PAPER 5 – ADVANCED ACCOUNTING

Q.No. 1 is Compulsory. Answer any Five Questions from the remaining Six Questions

Question 1(a): EPS – Rights Issue – AS 20 5 Marks

The following information is available for Raja Ltd. for the accounting year 2009-10 and 2010-11.

Net Profit: Year 2009 – 10 ₹ 25,00,000

Year 2010 – 11 ₹ 40,00,000

No. of shares outstanding prior to right issue 12,00,000 shares.

Right issue : One new share for each three outstanding i.e. 4,00,000 shares

: Right issue price ₹ 22

: Last date of exercise rights 30-6-2010

For rate of one equity share immediately prior to exercise of rights on 30.06.2010 : ₹ 28. Compute Basic EPS.

Solution: Also See Q No.30, Page 19.15 of "Ready Referencer on Advanced Accounting" for Group II IPCC & Q No. 52, Page 90 of "Workbook for Classroom discussion"

Step	Procedure
1	Number of Equity Shares outstanding prior to the Rights Issue = 12,00,000
2	Number of Shares issued by way of Rights = one for every three held = 12,00,000 ÷ 3 = 4,00,000 Exercise Price (i.e. Issue Price) ₹ 22.00
3	Fair Value of Equity Share prior to Rights Issue ₹ 28.00
4	Theoretical Ex–Rights Fair Value per Share is calculated as under – A = (Shares before Rights Issue × Fair Value before Rights) = (12,00,000 × 28) = ₹ 3,36,00,000 B = (Shares issued by way of Rights × Exercise Price) = (4,00,000 × 22) = ₹ 88,00,000 C = Fair Value of all Equity Shares including Rights = A + B = ₹ 4,24,00,000 D = Total Shares = Shares before Rights + Rights Shares = 12,00,000 + 4,00,000 = 16,00,000 E = Theoretical Ex–Rights Fair Value per Share = C ÷ D = ₹ 4,24,00,000 ÷ 16,00,000 = **₹ 26.50.**
5	Adjustment [or] Multiplier Factor = Step 3 ÷ Step 4 = ₹ 28.00 / ₹ 26.50 = **1.057** (approx.) i.e. Fair Value of Equity Share prior to Rights Issue ÷ Theoretical Ex–Rights Fair Value per Share
6	Weighted Average No. of Equity Shares for the current year = (See calculation below) 16,67,100
7	Basic EPS for current yr = Net Profit for the yr ÷ Step 6 = ₹ 40,00,000 ÷ 16,67,100= **₹ 2.40**
8	EPS for the previous year as originally reported = ₹ 25,00,000 ÷ 12,00,000 = ₹ 2.08 Adjusted EPS for the previous reporting period = ₹ 25,00,000 ÷ (12,00,000 × 1.057) = ₹ 1.97 = Net Profit for that year ÷ [Number of Equity Shares × Adjustment Factor]

Step 6: Computation of Weighted Average Number of Equity Shares for the current year

Period	Months	Time Weight	Adjustment Factor	No. of Equity Shares	Weighted Average Number of Shares
(1)	(2)	(3)	(4)	(5)	(6) = (3) × (4) × (5)
1st Apr – 30th June	3 months	3 / 12	1.057 (28/26.5)	Opg. Bal. = 12,00,000	3,17,100
30th June – 31st Mar	9 months	9 / 12	Not Applicable	(incl. Rights)=18,00,000	13,50,000
Weighted Average Number of Shares outstanding during the period					**16,67,100**

Question 1(b): Underwriter's Liability – Par Issue — 5 Marks

Delta Ltd. Issue 25,00,000 Equity Shares of ₹ 10 each at par. 7,00,000 shares were issued to the promoters and the balance offered to the public was underwritten by three underwriters P, Q & R in the ratio of 2 : 3 : 4 with Firm Underwriting of 50,000, 60,000 and 70,000 shares each respectively. Total subscription received 13,88,000 shares including Marked Application and excluding Firm Underwriting were as

P	3,00,000
Q	3,50,000
R	4,50,000

Unmarked and surplus applications to be distributed in Gross Liability ratio. Ascertain the liability of each underwriter.

Solution: Also See Q No.23, Page 5.49 of "Ready Referencer on Advanced Accounting" for Group II IPCC & Q No. 3, Page 57 of "Workbook for Classroom discussion"

Statement of Underwriters Liability (Figures in No. of Shares)

	Particulars	**P**	**Q**	**R**	**Total**
	Gross Liability	4,00,000	6,00,000	8,00,000	18,00,000
Less:	Unmarked Applications (See **Note** below)	(64,000)	(96,000)	(1,28,000)	(2,88,000)
		3,36,000	5,04,000	6,72,000	15,12,000
Less:	Marked Applications	(3,00,000)	(3,50,000)	(4,50,000)	(11,00,000)
		36,000	1,54,000	2,22,000	4,12,000
Less:	Firm Underwriting	(50,000)	(60,000)	(70,000)	(1,80,000)
	Balance to be taken under Contract	(14,000)	94,000	1,52,000	2,32,000
Adjust:	P's Surplus transferred to Q and R in Gross Liability Ratio (3 : 4)	14,000	(6,000)	(8,000)	—
	Net Liability	**—**	**88,000**	**1,44,000**	**2,32,000**
Add:	Firm Underwriting	50,000	60,000	70,000	1,80,000
	Total Liability	**50,000**	**1,48,000**	**2,14,000**	**4,12,000**

Note: Unmarked Applications = **2,88,000** i.e. Total Applications 13,88,000 – Marked Applications (3,00,000 + 3,50,000 + 4,50,000 = 11,00,000). These are distributed in the ratio of Gross Liability i.e. **equally.**

Question 1(c): Uniform Gross Profit – Purchase and Sale Quantity differences — 5 Marks

Brahma Limited has three departments and submits the following information for the year ending 31st March, 2011.

Particulars	A	B	C	Total (₹)
Purchase (units)	5,000	10,000	15,000	
Purchases (amount)				8,40,000
Sales (units)	5,200	9,800	15,300	
Selling price (₹ per unit)	40	45	50	
Closing Stock (units)	400	600	700	

You are required to prepare Departmental Trading Account of Brahma Limited assuming that the rate of profit on sales is uniform in each case.

Solution: Also See Q No.8, Page 2.10 of "Ready Referencer on Advanced Accounting" for Group II IPCC & Q No. 6, Page 18 of "Workbook for Classroom discussion"

1. Computation of Opening Stock Quantity (in units)

	Particulars	**A**	**B**	**C**
	Closing Stock	400	600	700
Add:	Units Sold	5,200	9,800	15,300
Less:	Purchases	(5,000)	(10,000)	(15,000)
	Opening Stock	**600**	**400**	**1,000**

2. Computation of Gross Profit Ratio

We are informed that the GP Ratio is the same for all departments. Selling Price is given for each department's products but the Sale Quantity is different from that of Purchase Quantity. To find the Uniform GP Rate, the sale value of Purchase Quantity should be compared with the Total Cost of Purchase, as under:

Assuming all purchases are sold, the sale proceeds would be –

Particulars	Sale Value of Purchase Quantity	Amount
Department A	5,000 units at ₹ 40	2,00,000
Department B	10,000 units at ₹ 45	4,50,000
Department C	15,000 units at ₹ 50	7,50,000
Total Sale Value of Purchase Quantity		**14,00,000**
Less: Cost of Purchase		8,40,000
Gross Profit Amount		**5,60,000**
Gross Profit Ratio	5,60,000 ÷ 14,00,000	40% of Selling Price

3. Computation of Profit and Cost for each article

Department	Selling Price	Profit at 2/5 of SP	Cost = Sales – Profit
Department A	₹ 40	2/5 of ₹ 40 = 16	₹ 24
Department B	₹ 45	2/5 of ₹ 45 = 18	₹ 27
Department C	₹ 50	2/5 of ₹ 50 = 20	₹ 30

4. Departmental Trading Account for the year

Particulars	A	B	C	Total	Particulars	A	B	C	Total
To Opg. stock	14,400	10,800	30,000	55,200	By Sales	2,08,000	4,41,000	7,65,000	14,14,000
To Purchase	1,20,000	2,70,000	4,50,000	8,40,000	By Clg. stock	9,600	16,200	21,000	46,800
To Gross Profit	83,200	1,76,400	3,06,000	5,65,600					
Total	**2,17,600**	**4,57,200**	**7,86,000**	**14,60,800**	**Total**	**2,17,600**	**4,57,200**	**7,86,000**	**14,60,800**

Opening and Closing Stocks are valued at Cost as indicated in WN 3 above. Sale Amount in the Trading Account is computed for the Sale Quantity only. Gross Profit is calculated at 40% of Sale Value.

Question 1(d): Employees' Stock Option Scheme 5 Marks

A Company has its Share Capital divided into Shares of ₹ 10 each. On 1st April 2010 it granted 20,000 Employees' Stock Options at ₹ 40, when the Market Price was ₹ 130. The options were to be exercised between 1st January 2011 to 15th March, 2010. The employees exercised their options for 18,000 shares only, the remaining options lapsed. The company closes its books on 31st March every year. Pass Journal entries with regard to Employees' Stock Option.

Solution: Also See Q No.19, Page 5.46 of "Ready Referencer on Advanced Accounting" for Group II IPCC & Q No. 23, Page 85 of "Workbook for Classroom discussion"

JOURNAL ENTRIES

Step 1: Recognition of Option Discount as Employee Benefits –

Date	Particulars	Dr.	Cr.
2010 April 1	Employee Compensation Expense Dr. To Employee Stock Options Outstanding (Being grant of 20,000 stock options to employees at ₹ 40 when market price is ₹ 130)	18,00,000	 18,00,000

Step 2: Entries for allotment of Shares to Employees exercising Stock Option –

Date	Particulars	Dr.	Cr.
2011 Jan. 1 to Mar.15	Bank (18,000 Shares × ₹ 40) Dr. Employee Stock Options Outstanding (18,000 Shares × ₹ 90) Dr. To Equity Share Capital (18,000 Shares × ₹ 10) To Securities Premium (18,000 Shares × ₹ 120) (Being allotment to employees of 18,000 equity shares of ₹ 10 each at a premium of ₹ 120 per share in exercise of Stock Options by Employees)	7,20,000 16,20,000	 1,80,000 21,60,000

Step 3: Cancellation / Reversal entry for Stock Options not exercised –

Date	Particulars	Dr.	Cr.
2011 Mar. 16	Employee Stock Options Outstanding Dr. To Employee Compensation Expense (Being entry for lapse of stock options for 2,000 shares)	1,80,000	 1,80,000

Step 4: Recognition of Employee Benefit (Discount on Stock options) in income statement –

Date	Particulars	Dr.	Cr.
2011 Mar. 31	Profit and Loss A/c Dr. To Employee Compensation Expense (Being transfer of employee compensation expense to P& L A/c)	16,20,000	 16,20,000

Employee Stock Options Outstanding will appear in the Balance Sheet as part of Net Worth or Shareholders' Equity. Deferred Employee Compensation will appear in the Balance Sheet as a negative item as part of Net Worth or Shareholders' Equity.

Question 2: Partnership Accounts – Amalgamation of Firms 16 Marks

A and B are partners of AB & Co. sharing profits and losses in the ratio of 2 : 1 and C and D are partners of CD & Co sharing profits and losses in the ratio of 3 : 2. On 1st April 2011 they decided to amalgamate and form a new firm M/s. AD & Co wherein all the partners of the both the firm would be partners sharing profits and losses in the ratio of 2 : 1 : 3 : 2 respectively to A, B C and D.

Their balance sheets on that date were as under:

Liabilities	AB & Co (₹)	CD & Co (₹)	Assets	AB & Co (₹)	CD & Co (₹)
Capitals			Building	75,000	90,000
A	1,50,000	–	Machinery	1,20,000	1,00,000
B	1,00,000	–	Furniture	15,000	12,000
C	–	1,20,000	Stock	24,000	36,000
D	–	80,000	Debtors	65,000	78,000
Reserve	66,000	54,000	Due from CD & Co	47,000	–
Creditors	52,000	35,000	Cash at Bank	18,000	15,000
Due to AB & Co.	–	47,000	Cash in hand	4,000	5,000
	3,68,000	3,36,000		3,68,000	3,36,000

The amalgamated firm took over the business on the following terms:

(a) Building was taken over at ₹ 1,00,000 and ₹ 1,25,000 of AB & Co. and CD & Co. respectively. And Machinery was taken over at ₹ 1,25,000 and ₹ 1,10,000 of AB & Co. and CD & Co. respectively.

(b) Goodwill of AB & Co. was worth ₹ 75,000 and that of CD & Co. was worth ₹ 50,000. Goodwill account was not to be opened in the books of the new firm, the adjustments being recorded through capital accounts of the partners.

(c) Provisions for doubtful debts has to be carried forward at ₹ 5,000 in respect of debtors of AB & Co and ₹ 8,000 in respect of CD & Co.

You are required to:

1. Compute the adjustments necessary for Goodwill.
2. Pass the Journal Entries in the books of AD & Co assuming that excess / deficit capital (taking D's Capital as base) with reference to share in profits are to be transferred to current accounts.

Solution: Also See Q No.29, Page 4.61 of "Ready Referencer on Advanced Accounting" for Group II IPCC & Q No. 19, Page 42 of "Workbook for Classroom discussion"

1. Adjustment for Raising & Writing off of Goodwill

Particulars	A	B	C	D	Total
1. Goodwill of AB & Co.	50,000	25,000	–	–	75,000
2. Goodwill of CD & Co.	–	–	30,000	20,000	50,000
3. Total	**50,000**	**25,000**	**30,000**	**20,000**	**1,25,000**
4. Written off in New Ratio	31,250	15,625	46,875	31,250	1,25,000
5. Difference	18,750 Cr.	9,375 Cr.	16,875 Dr.	11,250 Dr.	–

2. Journal Entries in the Books of AD & Co.

Date	Particulars		Dr.	Cr.
2011 April 1	Cash Account	Dr.	4,000	
	Bank Account	Dr.	18,000	
	CD & Co.	Dr.	47,000	
	Sundry Debtors	Dr.	65,000	
	Stock Account	Dr.	24,000	
	Furniture Account	Dr.	15,000	
	Machinery Account	Dr.	1,25,000	
	Building Account	Dr.	1,00,000	
	To Provision for Doubtful debts			5,000
	To Sundry Creditors			52,000
	To A's Capital Account			2,10,667
	To B's capital Account			1,30,333
	(Sundry assets and liabilities of M/s AB & Co. taken over at the values stated as per agreement dated.....)			
	Cash Account	Dr.	5,000	
	Bank Account	Dr.	15,000	
	Sundry Debtors A/c	Dr.	78,000	
	Stock Account	Dr.	36,000	
	Furniture Account	Dr.	12,000	
	Machinery Account	Dr.	1,10,000	
	Building Account	Dr.	1,25,000	
	To Provision for Doubtful Debts			8,000
	To AB & Co.			47,000
	To Sundry Creditors			35,000
	To C's Capital Account			1,80,600
	To D's Capital Account			8,000
	(Sundry assets and liabilities of M/s CD & Co. taken over at the values stated as per agreement dated...)			
	C's Capital Account	Dr.	16,875	
	D's Capital Account	Dr.	11,250	
	To A's Capital Account			18,750
	To B's capital Account			9,375
	(Adjustment in capital accounts consequent on raising goodwill of AB & Co. for ₹ 75,000, CD & Co. for ₹ 50,000 and writing off the dame in the new ratio between A, B, C & D as per agreement)			
	AB & Co.	Dr.	47,000	
	To CD & Co.			47,000
	(Mutual indebtedness of AB & Co. and CD & Co., cancelled on taking over of the two firms)			
	A's Capital Account	Dr.	1,20,269	
	To A's Current Account			1,20,269
	(Excess amount in A's Capital Account transferred to A's Current Account to reduce the balance in capital accounts in accordance with the profit sharing ratio)			
	B's Capital Account	Dr.	85,133	
	To B's Current Account			85,133
	(Excess amount in A's Capital Account transferred to A's Current Account to reduce the balance in capital accounts in accordance with the profit sharing ratio)			

Working Notes:

(i) Balance of Capital Accounts on transfer of business to M/s AD & Co.

(a) AB & Co.

	Particulars		B's Capital	S's Capital
	As per Balance Sheet		1,50,000	1,00,000
	Credit for Reserve		44,000	22,000
	Profit on Revaluation – Building 25,000 – Machinery 5,000	30,000		
Less:	Provision for Doubtful debts	5,000	16,667	8,333
			2,10,667	**1,30,333**

(b) CD & Co.

Particulars		C's Capital	D's Capital
As per Balance Sheet		1,20,000	80,000
Credit for Reserve		32,400	21,600
Profit on Revaluation – Building 35,000 – Machinery 20,000	55,000		
Less: Provision for Doubtful Debts	8,000	28,200	18,800
		1,80,600	**1,20,400**

(ii) Capital in the new firm

Particulars	A	B	C	D
Balance as taken over	2,10,667	1,30,333	1,80,600	1,20,400
Adjustment for Goodwill	18,750	9,375	(16,875)	(11,250)
	2,29,419	1,39,708	1,63,725	1,09,150
Total capital, ₹ 4,36,600 (See Note) in the new ratio of 2:1:3:2, taking D's Capital as the basis	1,09,150	54,575	1,63,725	1,09,150
Transfer to Current Account	1,20,269 (Cr.)	85,133 (Cr.)	–	–

Note: D's Capital is ₹ 1,09,150 and it is 2/8 of total. Therefore, the total is ₹ 4,36,600.

Question 3: Internal Reconstruction – Sub-Division and Surrender of Shares 16 Marks

The Balance Sheet of X Limited as at 31st March 2011, was as follows:

Liabilities	₹	Assets	₹
Authorised and Subscribed Capital:		Fixed Assets: Machineries	3,50,000
10,000 Equity Shares of ₹ 100 each	10,00,000		
Unsecured Loan:		Current Assets:	
15% Debentures	3,00,000	Stock	2,53,000
Accrued interest	45,000	Debtors	2,30,000
Current Liabilities		Bank	20,000
Creditors	52,000		
Provision for Income-Tax	36,000	Profit and Loss Account	5,80,000
Total	14,33,000	Total	14,33,000

It was decided to reconstruct the Company for which necessary resolution was passed and sanctions were obtained from appropriate authorities. Accordingly it was decided that –

1. Each Share shall be sub-divided into 10 Fully Paid Shares of ₹ 10 each.
2. After sub-division, each Shareholder shall surrender to the Company, 50% of his holdings for the purpose of re-issue to Debenture holders and Creditors as necessary.
3. Out of shares surrendered, 10,000 Shares of ₹ 10 each shall be converted into 10% Preference Shares of ₹ 10 each fully paid up.
4. The claims of the Debenture holders shall be reduced by 50%. In consideration of the reduction, the Debenture holders shall receive Preference Shares of ₹ 1,00,000 which are converted out of shares surrendered.
5. Creditors claim shall be reduced by 25%, it is to be settled by the issue of Equity Shares of ₹ 10 each out of shares surrendered.
6. Balance of Profit and Loss Account to be written off.
7. The shares surrendered and not re-issued shall be cancelled.

You are required to show the Journal Entries giving effect to the above and the resultant Balance Sheet.

Solution: Also See Q No.6, Page 7.11 of "Ready Referencer on Advanced Accounting" for Group II IPCC & Q No. 10, Page 64 of "Workbook for Classroom discussion"

1. Journal Entries in the books of the Company

S.No	Paritculars	Dr.	Cr.
1.	Equity Share Capital A/c (₹ 100) Dr. To Share Surrendered A/c To Equity Share Capital (₹ 10) A/c (Being sub-division of 10,000 Equity Shares of ₹ 100 each into 1,00,000 Equity Shares of ₹ 10 each and surrender of 50,000 of such sub-divided shares as per Capital Reduction scheme)	10,00,000	 5,00,000 5,00,000
2.	15% Debentures A/c Dr. Accrued Interest A/c Dr. To Reconstruction A/c (Being transfer of 50% of claims of Debenture holders to Reconstruction a/c in consideration of which 10% Preference Shares are being issued out of Share Surrender Account as per capital reduction scheme)	1,50,000 22,500	 1,72,500
3.	Creditors A/c Dr. To Reconstruction A/c (Being transfer of claims of Creditors to Reconstruction A/c in full, 25% of which is waiver and Equity Shares issued in consideration of the balance)	52,000	 52,000
4.	Share Surrendered A/c Dr. To 10% Preference Share Capital A/c (issued to Debentureholders) To Equity Share Capital (₹ 10) A/c (issued to Creditors) To Reconstruction A/c (balancing figure) – cancellation (Being issue of Preference and Equity Shares to discharge the claims of Debenture holders and Creditors respectively as per scheme; balance in Share Surrendered a/c being transferred to Reconstruction a/c on cancellation)	5,00,000	 1,00,000 39,000 **3,61,000**
6.	Reconstruction A/c Dr. To Profit and Loss A/c To Capital Reserve A/c (Being Dr. Balance of P&L Account written off against Reconstruction a/c and balance in Reconstruction A/c transferred to Capital Reserve)	5,85,500	 5,80,000 5,500

2. Shares Surrendered Account

Particulars	₹	Particulars	₹
To 10% Preference Share Capital A/c	1,00,000	By Equity Share Capital (₹ 100)	5,00,000
To Equity Share Capital A/c	39,000		
To Reconstruction A/c (balancing figure)	**3,61,000**		
Total	**5,00,000**	**Total**	**5,00,000**

3. Reconstruction (or) Capital Reduction Account

Particulars	₹	Particulars	₹
To Profit and Loss A/c	5,80,000	By 15% Debentures A/c	1,50,000
To Capital Reserve A/c (balancing figure)	**5,500**	By Accrued Interest on Debentures A/c	22,500
		By Creditors A/c	52,000
		By Shares Surrendered A/c – transfer	3,61,000
Total	**5,85,500**	**Total**	**5,85,500**

4. Balance Sheet of Vidhura Ltd (after reconstruction) as at 31st March

Liabilities	₹	Assets	₹
Share Capital:		**Fixed Assets:** Machineries	3,50,000
Authorised Capital:			
53,900 Equity Shares of ₹ 10 each	5,39,000		
10,000 Preference Shares of ₹ 10 each	1,00,000		
Issued and Paid Up:			
53,900 Equity Shares of ₹ 10 each	5,39,000	**Current Assets, Loans and Advances:**	
10% Preference Shares of ₹ 10 each (allotted as fully paid up under Reduction Scheme by conversion of Equity Shares)	1,00,000	Stock	2,53,000
		Debtors	2,30,000
		Bank	30,000
Reserves and Surplus: Capital Reserve	5,500		
Unsecured Loans:			
15% Debentures (50% of ₹ 3,00,000)	1,50,000		
Accrued interest (1/2 × 45,000)	22,500		
Current Liabilities and Provisions:			
Provision for Income-Tax	36,000		
Total	**8,53,000**	**Total**	**8,53,000**

Question 4(a): Liquidator's Final Statement of Account 8 Marks

The summarized Balance Sheet of Full Stop Limited. as on 31st March 2011, being the date of voluntary winding up is as under:

Liabilities	Amount	Assets	Amount
Share Capital:		Land and Buildings	5,20,000
5,000, 10% Cumulative Preference Shares of ₹ 100 each fully paid up	5,00,000	Plant and Machinery	7,80,000
Equity Share Capital:		Stock in trade	3,25,000
5,000 Equity Shares of ₹ 100 each ₹ 60 per share called up & paid up	3,00,000	Book Debts	10,25,000
5,000 Equity shares of ₹ 100 each ₹ 50 per share called up & paid up	2,50,000	Profit and Loss Account	5,50,000
Securities Premium	7,50,000		
10% Debentures	2,10,000		
Preference Creditors	1,05,000		
Bank Overdraft	4,85,000		
Trade Creditors	6,00,000		
Total	32,00,000	Total	32,00,000

Preference Dividend is in arrears for three years. By 31.03.2011 the assets realized were as follows:

Land and Buildings	6,20,000
Stock in Trade	3,10,000
Plant and Machinery	7,10,000
Book Debts	6,60,000

Expenses of Liquidation are ₹ 86,000. The Remuneration of the Liquidator is 2% of the realization of assets. Income Tax payable on Liquidation is ₹ 67,000. Assume that the final payments are made on 31.03.2011.

Prepare the Liquidator's Final Statement of Account.

Solution: **Also See Q No.12, Page 9.17 of "Ready Referencer on Advanced Accounting" for Group II IPCC**

1. Liquidator's Final Statement of Account

Receipts	Amount	Payments	Amount
– **Assets realized:**		– Liquidator's Remuneration (23,00,000 × 2%)	46,000
Land and Building 6,20,000		– Liquidator's Expenses	86,000
Stock-in-Trade 3,10,000		– Debentureholders	
Plant and Machinery 7,10,000		Face Value of Debentures	2,10,000
Book Debts 6,60,000	**23,00,000**	Debenture Interest for one year at 10%	21,000
– **Call Money** on 5,000 ₹ 50 paid	10,000	– Preferential Creditors	
shares at ₹ 2 per share		As given in Balance Sheet	1,05,000
		Income Tax Liability (given)	67,000
		– Unsecured Creditors	
		Bank Overdraft (assumed unsecured)	4,85,000
		Trade Creditors	6,00,000
		– Preference Shareholders	
		Preference Capital	5,00,000
		Arrears of Dividend (5,00,000 × 10% × 3yrs)	1,50,000
		– Equity Shareholders Refund on 5,000 Shares	
		₹ 60 paid up at ₹ 8 per share	40,000
Total	**23,10,000**	**Total**	**23,10,000**

2. Calls from Holders of Partly Paid Shares

Particulars	₹
a. Total of Receipts before considering Call Money (from the above account)	23,00,000
b. Total Payments before final payment to Equity Shares (from the above account)	22,70,000
c. Surplus from above before Calls made on Equity Shares (**a** – **b**)	30,000
d. Notional Call on 5,000 Partly Paid Shares at ₹ 10 each (to make all shares ₹ 60 paid up)	50,000
e. Surplus Cash Balance after Notional Call (comparing **c** and **d**)	**80,000**
f. Number of Shares deemed paid at ₹ 60 per share (5,000 + 5,000)	10,000
g. Hence, Refund on every ₹ 60 paid up Shares (**e** ÷ **f**)	8.00
h. Therefore, **Required Call on ₹ 50 paid up Share** (₹ 10 Notional Call – ₹ 8 Loss)	**₹ 2**

Question 4(b): Preparation of Branch Account in the books of Head Office 8 Marks

XYZ Company is having its Branch at Kolkata. Goods are invoiced to the branch at 20% profit on sale. Branch has been instructed to send all cash daily to head office. All expenses are paid by head office except petty expenses which are met by the Branch Manager. From the following particulars prepare branch account in the books of Head Office.

Particulars	₹	Particulars	₹
Stock on 1st April, 2010 (Invoice Price)	30,000	Discount allowed to debtors	160
Sundry Debtors on 1st April, 2010	18,000	Expenses paid by the Head Office	
Cash in hand on 1st April, 2010	800	– Rent	1,800
Office Furniture on 1st April, 2010	3,000	– Salary	3,200
Goods invoiced from the head office (Invoice Price)	1,60,000	– Stationary and Printing	800
Goods returned to Head Office	2,000	Petty Expenses paid by the Branch	600
Goods returned by Debtors	960	Depreciation to be provided on branch furniture at 10% p.a.	
Cash received from Debtors	60,000		
Cash Sales	1,00,000	Stock on 31st March 2011 (Invoice Price)	28,000
Credit Sales	60,000		

Solution: : Also See Q No.10, Page 3.28 of "Ready Referencer on Advanced Accounting" for Group II IPCC & Q No. 2, Page 20 of "Workbook for Classroom discussion"

1. Branch Debtors Account (to ascertain Closing Debtors)

Particulars	₹	Particulars	₹
To balance b/d – Opening Balance	18,000	By Cash – Amounts received	60,000
To Sales (Credit)	60,000	By Sales Returns	960
		By Discount	160
		By balance c/d – Closing Balance	**16,880**
Total	**78,000**	**Total**	**78,000**

2. Branch Account

Particulars		₹	**Particulars**		₹
To balance b/d			By Stock Reserve A/c (Opening Stock – 20% × ₹ 30,000)		6,000
– Stock	30,000		By Bank A/c:		
– Debtors	18,000		– Cash Sales	1,00,000	
– Furniture	3,000		– Received from Drs	60,000	1,60,000
– Petty Cash	800	51,800			
To Goods sent to Branch A/c		1,60,000	By Goods Sent to Branch A/c (Returns from Branch)		2,000
To Goods sent to Branch A/c (Loading on Returns 2,000 × 20%)		400	By Goods Sent to Branch A/c (Loading – 20% × ₹ 1,60,000)		32,000
To Bank A/c:			By balance c/d		
– Rent	1,800		– Stock	28,000	
– Salary	3,200		– Debtors	16,880	
– Stationery & Printing	800	5,800	– Furniture (3,000 – 300)	2,700	
To Stock Reserve A/c (Loading on Clg. Stock – 28,000 × 20%)		5,600	– Petty Cash (800 – 600)	200	47,780
To Profit and Loss A/c (Profit)		**24,180**			
Total		**2,47,780**	**Total**		**2,47,780**

Notes:

1. Depreciation on Furniture is not debited as a separate item in the Branch Account since the Furniture (Closing Balance) at the end is shown at the Depreciated Value.
2. Sales Returns and Discount are accounted for automatically since Opening and Closing balances of Debtors are stated in the Branch Account.

3. Goods Sent to Branch Account

Particulars	₹	**Particulars**	₹
To Branch A/c (Loading)	32,000	By Branch A/c	1,60,000
To Branch A/c (Returns from Branch)	2,000	By Branch A/c (Loading)	400
To Purchases A/c (Balance transferred / adjusted)	1,26,400		
Total	**1,60,400**	**Total**	**1,60,400**

Question 5: Provision for Risk Assets and Profit & Loss Account of a Bank — 16 Marks

From the following information prepare the Profit & Loss Account of Jawahar Bank Limited for the year ended 31st March, 2011. Also give necessary Schedules.

Particulars	Figures are in ₹ 'Thousands
Interest earned on Term Loans	17.26
Interest earned on Term Loans classified as NPA	4.52
Interest received on Term Loan classified as NPA	2.04
Interest on Cash Credits and Overdrafts	38.54
Interest earned but not received on Cash Credit and Overdraft treated as NPA	8.39
Interest on Deposits	27.20
Commission	1.97
Profit on sale of Investments	11.76

Particulars	Figures are in ₹ 'Thousands
Profit on revaluation of Investments	2.76
Income from Investments	15.53
Salaries, Bonus and Allowances	18.75
Rent, Taxes and Lighting	1.70
Printing and Stationary	0.75
Director's fees, allowances, expenses	1.33
Law charges	0.22
Repairs and Maintenance	0.18
Insurance	0.30

Other Information:	Figures are in ₹ 'Thousands
Make necessary provision on risk assets:	
(i) Sub-standard	15.00
(ii) Doubtful for one year	7.00
(iii) Doubtful for two years	2.40
(iv) Loss assets	0.65
Investments	3700

Bank should not keep more than 25% of its investments as 'held-for-maturity' investment. The market value of its best 75% investments is ₹ 9,00,000 as on 31st March, 2011.

Solution:

1. Computation of Provision for Risk Assets:

Classification of Assets	Rate	(₹ in 'Thousands)	Provision – (₹ in 'Thousands)
Sub–Standard	10%	15.00	1.5
Doubtful			
1 Year	20%	7.00	1.40
2 Years	30%	2.40	0.72
Loss	100%	0.65	0.65
Total			**4.27**

2. Computation of Provision based on Valuation of Investments:

Particulars	Amount (₹ in 'Thousands)
Total value of Investments – Given	3700
Investments classified as "Held–For–Maturity" – 25%	925
Other investments – 75%	2,775
Investments valued as on 31st March 2011 – Given	900
Balance to be provided in the Profit & Loss A/c	**1,875**

Note: Investments classified as "Held–For–Maturity" should be valued at cost. Hence no adjustment is made in the valuation of those investments.

3. Profit and Loss Account of Jawahar Bank Limited for the year ended 31.03.2011 (₹ in 'Thousands)

Particulars	Sch. No.	31.3.2011	31.3.2010
I. Income			
Interest Earned	13	73.37	
Other Income	14	16.49	
Total		**89.86**	
II. Expenditure			
Interest Expended	15	27.20	
Operating Expenses	16	23.23	
Provisions and Contingencies [1,875 + 4.27]		1879.27	
Total		**1,929.70**	

Particulars	Sch. No.	31.3.2011	31.3.2010
III. Profit / Loss			
Net Profit / (Loss) for the Year		(1,839.84)	
Profit / (Loss) Brought Forward		—	
Total		**(1,839.84)**	
IV. Appropriations:		—	

4. Schedules to the Profit and Loss Account for the year ending 31.12.2004 (₹ 'Thousands)

Particulars	31.12.11	31.03.10
Schedule 13 – Interest Earned		
Interest / Discount [17.26 + 2.04 + 38.54]	57.84	
Income on Investment	15.53	
Interest on Balance with RBI and other Inter Bank Fund	--	
Total	**73.37**	
Schedule 14 – Other Income		
Commission Exchange and Brokerage	1.97	
Profit on Sale of Investments	11.76	
Profit on Revaluation of Investments	2.76	
Total	**16.49**	
Schedule 15 – Interest Expended		
Interest on Deposits	27.20	
Interest on RBI / Inter-bank Borrowings	--	
Total	**27.20**	
Schedule 16 – Operating Expenses		
Payment to and Provisions for Employees – Salaries, Bonus and Allowances	18.75	
Rent, Taxes and Lighting	1.70	
Printing and Stationary	0.75	
Director's Fees, Allowance and Expenses	1.33	
Law charges	0.22	
Repairs and Maintenance	0.18	
Insurance	0.30	
Total	**23.23**	

Notes:

1. For Assets classified as NPA, interest should be recognized only when it is received and not to be recognized on accrual basis. Therefore in the Profit & Loss Account interest received from NPA alone is recognized.
2. Interest earned on normal Term Loans is assumed to be exclusive of Interest earned on NPA. Alternate assumptions hold good.

Question 6(a): Valuation of Asset and Finance Charge – AS 19 — 8 Marks

Lessee Ltd. took a machine on Lease from Lessor Ltd. the fair value being ₹ 7,00,000. The Economic Life of machine as well as the lease term is 3 years. At the end of each year Lessee Ltd. pays ₹ 3,00,000. The Lessee has guaranteed a Residual Value of ₹ 22,000 on expiry of the lease to the Lessor. However Lessor Ltd. estimates that the Residual Value of the machinery will be only ₹ 15,000. The implicit rate of return is 15% p.a. and present value factors at 15% are 0.869, 0.756 and 0.657 at the end of first, second and third years respectively.

Calculate the Value of Machinery to be considered by Lessee Ltd. and the Finance Charges in each year.

Solution: Also See Q No.18, Page 18.9 of "Ready Referencer on Advanced Accounting" for Group II IPCC

1. Value of Machinery to be recorded as an Asset and Liability = **Least of** – (a) Fair Value of the asset, and (b) Present Value of Minimum Lease Payments (MLP) & Guaranteed Residual Value (GRV).

2. Present Value of MLP and GRV is computed below –
   = PV of MLP i.e. Annual Lease Rental × PV Factor + PV of GRV i.e. GRV × PV Factor at 15% for Year 3
   = (₹ 3,00,000 × 2.282) + [₹ 22,000 ÷ $(1 + 0.15)^3$]
   = ₹ 6,84,600 + ₹ 14,465 = **₹ 6,99,065.**

3. **Asset and Liability Recognition:** As the calculated amount ₹ 6,99,065 is lower than the Fair Value of the Leased Asset ₹ 7,00,000, the amount of machinery recognized as an asset and the amount of outstanding liability from the lease could be recorded at **₹ 6,99,065** by the Lessee.

4. **Finance Charges:** The Lessee should apportion the Lease Payments between Finance Charge and Reduction in Outstanding Liability as follows –

Date	Finance Charge	Payment	Reduction in O/s Liability	O/s Liab.
Year 1	—	—	—	₹ 6,99,065
Year 1 End	6,99,065 × 15% = ₹ 1,04,860	₹ 3,00,000	3,00,000 – 1,04,860 = ₹ 1,95,140	₹ 5,03,925
Year 2 End	5,03,925 × 15% = ₹ 75,589	₹ 3,00,000	3,00,000 – 75,589 = ₹ 2,24,411	₹ 2,79,514
Year 3 End	2,79,514 × 15% = ₹ 42,486*	₹ 3,00,000	3,00,000 – 42,486 = ₹ 2,57,514	₹ 22,000

***** Interest Amount is taken as the balancing figure due to approximation in computing the Interest implicit in the Lease.

Question 6 (b): Revenue Account of Fire Insurance Business — 8 Marks

Modern Insurance Company's Fire Insurance division provide the following information, show the amount of claim at it would appear in the Revenue Account for the year ended 31st March, 2011.

Particulars		Direct Business (₹)	Re-insurance (₹)
Claims paid during the Year		35,30,000	8,20,000
Claims Payable	– 11.4.2010	8,23,000	58,000
	– 31.3.2011	8,75,000	87,000
Claims Received		—	3,20,000
Claims Receivable	– 01.4.2010	—	85,000
	– 31.3.2011	—	1,42,000
Expenses of Management (including ₹ 38,000 Surveyor's Fee and ₹ 42,000 Legal Expenses for settlement of claims)		3,45,000	—

Solution: Also See Q No.3, Page 12.15 of "Ready Referencer on Advanced Accounting" for Group II IPCC & Q No. 2, Page 76 of "Workbook for Classroom discussion"

1. Calculation of Claims paid during the year

	Particulars	₹	₹
	Claims paid under:		
	– Direct Business	35,30,000	
	– Reinsurance	8,20,000	43,50,000
Add:	Surveyor's fee		38,000
	Legal expenses		42,000
	Claims paid by the Company		44,30,000
Less:	Claims Received from Re-Insurers		(3,20,000)
	Net Claims Paid by the Company		**41,10,000**

2. Calculation of Opening and Closing Outstanding Claims (₹)

	Particulars	Opening	Closing
	Balance outstanding as per Books under		
	– Direct business	8,23,000	8,75,000
	– Reinsurance	58,000	87,000
	Total Outstanding Claims	8,81,000	9,62,000
Less:	Claims receivable from Re-insurers	(85,000)	(1,42,000)
	Corrected Balance	**7,96,000**	**8,20,000**

3. Abstract of the Fire Revenue Account for the year ending 31.3.2011

Particulars	₹	₹
To Claim less Re-insurance:		
Paid during the year	41,10,000	
Add: Outstanding claims at the end of the year	8,20,000	
	49,30,000	
Less: Outstanding claims at the beginning of the year	(7,96,000)	**41,34,000**

Question 7(a): Redemption of Debentures – Part Conversion into Equity Shares 4 Marks

XYZ Ltd. had issued 30,000, 15% Convertible Debenture of ₹ 100 each on 1st April 2008. The debentures are due for redemption on 1st March, 2011. The terms of issue of debentures provided that they were redeemable at a premium of 5% and also conferred option to the Debentureholders to convert 20% of their holding equity shares (Nominal Value of ₹ 10) at a price of ₹ 15 per share. Debentureholders holding 2,500 debentures did not exercise the option. Calculate the number of Equity Shares to be allotted to the Debenture holders exercising the option to the maximum.

Solution: Also See Q No.7, Page 6.10 of "Ready Referencer on Advanced Accounting" for Group II IPCC & Q No. 4, Page 47 of "Workbook for Classroom discussion"

Computation of number of Shares to be allotted

Particulars	
Total Number of Debentures	30,000
Less: Number of Debentures not opted for conversion	2,500
Balance Debentures opting for conversion	27,500
Convertible Portion Debentures = 20% of 27,500	5,500
Redemption value of 5,500 debentures (₹ 105 × 5,500)	₹ 5,77,500
Number of Equity shares to be allotted = 5,77,500 ÷ 15 = **38,500 Shares** of ₹ 10 each	

Question 7(b): Accounting for Government Grants – AS 12 4 Marks

Siva Limited received a Grant of ₹ 1,500 Lakhs during the last accounting year (2009–10) from Government for welfare activities to be carried on by the company for its employees. The grant prescribed conditions for its utilization. However during the year 2010–11, it was found that the conditions of the grant were not compiled with and the grant had to be refunded to the Government in full. Elucidate the current accounting treatment with reference to the provisions of AS–12.

Solution:

1. **Principle:**
   (a) The amount refundable in respect of a revenue item is applied first against any unamortised Deferred Credit remaining in respect of the Grant.
   (b) Any excess of Grant refundable over the Deferred Credit or when there is no Deferred Credit, it is **immediately charged** to the P&L Statement.
   Note: When Government gives grant subject to fulfillment of certain conditions, in those cases, such Grant should be accounted for deferred income method over the period of fulfillment of conditions, in proportion to the expenditure incurred.

2. **Analysis and Conclusion:**
   (a) As the grant of ₹ 1,500 Lakhs is received for welfare activities to be carried on by the company for its employees, it is a **revenue** grant. The entire grant should be accounted for as "Revenue" in the Profit and Loss Account for Financial Year 2009-10.
   (b) If the Company has to incur any expenditure to meet the conditions specified under the grant, then such grant should be amortized and offered as income in proportion to the costs to be incurred.
   (c) Therefore, the treatment in case of refund will be as follows —
   - If the Company had credited the entire Grant as Revenue in the Profit and Loss Account, the refund should be debited to Profit and Loss Account.
   - If the Company has followed Deferred Credit Method, then the payment should first be adjusted against balance in Deferred Credit A/c and the balance debited to Profit and Loss Account.

Question 7(c): Impairment of Assets – AS 28 4 Marks

Carrying amount of a Machine is ₹ 1,00,000 (Historical cost less depreciation). The Machine is expected to generate ₹ 25,000 net cash flow for 5 years. The Net Realizable Value (or Net Selling Price) of the Machine on current date is ₹ 85,000. The enterprises required rate of earning is 10% p.a. State the value at which the enterprise should carry its machine. The present value factors at 10% are 0.909, 0.826, 0.751, 0.683 at the end of first, second, third, fourth and fifth year respectively.

Solution:

1. Computation of Value in Use

Year	Cash Flow (₹)	Discount Rate at 10%	Discounted Cash Flow (₹)
1	25,000	0.909	22,725
2	25,000	0.826	20,652
3	25,000	0.751	18,775
4	25,000	0.683	17,075
5	25,000	0.621	15,525
Value in Use			**94,752**

2. Computation of Other Particulars

Particulars	₹ Lakhs
1. Carrying Amount (Historical Cost less Depreciation)	1,00,000
2. Recoverable Amt (Net Realisable Value 85,000 [or] Value in Use 94,752, whichever is **higher**)	94,752
3. Impairment Loss = Carrying Amount **Less** Recoverable Amount (1 – 2)	5,248
4. Revised Carrying Amount = Old Carrying Amount Less Impairment Loss (1 – 5)	94,752

Question 7(d): Disclosure requirement – Non Prior Period Items 4 Marks

A company signed an agreement with the Employee's Union on 01.09.2010 for revision of wages with retrospective effect from 01.04.2009. This would cost the company an additional liability of ₹ 10 Lakhs per annum. Is a disclosure necessary for the amount paid in 2010–11?

Solution: **Also See Q No.26, Page 14.10 of "Ready Referencer on Advanced Accounting" for Group II & Q No.28, Page 86 of "Workbook for Classroom discussion"**

1. **Nature:** Revision wages for earlier years as a result of an agreement entered with the Employee's union in the current year is an event in the **ordinary course** and relates to **normal activities of business**. Although abnormal in amount or infrequent in nature it is not an extraordinary item under AS–5.

2. **Not a Prior Period Item:** This amount is **not a Prior Period Item,** as it does not arise out of errors or omissions in the preparation of Financial Statements of one or more prior periods.

3. **Treatment:** Additional Liability for wages of ₹ 10,00,000 should be **included in current year's wages** for financial year 2010 – 2011.

4. **Disclosure:** As per AS – 5, when items of income and expenses within profit / loss from ordinary activities are of such size, the nature or incidence that their disclosure is relevant to explain the performance of the enterprise for the period, they should be **disclosed separately**. Separate disclosure of such expense is required since it may be relevant to users of Financial Statements, in understanding the financial position and performance of the enterprise.

Question 7(e): 4 Marks

Why Goods are marked on Invoice Price by the Head Office while sending goods to the branch?

Solution:

1. **Control:** The Head Office may not reveal the actual cost and profit to the branch in order to have control over the cost. The goods are sent in the invoice price to all the branches so that the head office can have a control over the price of the goods sent to all the branches while preparing the branch accounts in the books of head office rather than reversing the invoice price independently for all the branches.
2. **Rewarding of the Employees:** For the purpose of rewarding the branch managers based on the profits made by their respective branches.
3. **Pricing Policy:** To maintain Uniform Pricing Policy so that the price of the products remain the same in both the head office and their branches.

Guru Kripa's Guideline Answers for May 2011 CA PCC Examination

PAPER 1 – ADVANCED ACCOUNTING [Questions Relevant to Group II – IPCC]

Question 1(a): Treatment of Interest – AS 16 5 Marks

GHI Limited obtained a loan for ₹ 70 Lakhs on 15th April, 2010 from JKL Bank, to be utilized as under:

Particulars	₹
Construction of Factory Shed	25,00,000
Purchase of Machinery	20,00,000
Working Capital	15,00,000
Advance for Purchase of Truck	10,00,000

In March 2011 Construction of the Factory Shed was completed and Machinery which was ready for its intended use installed. Delivery of Truck was received in the next Financial Year. Total Interest ₹ 9,10,000 charged by the bank for the Financial Year ending 31.03.2011. Show the treatment of Interest under AS 16 and also explain the nature of Assets.

Solution: Also See Q No.7, Page 17.2 of "Ready Referencer on Advanced Accounting" for Group II & Q No.40, Page 88 of "Workbook for Classroom discussion"

1. **Principle:** As per AS – 16, 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.
2. **Analysis:** Interest Rate for the Term Loan = ₹ 9,10,000 ÷ ₹ 70,00,000 = 13%.
3. **Conclusion:** The treatment for the total interest of ₹ 52.20 Lakhs is given below –

Purpose / Utilisation	Loan Amount	Interest Amount	Accounting Treatment
Construction of Factory Shed	₹ 25,00,000	₹ 25,00,000 × 13% = ₹ 3,25,000	Added to the Cost of the Factory Shed as per AS – 16.
Purchase of Machinery	₹ 20,00,000	₹ 20,00,000 × 13% = ₹ 2,60,000	Added to Cost of Machinery as per AS – 16.
Working Capital	₹ 15,00,000	₹ 15,00,000 × 13% = ₹ 1,95,000	Written off to P&L Account as per AS – 16.
Advance for Purchase of Truck	₹ 10,00,000	₹ 10,00,000 × 13% = ₹ 1,30,000	Kept in Interest Suspense A/c (Capital WIP A/c) till the date of acquisition / installation of additional assets & capitalised later on asset creation.
Total	**₹ 70,00,000**	**₹ 9,10,000**	

Question 1(b): Computation of Basic EPS – AS 20 5 Marks

In April, 2010, A Limited issued 18,00,000 Equity Shares of ₹ 10 each; ₹ 5 per share was called up on that date which was paid by all the shareholders. The remaining ₹ 5 was called up on 1.9.2010. All the Shareholders (except one having 3,60,000 shares) paid the sum in September 2010. The Net Profit for the year ended 31.3.2011 is ₹ 33 Lakhs after Dividend on Preference Shares and Dividend Distribution Tax of ₹ 6.60 Lakhs. Compute the Basic EPS for the year ended 31st March, 2011 as per AS – 20.

Solution: Also See Q No.14, Page 19.7 of "Ready Referencer on Advanced Accounting" for Group II & Q No.50, Page 89 of "Workbook for Classroom discussion"

1. Computation of Weighted Average No. of Shares

Date	Shares Outstanding	Proportion of Paid–up Value to Face Value	Period Outstanding	Weighted Average No. of Shares
1	**2**	**3**	**4**	**5 = 2 × 3 × 4 / 12**
1st Apr	18,00,000 (Partly Paid)	₹ 5 ÷ ₹ 10 = 50%	5 Mths (Upto 31st Aug)	3,75,000
1st Sep	14,40,000 (Fully Paid)	₹ 100 ÷ ₹ 100 = 100%	7 Mths (Upto 31st Mar)	8,40,000
	3,60,000 (Partly Paid)	₹ 50 ÷ ₹ 100 = 50%	7 Mths (Upto 31st Mar)	1,05,000
Weighted Average No. of Shares				**13,20,000**

2. Basic EPS = $\dfrac{\text{Net Profit or Loss for the period attributable to Equity Shareholders}}{\text{Weighted Average Number of Equity Shares outstanding during the period.}}$

= ₹ 33,00,000 ÷ 13,20,000 = **₹ 2.50 per Share.**

Question 1(d): Treatment of Amortization of Intangible Asset – AS 26 5 Marks

Base Limited is showing an Intangible Asset at ₹ 85 Lakhs as on 1.4.2011. This Asset was acquired for ₹ 112 Lakhs on 1.4.2008 and the same was available for use, from that date. The Company has been following the policy of Amortization of the Intangible Asset over a period of 12 years on Straight Line Basis. Comment on the Accounting Treatment of the above with reference to the relevant Accounting Standard.

Solution: Also See Q No.26, Page 14.10 of "Ready Referencer on Advanced Accounting" for Group II

1. **Useful Life above 10 years:** As per AS – 26, there may be persuasive evidence in some cases that the useful life will be a specific period longer than ten years. In such cases the enterprise should –
   (a) Amortise the Intangible Asset over the best estimate of its useful life,
   (b) Estimate the recoverable amount of the Intangible Asset at least annually in order to identify any impairment loss, and
   (c) Disclose the reasons for overriding the presumptive period of 10 years and the factor(s) that played a significant role in determining the useful life of the asset.

2. **Analysis and Conclusion:**
   (a) If in the instant case, if the useful life of the Intangible Asset is 12 Years, then the Company may write off the balance of ₹ 85,00,000 over its remaining useful life.
   (b) However, if the useful life is already over, the entire amount may be written off during the current year itself.

Question 4(a): Calculation of Provisions & Contingencies and Preparation of Profit & Loss A/c of a Bank 8 Marks

From the following information, calculate the amount of Provision and Contingencies and prepare Profit and Loss Account of Hamara Bank Limited" for the year ending 31st March, 2010.

Particulars	₹ In Lakhs	Particulars	₹ In Lakhs
Interest and Discount	4,430	Interest expended	1,360
Other Income	125	Operating Expenses	1,331
Interest Accrued on Investments	10		

Additional Information:

(i) Rebate on bills discounted to be provided for ₹ 15 Lakhs

(ii) Classification of Advances

Standard Assets – ₹ 2,500 Lakhs

Sub-Standard Assets – ₹ 560 Lakhs

Doubtful Assets not covered by security – ₹ 255 Lakhs

Doubtful Assets covered by security

For 1 year – ₹ 25 Lakhs

For 2 years – ₹ 50 Lakhs

For 3 years – ₹ 75 Lakhs

Loss Assets – ₹ 100 Lakhs

(iii) Make Tax Provisions @ 35% of the profit

(iv) Profit and Loss Account (Cr.) brought forward from previous year – ₹ 40 Lakhs.

Solution:

Profit and Loss Account of Hamara Bank Limited for the year ending 31.12.2010 (₹ In Lakhs)

Particulars	Sch. No.	31.03.10	31.03.09
I. Income			
Interest earned	13	4,425.00	
Other Income	14	125.00	
Total		**4,550.00**	
II. Expenditure			
Interest expended	15	1,360.00	
Operating expenses	16	1,331.00	
Provisions and Contingencies (including Provision for Tax) [₹ 4,550 – (₹ 1,360 + ₹ 1,331 + ₹ 546)] × 35% **Plus** ₹ 546 Provision for Risk Assets		1,005.55	
Total		**853.45**	
III. Profit / Loss			
Net Profit for the year		853.45	
Profit / (Loss) Brought Forward		40.00	
Total		**893.45**	
IV. Appropriations:		**--**	

Schedule to the Profit and Loss Account for the year ending 31.12.2004 (₹ In Lakhs)

Particulars	31.12.10	31.03.09
Schedule 13 – Interest Earned		
Interest / Discount [4,430 – 15]	4,415	
Income on Investment	10	
Total	**4,425**	
Schedule 14 – Other Income		
Commission Exchange and Brokerage	—	
Profit on Sale of Investments	—	
Other Income	125	
Total	**125**	
Schedule 15 – Interest Expended		
Interest on Deposits	1,360	
Interest on RBI / Inter-bank Borrowings	—	
Total	**1,360**	
Schedule 16 – Operating Expenses		
Total of Operating Expenses	1,331	
Total	**1,331**	

Working Note:

1. Computation of Provision for Risk Assets:

Classification of Assets	Rate	(₹ in Lakhs)	Provision – (₹ in Lakhs)
Standard Assets	0.40%	2,500	10
Sub–Standard	10%	560	56
Doubtful Assets not covered by Security	100%	255	255
Doubtful Assets covered by Security			
1 Year	20%	25	5
2 Years	30%	50	15
3 Years	30%	100	30
4 Years	100%	75	75
Loss Assets	100%	100	100
Total			**546**

Question 5(a): Replacement of Power House – Replacement Account – Electricity Company 8 Marks

Jaipur Electric Company Limited rebuilt and re-equipped a part of their Power House at the Cost of ₹ 85 Lakhs. The part of the Old Power House thus superseded originally costed ₹ 50 Lakhs, but if erected at the present time would cost 40% more. ₹ 3 Lakhs is realized from the sale of old materials. Old materials worth ₹ 6 Lakhs are used in the reconstruction and are included in the cost of ₹ 85 lakhs above.

Give necessary Journal Entries for recording the above transactions in the books of the Company, indicating the allocations between amount to be Capitalized and amount to be Written Off to Revenue Account.

Solution:

1. Current Cost of Replacement

Particulars	Amount	Increase in cost		Current cost
		Rate	Amount ₹	
Cost of the existing Power House	50,00,000	40%	20,00,000	70,00,000
Estimated Current Cost for Replacement of Power House (amount to be charged to Replacement Account)	**50,00,000**		**20,00,000**	**70,00,000**

2. Additional Cost of Reconstruction (To be Capitalized)

	Particulars	₹
	Cost of re-building	85,00,000
Less:	Estimated Current Cost for replacement of Power House	70,00,000
	Additional Cost of New Main to be Capitalized (excluding Old Materials used)	**15,00,000**

3. Journal Entries

SNo	Particulars	Debit ₹	Credit ₹
1.	Replacement A/c Dr. To Bank A/c (Being current cost of replacement charged to replacement account)	70,00,000	70,00,000
2.	New Power House A/c [₹ 15,00,000 – ₹ 6,00,000] Dr. To Bank A/c (Being balance amount capitalized)	9,00,000	9,00,000
3.	New Power House A/c Dr. To Replacement A/c (Being value of old Materials used in reconstruction)	6,00,000	6,00,000
4.	Bank A/c Dr. To Replacement A/c (Being the amount realized from sale of old materials credited to Replacement A/c)	3,00,000	3,00,000
5.	Revenue Account Dr. To Replacement A/c (Being the net current cost of replacement transferred to revenue account)	61,00,000	61,00,000

4. Replacement Account

Particulars	₹	Particulars	₹
To Bank A/c	70,00,000	By New Power House A/c By Bank A/c By Revenue A/c – **Balancing Figure**	6,00,000 3,00,000 61,00,000
Total	**70,00,000**	**Total**	**70,00,000**

Question 6(a): Computation of Profits of Branch and Head Office – Branch Accounts 8 Marks

N Limited has a Retail Branch at Noida. Goods are sold to Customers at Cost plus 100%. The Wholesale Price is Cost Plus 80%. Goods are invoiced to Noida at Wholesale Price. From the following particulars, find out the Profit made by the Head Office and Noida Branch for the year ended 31st March, 2010 using Invoice Method.

Particulars	Head Office (₹)	Noida (₹)
Stock on April 1, 2009	50,000	–
Purchases	3,00,000	–
Goods Sent to Branch (at Invoice Value)	1,08,000	–
Sales	3,06,000	1,00,000
Expenses	90,000	4,000

Sales at Head Office are made only on Wholesale basis and Sales at Branch are made only to Customers. Stock at Branch is valued at Invoice Price.

Solution:

1. Computation of Branch Closing Stock at Invoice Price

	Particulars	₹
	Invoice value of goods sent to Branch	1,08,000
Less:	Invoice value of goods sold by branch (₹ 1,00,000 × 180 ÷ 200)	(90,000)
	Branch Closing Stock (at Invoice Price)	**18,000**

2. Computation of Head Office Closing Stock

	Particulars	₹
	Opening Stock	56,000
Add:	Purchases	3,00,000
		3,56,000
Less:	Cost of goods sold (₹ 3,06,000 × 100 ÷ 180) (Sales by HO)	(1,70,000)
		1,86,000
Less:	Cost of goods sent to branch (₹ 1,08,000 × 100 ÷ 180)	(60,000)
	Head Office Closing Stock	**1,26,000**

3. Trading and Profit and Loss Account for the year ended on 31.12.2010

Particulars	HO	Branch	Particulars	HO	Branch
To Opening Stock	56,000	NIL	By Sales	3,06,000	1,00,000
To Purchases	3,00,000	NIL	By Goods Sent to Branch	1,08,000	—
To Goods received from HO	—	1,08,000	By Closing Stock	1,26,000	18,000
To Gross Profit	1,84,000	10,000			
Total	**5,40,000**	**1,18,000**	**Total**	**5,40,000**	**1,18,000**
To Expenses	90,000	4,000	By Gross Profit	1,84,000	10,000
To Net Profit	94,000	6,000			
Total	**1,84,000**	**10,000**	**Total**	**1,84,000**	**10,000**

Note: The Closing Stock of the Branch is in the Invoice Price due to the requirement of the question.

Question 6(b): Liability of Underwriter – Par Issue — 8 Marks

Rising Sun Limited came up with an issue of 25,00,000 Equity Shares of ₹ 10 each at par. 4,00,000 Shares were issued to the Promoters and balance offered to the Public. Issue was Underwritten by three Underwriters A & Co, B & Co, and C & Co, equally, with Firm Underwriting of 1,00,000 Shares each. Subscription totaled 17,26,000 Shares, including the marked forms which were as under :

A & Co – 5,18,000 Shares, B & Co – 5,50,000 Shares, C & Co – 4,72,000 Shares

The Underwriters had applied for the number of shares covered by Firm Underwriting. The amount payable on application and allotment were ₹ 3 & ₹ 2 respectively. The agreed Commission is 3%.

You are required to calculate:

1. The Liability of each Underwriter.
2. The amount Payable and/or Receivable by the Underwriters.

Solution: Also See Q No.26, Page 5.51 of "Ready Referencer on Advanced Accounting" for Group II

1. Statement of Underwriters Liability (Figures in No. of Shares)

	Particulars	A & Co	B & Co	C & Co	Total
	Gross Liability	7,00,000	7,00,000	7,00,000	21,00,000
Less:	Unmarked Applications **[W.N. 1]**	(62,000)	(62,000)	(62,000)	(1,86,000)
		6,38,000	6,38,000	6,38,000	19,14,000
Less:	Marked Applications	(5,18,000)	(5,50,000)	(4,72,000)	(15,40,000)
		1,20,000	88,000	1,66,000	3,74,000
Less:	Firm Underwriting	(1,00,000)	(1,00,000)	(1,00,000)	(3,00,000)
	Balance to be taken under Contract	20,000	(12,000)	66,000	74,000
Adjust:	B & Co's Surplus transferred in Gross Liability Ratio (equally)	(6,000)	12,000	(6,000)	—
	Net Liability	**14,000**	—	**60,000**	**74,000**
Add:	Firm Underwriting	1,00,000	1,00,000	1,00,000	3,00,000
	Total Liability	**1,14,000**	**1,00,000**	**1,60,000**	**3,74,000**
	Amt Due upto allotment at 5 per Share (₹)	5,70,000	5,00,000	8,00,000	18,70,000
Less:	Amount paid for Firm Underwriting for 1,00,000 Shares at ₹ 3 per Share (₹)	(3,00,000)	(3,00,000)	(3,00,000)	(9,00,000)
	Balance Due from Underwriters	2,70,000	2,00,000	5,00,000	9,70,000
Less:	Underwriting Commission payable by Co. **[W.N. 2]**	(2,10,000)	(2,10,000)	(2,10,000)	(6,30,000)
	Amount Due from / (P'ble to) Underwriters	**60,000**	**(10,000)**	**2,90,000**	3,40,000

Working Notes:

1. Unmarked Applications = **1,86,000** i.e. Total Applications 17,26,000 – Marked Applications (5,18,000 + 5,50,000 + 4,72,000 = 15,40,000). These are distributed in the ratio of Gross Liability i.e. **equally.**

2. The Commission Payable is calculated on Shares issued to public at par value.

Question 7(a): Treatment of Revision in an Accounting Estimate – AS 5 — 4 Marks

A Limited company created a Provision for Bad and Doubtful Debts at 5% on Debtors in preparing the Financial Statements for the year 2009–2010. Subsequently on a review of the credit period allowed and financial capacity of the customers, the Company decided to increase the provision to 10% on Debtors as on 31.03.2010. The Accounts are not approved by the Board of Directors till the date of decision. While applying the relevant Accounting Standard, can this revision be considered as an Extraordinary Item or Prior Period Item?

Solution: Also See Q No.35, Page 14.14 of "Ready Referencer on Advanced Accounting" for Group II & Q No.29, Page 86 of "Workbook for Classroom discussion"

1. **Estimate:** Creating a provision for Doubtful Debts at 5% on Debtors is an accounting estimate. An Accounting Estimate may have to be revised – (a) If there are changes in circumstances on which the estimate was based, or (b) as a result of new information, more experience, or subsequent developments.

2. **Disclosure of Change in Accounting Estimates:** The effect of a change in an accounting estimate should be included in the determination of Net Profit or Loss in –
   (a) The period of the change, if the change affects the period only, e.g. Bad Debts.
   (b) The period of the change and future periods, if the change affects both, e.g. Useful Life of assets.

3. **Conclusion:** The above disclosure is sufficient, i.e. change in provisioning from 5% to 10%. The change in provisioning is neither an Extraordinary Item nor a Prior Period Item.

Question 7(b): Payment of Dividend in Case of a Banking Company 4 Marks

What are the restrictions imposed by the Banking Regulations Act, 1949 on payment of Dividend in case of Banking Companies?

Solution: Also See Q No.14, Page 10.9 of "Ready Referencer on Advanced Accounting" for Group II

1. **Condition:** The Banking Company has to completely write-off all its capitalized expenses including Preliminary Expenses, Organisation Expenses, Share Selling Commission, Losses incurred by Tangible Assets.

2. **Excluded Items: The following need not be written off for declaration of dividend:**
   (a) Depreciation in the value of investment in approved securities in cases where such depreciation has not actually been capitalized or accounted for as a loss;
   (b) Depreciation in value of investment in Shares / Debentures / Bonds (other than approved securities) where adequate provision for depreciation has been made;
   (c) Bad Debts where adequate provision for such debts has been made.

Question 7(c)(ii): Events Occurring after the Balance Sheet Date – AS 4 2 Marks

In preparing the Financial Statements of Lotus Limited for the year ended 31st March, 2010 you come across the following information. State with reason, how you would deal with it in the Financial Statements?

The Company invested ₹ 50 Lakhs in April, 2010 in the acquisition of another Company doing similar Business, the negotiations for which had just started.

Solution: Also See Q No.5, Page 13.2 of "Ready Referencer on Advanced Accounting" for Group II

1. **Nature of Event:** The acquisition of another Company is an event occurring after the Balance Sheet date. However, no adjustment to assets and liabilities is required, as the event **does not** affect the determination and the condition of the amounts stated in the Financial Statements for the year ended 31st March.

2. As per AS – 4, disclosure should be made in the report of the approving authority of those events occurring after the Balance Sheet date that represent material changes and commitments affecting the financial position of the enterprise. Hence, the investment of ₹ 50 Lakhs in April in the acquisition of another Company should be **disclosed** in the report of the Board of Directors.

STUDENTS' NOTES

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