Assets</i>        | 11,166              |
| 90 lakh Equity shares of Rs. 10 each, Rs. 8 paid up  | 720                 | <i>Current Assets</i>            | 2,910               |
| 150 lakh Equity shares of Rs. 5 each, fully paid-up  | 750                 | <i>Loans and Advances</i>        | 933                 |
| <i>Reserves and Surplus</i>                          | 5,628               | <i>Miscellaneous Expenditure</i> | 171                 |
| <i>Secured Loans</i>                                 | 4,500               |                                  |                     |
| <i>Current Liabilities</i>                           | 1,242               |                                  |                     |
| <i>Provisions</i>                                    | <u>960</u>          |                                  |                     |
|                                                      | <u>15,600</u>       |                                  | <u>15,600</u>       |

You are required to calculate the following for each one of the three categories of equity shares appearing in the above mentioned Balance Sheet:

- (i) Intrinsic value on the basis of book values of Assets and Liabilities including goodwill;
- (ii) Value per share on the basis of dividend yield.

Normal rate of dividend in the concerned industry is 15%, whereas Glorious Ltd. has been paying 20% dividend for the last four years and is expected to maintain it in the next few years; and

- (iii) Value per share on the basis of EPS.

For the year ended 31st March, 2005 the company has earned Rs. 1,371 lakh as profit after tax, which can be considered to be normal for the company. Average EPS for a fully paid share of Rs. 10 of a Company in the same industry is Rs. 2. (16 Marks)

#### Answer

| (i) Intrinsic value per share on the basis of book values      | Rs. in lakhs | Rs. in lakhs |
|----------------------------------------------------------------|--------------|--------------|
| Goodwill                                                       |              | 420          |
| Other Fixed Assets                                             |              | 11,166       |
| Current Assets                                                 |              | 2,910        |
| Loans and Advances                                             |              | <u>933</u>   |
|                                                                |              | 15,429       |
| Less: Secured loans                                            | 4,500        |              |
| Current liabilities                                            | 1,242        |              |
| Provisions                                                     | <u>960</u>   | <u>6,702</u> |
|                                                                |              | 8,727        |
| Add: Notional call on 90 lakhs equity shares @ Rs. 2 per share |              | <u>180</u>   |
|                                                                |              | <u>8,907</u> |

$$\text{Value per equivalent share of Rs.10 each} = \frac{\text{Rs.8,907 lakhs}}{345 * \text{lakhs shares}} = \text{Rs.25.82 (approx)}$$

Hence, intrinsic values of each equity share are as follows:

Value of fully paid-up share of Rs. 10 = Rs. 25.82

Value of partly paid-up share of Rs. 8 = Rs. 25.82 – Rs. 2 = Rs. 23.82

Value of fully paid-up share of Rs. 5 =  $\text{Rs.25.82} \times \frac{5}{10} = \text{Rs.12.91}$

\*Calculation of equivalent number of equity shares of Rs. 10 each:

|                                                                                                                  | <i>Shares in lakhs</i> |
|------------------------------------------------------------------------------------------------------------------|------------------------|
| Fully paid shares of Rs. 10 each                                                                                 | 180                    |
| Partly-paid shares after notional call                                                                           | 90                     |
| Fully paid shares of Rs. 5 each, $\left[ \frac{\text{Rs. 150 lakhs}}{\text{Rs. 10}} \times \text{Rs. 5} \right]$ | <u>75</u>              |
|                                                                                                                  | <u>345</u>             |

**(ii) Value per share on dividend yield basis:**

Value of fully paid-up share of Rs. 10 =  $\frac{20}{15} \times \text{Rs. 10} = \text{Rs. 13.33}$  (approx)

Value of partly paid-up share of Rs. 8 =  $\frac{20}{15} \times \text{Rs. 8} = \text{Rs. 10.67}$  (approx)

Value of fully paid-up share of Rs. 5 =  $\frac{20}{15} \times \text{Rs. 5} = \text{Rs. 6.67}$  (approx)

**(iii) Value per share on the basis of EPS:**

Profit after tax = Rs. 1,371 lakhs

Total share capital = Rs. (1,800 + 720 + 750) lakhs = Rs. 3,270 lakhs

Earning per rupee of share capital = Rs.  $\frac{1,371 \text{ lakhs}}{3,270 \text{ lakhs}} = \text{Re. 0.419}$  (approx)

Earning per fully paid share of Rs. 10 = Re.  $0.419 \times 10 = \text{Rs. 4.19}$

Earning per share of Rs. 10 each, Rs. 8 paid-up = Re.  $0.419 \times 8 = \text{Rs. 3.35}$  (approx)

Earning per share of Rs. 5, fully paid-up = Re.  $0.419 \times 5 = \text{Rs. 2.10}$  (approx)

Value of fully paid share of Rs. 10 = Rs.  $\frac{4.19}{2} \times 10 = \text{Rs. 20.95}$

Value of share of Rs. 10, Rs. 8 paid-up = Rs.  $\frac{3.35}{2} \times 10 = \text{Rs. 16.75}$

Value of fully paid share of Rs. 5 = Rs.  $\frac{2.10}{2} \times 10 = \text{Rs. 10.50}$

**Question 4**

- (a) Venus Ltd. has an asset, which is carried in the Balance Sheet on 31.3.2005 at Rs. 500 lakhs. As at that date the value in use is Rs. 400 lakhs and the net selling price is Rs. 375 lakhs.

From the above data:

- (i) Calculate impairment loss.
  - (ii) Prepare journal entries for adjustment of impairment loss.
  - (iii) Show, how impairment loss will be shown in the Balance Sheet.
- (b) Himalaya Ltd. in the past three years spent Rs. 75,00,000 to develop a Drug to treat Cancer, which was charged to Profit and Loss Account since they did not meet AS 8 criteria for capitalization. In the current year approval of the concerned Government Authority has been received. The Company wishes to capitalize Rs. 75,00,000 and disclose it as a prior period item. Is it correct? Give reason for your views.
- (c) Bottom Ltd. entered into a sale deed for its immovable property before the end of the year. But registration was done with registrar subsequent to Balance Sheet date. But before finalisation, is it possible to recognise the sale and the gain at the Balance Sheet date? Give your view with reasons. (6 + 5 + 5 = 16 Marks)

**Answer**

- (a) (i) Impairment loss is the amount by which the carrying amount of an asset exceeds its recoverable amount.

Thus, Impairment loss = Carried amount – Recoverable amount\*

$$= \text{Rs. 500 lakhs} - \text{Rs. 400 lakhs} = \text{Rs. 100 lakhs}$$

\*Recoverable amount is higher of asset's net selling price Rs. 375 lakhs and its value in use Rs. 400 lakhs.

∴ Recoverable amount = Rs. 400 lakhs

(ii)

**Journal Entries**

| Particulars                                      |                         | Dr.<br>Amount<br>Rs. in lakhs | Cr.<br>Amount<br>Rs. in lakhs |
|--------------------------------------------------|-------------------------|-------------------------------|-------------------------------|
| (i)                                              | Impairment loss account | Dr. 100                       |                               |
|                                                  | To Asset account        |                               | 100                           |
| (Being the entry for accounting impairment loss) |                         |                               |                               |

|      |                                                                          |     |     |     |
|------|--------------------------------------------------------------------------|-----|-----|-----|
| (ii) | Profit and loss account                                                  | Dr. | 100 |     |
|      | To Impairment loss account                                               |     |     | 100 |
|      | (Being the entry to transfer impairment loss to profit and loss account) |     |     |     |

(iii) **Balance Sheet of Venus Ltd. as on 31.3.2005**

|                         | <i>Rs. in lakhs</i> |
|-------------------------|---------------------|
| Asset less depreciation | 500                 |
| Less: Impairment loss   | <u>100</u>          |
|                         | <u>400</u>          |

- (b) AS 8 'Accounting for Research and Development' stands withdrawn w.e.f. 1st April, 2003 i.e. the date from which AS 26 'Intangible Assets' becomes mandatory. In any case, under either standard, the condition for recognition of a research and development asset has to be fulfilled when the expenditure was incurred. If the recognition conditions are not fulfilled the amount has to be charged to the profit and loss account. Once the amount is charged to the profit and loss account, such amount cannot be restated later as a research and development asset when the condition for recognition get fulfilled. The company therefore cannot capitalize Rs. 75,00,000 even as a prior period item.
- (c) Yes, it is possible for the Bottom Ltd. to recognize the sale and the gain at the balance sheet date according to AS 9\* 'Revenue Recognition'. It is evident that the significant risks and rewards of ownership had passed before the balance sheet date and the delay in transfer of property was merely because of formality in getting the transfer deed registered. Further the registration post the balance sheet date confirms the condition of sale at the balance sheet date as per AS 4 'Contingencies and Events occurring after the Balance Sheet Date'.

**Question 5**

- (a) In view of the provisions of Accounting Standard 25 on Interim Financial Reporting, on what basis will you calculate, for an interim period, the provision in respect of defined benefit schemes like pension, gratuity etc. for the employees?
- (b) Briefly describe the significance of Environmental Accounting.
- (c) A Company has its share capital divided into shares of Rs. 10 each. On 1st April, 2004 it granted 10,000 employees' stock options at Rs. 40, when the market price was Rs. 130. The options were to be exercised between 16th December, 2004 and 15th March, 2005. The employees exercised their options for 9,500 shares only; the remaining options lapsed. The company closes its books on 31st March every year.

Show Journal Entries.

(5 + 5 + 6 = 16 Marks)

**Answer**

- (a) Accounting Standard 25 suggests that provision in respect of defined benefit schemes like pension and gratuity for an interim period should be calculated on year-to-date basis by using the actuarially determined rates at the end of the prior financial year, adjusted for significant market fluctuations since that time and for significant curtailments, settlements or other significant one-time events.
- (b) Environmental accounting can be defined as a system (methodology) for measuring environmental performance and communicating the results of these measurements to users. It helps in presenting the utilization of natural resources by an enterprise, the costs incurred to use them and the income earned therefrom in a transparent manner. Environmental accounting, entirely a new concept, is a faithful attempt to identify the resources exhausted and the costs rendered reciprocally to the enterprise by a business corporation. Thus environmental accounting stands for recording and documenting environmental performance to facilitate effectiveness of environmental management system with reference to compliance, safety and quality control. It provides a data base for taking corrective steps and future action for developing organisation's environmental strategy and for identifying environmentally based opportunities for gaining an edge over one's competitors. If proper environmental accounting system is established, the enterprise will be able to anticipate environmental damage and therefore can prevent it from happening.

(c)

**Journal Entries**

|              | Particulars                                                                                                                                      |     | Dr.<br>Rs. | Cr.<br>Rs. |
|--------------|--------------------------------------------------------------------------------------------------------------------------------------------------|-----|------------|------------|
| 2004         |                                                                                                                                                  |     |            |            |
| April 1      | Employee Compensation Expense                                                                                                                    | Dr. | 9,00,000   |            |
|              | To Employee Stock Options Outstanding                                                                                                            |     |            | 9,00,000   |
|              | (Being grant of 10,000 stock options to employees at Rs. 40 when market price is Rs. 130)                                                        |     |            |            |
| 2005         |                                                                                                                                                  |     |            |            |
| 16th         | Bank account                                                                                                                                     | Dr. | 3,80,000   |            |
| Dec. to 15th | Employee stock options outstanding                                                                                                               | Dr. | 8,55,000   |            |
|              | To Equity share capital                                                                                                                          |     |            | 95,000     |
| March        | To Securities premium                                                                                                                            |     |            | 11,40,000  |
|              | (Being allotment to employees of 9,500 equity shares of Rs. 10 each at a premium of Rs. 120 per share in exercise of stock options by employees) |     |            |            |
| March 16     | Employee stock options outstanding                                                                                                               | Dr. | 45,000     |            |
|              | To Employee compensation expense                                                                                                                 |     |            | 45,000     |
|              | (Being entry for lapse of stock options for 500 shares)                                                                                          |     |            |            |

|          |                                                                              |     |          |          |
|----------|------------------------------------------------------------------------------|-----|----------|----------|
| March 31 | Profit and Loss account                                                      | Dr. | 8,55,000 |          |
|          | To Employee compensation expense                                             |     |          | 8,55,000 |
|          | (Being transfer of employee compensation expense to profit and loss account) |     |          |          |

**Question 6**

- (a) While closing its books of account on 31st March, 2005 a Non-Banking Finance Company has its advances classified as follows:

|                                      | Rs.in lakhs |
|--------------------------------------|-------------|
| Standard assets                      | 16,800      |
| Sub-standard assets                  | 1,340       |
| Secured positions of doubtful debts: |             |
| – upto one year                      | 320         |
| – one year to three years            | 90          |
| – more than three years              | 30          |
| Unsecured portions of doubtful debts | 97          |
| Loss assets                          | 48          |

Calculate the amount of provision, which must be made against the Advances.

- (b) In May, 2004 Speed Ltd. took a bank loan to be used specifically for the construction of a new factory building. The construction was completed in January, 2005 and the building was put to its use immediately thereafter. Interest on the actual amount used for construction of the building till its completion was Rs. 18 lakhs, whereas the total interest payable to the bank on the loan for the period till 31st March, 2005 amounted to Rs. 25 lakhs.

Can Rs. 25 lakhs be treated as part of the cost of factory building and thus be capitalized on the plea that the loan was specifically taken for the construction of factory building?

- (c) Distinguish between “Timing differences” and “Permanent differences” referred to in AS 22 on Accounting for Taxes, giving 2 examples of each. (8 + 4 + 4 = 16 Marks)

**Answer**

- (a) ` Calculation of provision required on advances as on 31st March, 2005

|                     | Amount<br>Rs. in lakhs | Percentage<br>of provision | Provision<br>Rs. in lakhs |
|---------------------|------------------------|----------------------------|---------------------------|
| Standard assets     | 16,800                 | NIL                        | NIL                       |
| Sub-standard assets | 1,340                  | 10                         | 134                       |

Secured portions of doubtful debts—

|                                      |     |     |            |
|--------------------------------------|-----|-----|------------|
| —upto one year                       | 320 | 20  | 64         |
| — one year to three years            | 90  | 30  | 27         |
| —more than three years               | 30  | 50  | 15         |
| Unsecured portions of doubtful debts | 97  | 100 | 97         |
| Loss assets                          | 48  | 100 | <u>48</u>  |
|                                      |     |     | <u>385</u> |

- (b) As per para 19 of AS 16 'Borrowing Costs', capitalization of borrowing costs should cease when substantially all the activities necessary to prepare the qualifying asset for its intended use or sale are complete. Therefore, interest on the amount that has been used for the construction of the building upto the date of completion (January, 2005) i.e. Rs. 18 lakhs alone can be capitalized. It cannot be extended to Rs. 25 lakhs.
- (c) As per AS 22, timing differences are the differences between taxable income and accounting income for a period that originate in one period and are capable of reversal in one or more subsequent periods.

**Examples:**

- Unabsorbed depreciation and carry forward of losses which can be set-off against future taxable income.
- Statutory dues deferred for payment under Section 43B of the Income-Tax Act.

"Permanent Differences" are the differences between taxable income and accounting income for a period that originate in one period but do not reverse subsequently.

**Examples:**

- Agricultural income.
- Donations/contributions disallowed for tax purposes.