PAPER – 1 : ADVANCED ACCOUNTING

QUESTIONS

Branch Accounting

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

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

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

(i) Nagpur Branch Stock Account

(ii) Nagpur Branch Debtors Account

(iii) Nagpur Branch Adjustment Account.

Also compute shortage of Stock at Branch, if any.

Departmental Accounts

2. FGH Ltd. has three departments I.J.K. The following information is provided for the year ended 31.3.2008:

	I	J	K
	Rs.	Rs.	Rs.
Opening stock	5,000	8,000	19,000
Opening reserve for unrealised profit	—	2,000	3,000

Materials consumed	16,000	20,000	—
Direct labour	9,000	10,000	—
Closing stock	5,000	20,000	5,000
Sales	—	—	80,000
Area occupied (sq. mtr.)	2,500	1,500	1,000
No. of employees	30	20	10

Stocks of each department are valued at costs to the department concerned. Stocks of I are transferred to J at cost plus 20% and stocks of J are transferred to K at a gross profit of 20% on sales. Other common expenses are salaries and staff welfare Rs. 18,000, rent Rs. 6,000.

Prepare Departmental Trading, Profit and Loss Account for the year ending 31.3.2008.

Partnership Accounts

3. Firm X & Co. consists of partners A and B sharing Profits and Losses in the ratio of 3 : 2. The firm Y & Co. consists of partners B and C sharing Profits and Losses in the ratio of 5 : 3.

On 31st March, 2008 it was decided to amalgamate both the firms and form a new firm XY & Co., wherein A, B and C would be partners sharing Profits and Losses in the ratio of 4:5:1.

Balance Sheet as at 31.3.2008

Liabilities	X & Co.,	Y & Co.	Assets	X & Co.	Y & Co.
	Rs.	Rs.		Rs.	Rs.
Capital:			Cash in hand/bank	40,000	30,000
A	1,50,000	---	Debtors	60,000	80,000
B	1,00,000	75,000	Stock	50,000	20,000
C	---	50,000	Vehicles	---	90,000
Reserve	50,000	40,000	Machinery	1,20,000	---
Creditors	1,20,000	55,000	Building	1,50,000	---
	4,20,000	2,20,000		4,20,000	2,20,000

The following were the terms of amalgamation:

(i) Goodwill of X & Co., was valued at Rs.75,000. Goodwill of Y & Co. was valued at Rs.40,000. Goodwill account not to be opened in the books of the new firm but adjusted through the Capital accounts of the partners.

(ii) Building, Machinery and Vehicles are to be taken over at Rs.2,00,000, Rs.1,00,000 and Rs.74,000 respectively.

(iii) Provision for doubtful debts at Rs.5,000 in respect of X & Co. and Rs.4,000 in respect of Y & Co. are to be provided.

You are required to:

(i) Show, how the Goodwill value is adjusted amongst the partners.

(ii) Prepare the Balance Sheet of XY & Co. as at 31.3.2008 by keeping partners capital in their profit sharing ratio by taking capital of 'B' as the basis. The excess or deficiency to be kept in the respective Partners' Current account.

Self-Balancing Ledgers

4. From the following information prepare Sales Ledger Adjustment Account and Bought Ledger Adjustment Account in the General Ledger:

On 1.4.2007 balance in bought ledger (Dr.) Rs. 10,000, (Cr.) Rs. 96,000, balance in sales ledger (Dr.) Rs. 1,41,880 (Cr.) Rs. 2,240:

31.3.2008	Rs.	31.3.2008	Rs.
Purchases	5,40,000	Discount received	7,200
Purchases return	20,000	Bills receivable received	40,000
Total sales	7,68,000	Bills payable issued	22,400
Cash sales	40,000	Reserve for doubtful debts	9,160
Sales return	10,000	Cash paid to customers	1,840
Cash received from customers	6,24,000	Bills receivable dishonoured	6,000
Discount allowed	11,200	Bought ledger balance	10,400
Cash paid to suppliers	4,80,000	Sales ledger balanced	1,83,200
Transfer from sales to bought ledger	20,800		

Hire Purchase Accounting

5. ABC Ltd. sells goods on Hire-purchase by adding 50% above cost. From the following particulars, prepare Hire-purchase Trading account to reveal the profit for the year ended 31.3.2008:

		Rs.
1.4.2007	Instalments due but not collected	10,000
1.4.2007	Stock at shop (at cost)	36,000
1.4.2007	Instalment not yet due	18,000

31.3.2008	Stock at shop	40,000
31.3.2008	Instalments due but not collected	18,000

Other details:

Total instalments became due	1,32,000
Goods purchased	1,20,000
Cash received from customers	1,21,000

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

Account Current

6. Mr. A owed Rs. 4,000 on 1st January, 2008 to Mr. X. The following transactions took place between them. It is agreed between the parties that interest @ 10% p.a. is to be calculated on all transactions.

	Rs.
15 January, 2008 Mr. X sold goods to Mr. A	2,230
29 January, 2008 Mr. X bought goods from Mr. A	1,200
10 February, 2008 Mr. A paid cash to Mr. X	1,000
13 March, 2008 Mr. A accepted a bill drawn by Mr. X for one month	2,000

They agree to settle their complete accounts by one single payment on 15th March, 2008. Prepare Mr. A in Account Current with Mr. X and ascertain the amount to be paid. Ignore days of grace.

Underwriting of Shares

7. Scorpio Ltd. came out with an issue of 45,00,000 equity shares of Rs. 10 each at a premium of Rs. 2 per share. The promoters took 20% of the issue and the balance was offered to the public. The issue was equally underwritten by A & Co; B & Co. and C & Co.

   Each underwriter took firm underwriting of 1,00,000 shares each. Subscriptions for 31,00,000 equity shares were received with marked forms for the underwriters as given below:

A & Co.		7,25,000 shares
B & Co.		8,40,000 shares
C & Co.		13,10,000 shares
	Total	28,75,000 shares

The underwriters are eligible for a commission of 5% on face value of shares. The entire amount towards shares subscription has to be paid alongwith application. You are required to:

(a) Compute the underwriters liability (number of shares)

(b) Compute the amounts payable or due to underwriters.

Bonus Issue

8. The Balance Sheet of A Ltd. as at 31.3.2008 is as follows:

Balance Sheet as at 31.3.2008

Liabilities	Rs.	Assets	Rs.
Authorised Share Capital		Sundry Assets	17,00,000
1,50,000 Equity Shares of Rs. 10 each	15,00,000		
Issued, Subscribed and Paid-up			
80,000 Equity Shares of			
Rs. 7.50 each called-up and paid-up	6,00,000		
Reserves and surplus			
Capital Redemption Reserve	1,50,000		
Plant Revaluation Reserve	20,000		
Securities Premium Account	1,50,000		
Development Rebate Reserve	2,30,000		
Investment Allowance Reserve	2,50,000		
General Reserve	3,00,000		
	17,00,000		17,00,000

The company wanted to issue bonus shares to its share holders at the rate of one share for every two shares held. Necessary resolutions were passed; requisite legal requirements were complied with:

(a) You are required to give effect to the proposal by passing journal entries in the books of A Ltd.

(b) Show the amended Balance Sheet.

Redemption of Debenture

9 Alpha Limited recently made a public issue in respect of which the following information is available:

(a) No. of partly convertible debentures issued 2,00,000; face value and issue price Rs.100 per debenture.

(b) Convertible portion per debenture 60%, date of conversion on expiry of 6 months from the date of closing of issue.

(c) Date of closure of subscription lists 1.5.2008, date of allotment 1.6.2008, rate of interest on debenture 15% payable from the date of allotment, value of equity share for the purpose of conversion Rs. 60 (Face Value Rs. 10).

(d) Underwriting Commission 2%.

(e) No. of debentures applied for 1,50,000.

(f) Interest payable on debentures half-yearly on 30th September and 31st March.

Write relevant journal entries for all transactions arising out of the above during the year ended 31st March, 2009 (including cash and bank entries).

Buy-back of Shares

10. The Balance Sheet of Gunshot Ltd. as on 31.3.2008 is given :

(Rs. In '000)

Liabilities	Amount	Fixed Assets	Amount
Share Capital :		Fixed Assets	2,700
Equity shares of Rs. 10 each	800	Non-trade Investments	300
Securities Premium	100	Stock	600
General Reserve	780	Sundry Debtors	360
Profit and Loss Account	120	Cash and Bank	160
10% Debenture	2,000		
Creditors	320		
	4,120		4,120

Gunshot Ltd. buy back 16,000 shares of Rs. 20 per share. For this purpose, the Company sold its all non-trade investments for Rs. 3, 20,000. Give Journal Entries with full narrations effecting the buy back.

Amalgamation of Companies

11. The financial position of two companies Hari Ltd. and Vayu Ltd. as on 31st March, 2008 was as under:

Assets	Hari Ltd. (Rs.)	Vayu Ltd. (Rs.)
Goodwill	50,000	25,000
Building	3,00,000	1,00,000
Machinery	5,00,000	1,50,000
Stock	2,50,000	1,75,000

Debtors	2,00,000	1,00,000
Cash at Bank	50,000	20,000
Preliminary Expenses	30,000	10,000
	13,80,000	5,80,000
Liabilities		
Share Capital:	Hari Ltd. (Rs.)	Vayu Ltd. (Rs.)
Equity Shares of Rs. 10 each	10,00,000	3,00,000
9% Preference Shares of Rs. 100 each	1,00,000	–
10% Preference Shares of Rs. 100 each	–	1,00,000
General Reserve	1,00,000	80,000
Retirement Gratuity fund	50,000	20,000
Sundry Creditors	1,30,000	80,000
	13,80,000	5,80,000

Hari Ltd. absorbs Vayu Ltd. on the following terms:

(a) 10% Preference Shareholders are to be paid at 10% premium by issue of 9% Preference Shares of Hari Ltd.

(b) Goodwill of Vayu Ltd. is valued at Rs. 50,000, Buildings are valued at Rs. 1,50,000 and the Machinery at Rs. 1,60,000.

(c) Stock to be taken over at 10% less value and Reserve for Bad and Doubtful Debts to be created @ 7.5%.

(d) Equity Shareholders of Vayu Ltd. will be issued Equity Shares @ 5% premium.

Prepare necessary Ledger Accounts to close the books of Vayu Ltd. and show the acquisition entries in the books of Hari Ltd. Also draft the Balance Sheet after absorption as at 31st March, 2008.

Internal Reconstruction of Company

12. Following is the Balance Sheet as at March 31, 2008:

(Rs. '000)

Liabilities	Max Ltd.	Mini Ltd.	Assets	Max Ltd.	Mini Ltd.
Share capital:			Goodwill	20	–
Equity shares of Rs. 100 each	1,500	1,000	Other fixed assets	1,500	760
9% Preference shares of Rs. 100 each	500	400	Debtors	651	440
			Stock	393	680
General reserve	180	170	Cash at bank	26	130

Profit and loss account	–	15	Own debenture (Nominal value Rs. 2,00,000)	192	
12% Debentures of Rs. 100 each	600	200			
Sundry creditors	415	225	Discount on issue of debentures	2	
			Profit and loss account	411	
	3,195	2,010		3,195	2,010

On 1.4.2008, Max Ltd. adopted the following scheme of reconstruction:

(i) Each equity share shall be sub-divided into 10 equity shares of Rs. 10 each fully paid up. 50% of the equity share capital would be surrendered to the Company.

(ii) Preference dividends are in arrear for 3 years. Preference shareholders agreed to waive 90% of the dividend claim and accept payment for the balance.

(iii) Own debentures of Rs. 80,000 were sold at Rs. 98 cum-interest and remaining own debentures were cancelled.

(iv) Debentureholders of Rs. 2,80,000 agreed to accept one machinery of book value of Rs. 3,00,000 in full settlement.

(v) Creditors, debtors and stocks were valued at Rs. 3,50,000, Rs. 5,90,000 and Rs. 3,60,000 respectively. The goodwill, discount on issue of debentures and Profit and Loss (Dr.) are to be written off.

(vi) The Company paid Rs. 15,000 as penalty to avoid capital commitments of Rs. 3,00,000.

On 2.4.2008 a scheme of absorption was adopted. Max Ltd. would take over Mini Ltd. The purchase consideration was fixed as below:

(a) Equity shareholders of Mini Ltd. will be given 50 equity shares of Rs. 10 each fully paid up, in exchange for every 5 shares held in Mini Ltd.

(b) Issue of 9% preference shares of Rs. 100 each in the ratio of 4 preference shares of Max Ltd. for every 5 preference shares held in Mini Ltd.

(c) Issue of one 12% debenture of Rs. 100 each of Max Ltd. for every 12% debentures in Mini Ltd.

You are required to give Journal entries in the books of Max Ltd. and draw the resultant Balance Sheet as at 2nd April, 2008.

Liquidation of Companies

13. The position of Valueless Ltd. on its liquidation is as under:

Issued and paid up Capital:

3,000 11% preference shares of Rs. 100 each fully paid.

3,000 Equity shares of Rs. 100 each fully paid.

1,000 Equity shares of Rs. 50 each Rs. 30 per share paid.

Calls in Arrears are Rs. 10,000 and Calls received in Advance Rs. 5,000. Preference Dividends are in arrears for one year. Amount left with the liquidator after discharging all liabilities is Rs. 4,13,000. Articles of Association of the company provide for payment of preference dividend arrears in priority to return of equity capital. You are required to prepare the Liquidators final statement of account.

Electricity Companies

14. The following balances relate to NTPC. Ltd. and pertains to the accounts for the year ended on 31st December, 2008:

	(Rs.in lakhs)
Share Capital	200
Fixed Assets	400
Monthly Average of Current Assets	40
Reserve Fund (invested in 6% Govt. Securities Face Value Rs. 120 lakhs)	120
Contingencies Reserve (invested in 6% State Govt. Loans)	40
Loan from Electricity Board	60
Developments Reserve	20
10% Debentures	16
Depreciation Reserve on Fixed Assets	160
Security Deposits of Customers	150
Customers' Contribution to main lines	4
Preliminary Expenses	10
Tariffs and Dividend Control Reserve	12

The company earned a post tax profit of Rs. 20.4 lakhs. Indicate the disposal of profit, bearing in mind the provisions of the Electricity (Supply) Act, 1948, assuming the Reserve Bank of India rate on the relevant date was 8%.

Insurance Companies

15. Indian Insurance Co. Ltd. furnishes you with the following information :

(i) On 31.12.2006 it had reserve for unexpired risk to the tune of Rs. 40 crores. It comprised of Rs. 15 crores in respect of marine insurance business : Rs. 20 crores in respect of fire insurance business and Rs. 5 crores in respect of miscellaneous insurance business.

(ii) It is the practice of Indian Insurance Co. Ltd. to create reserves at 100% of net premium income in respect of marine insurance policies and at 50% of net premium income in respect of fire and miscellaneous income policies.

(iii) During 2007, the following business was conducted :

	Marine	Fire	Miscellaneous
	(Rs. in crores)		
	Rs.	Rs.	Rs.
Premia collected from :			
(a) Insureds in respect of policies issued	18	43	12
(b) Other insurance companies in respect of risks undertaken	7	5	4
Premia paid/payable to other insurance companies on business ceded	6.7	4.3	7

Indian Insurance Co. Ltd. asks you to :

(a) Pass journal entries relating to "Unexpired risks reserve".

(b) Show in columnar form "Unexpired risks reserve" a/c for 2007.

Banking Companies

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

	Rs. in lakhs
Assets	
Standard	20,000
Substandard	16,000
Doubtful	
For one year (secured)	6,000
For two years and three years (secured)	4,000
For more than three years (secured by mortgage of plant and machinery Rs.600 lakhs)	2,000
Non-recoverable Assets	1,500

Financial Statements of Not-for-Profit Organisations

17. Smith Library Society showed the following position on 31st March, 2007:

Balance Sheet as on 31st March, 2007

Liabilities	Rs.	Assets	Rs
Capital fund	7,93,000	Electrical fittings	1,50,000
Expenses payable	7,000	Furniture	50,000
		Books	4,00,000

		Investment in securities	1,50,000
		Cash at bank	25,000
		Cash in hand	25,000
	8,00,000		8,00,000

The receipts and payment account for the year ended on 31st March, 2008 is given below:

	Rs.		Rs.
To Balance b/d		By Electric charges	7,200
Cash at bank 25,000		By Postage and stationary	5,000
Cash in hand 25,000	50,000	By Telephone charges	5,000
To Entrance fees	30,000	By Books purchased	60,000
To Membership subscription	2,00,000	Bu Outstanding expenses paid	7,000
To Sale proceeds of old papers	1,500	By Rent	88,000
To Hire of lecture hall	20,000	By Investment in securities	40,000
To Interest on securities.	8,000	By Salaries	66,000
		By Balance c/d	
		Cash at bank	20,000
		Cash in hand	11,300
	3,09,500		3,09,500

You are required to prepare income and expenditure account for the year ended 31st March, 2008 and a balance sheet as at 31st, March, 2008 after making the following adjustments:

Membership subscription included Rs. 10,000 received in advance.

Provide for outstanding rent Rs. 4,000 and salaries Rs. 3,000.

Books to be depreciated @ 10% including additions. Electrical fittings and furniture are also to be depreciated at the same rate.

75% of the entrance fees is to be capitalized.

Interest on securities is to be calculated @ Rs. 5% p.a. including purchases made on 1.10.2007 for Rs. 40,000.

Insurance Claims

18. Mr. A prepares accounts on 30th September each year, but on 31st December, 2008 fire destroyed the greater part of his stock. Following information was collected from his book:

	Rs.
Stock as on 1.10.2008	29,700
Purchases from 1.10.2008 to 31.12.2008	75,000
Wages from 1.10.2008 to 31.12.2008	33,000
Sales from 1.10.2008 to 31.12.2008	1,40,000

The rate of gross profit is 33.33% on cost. Stock to the value of Rs. 3,000 was salvaged. Insurance policy was for Rs. 25,000 and claim was subject to average clause.

Additional information:

(i) Stock in the beginning was calculated at 10% less than cost.

(ii) A plant was installed by firm's own worker. He was paid Rs. 500, which was included in wages.

(iii) Purchases include the purchase of the plant for Rs. 5,000

You are required to calculate the claim for the loss of stock.

19. Answer the following questions (Give adequate working notes in support of your answer):

(i) The economic life of an enterprise is artificially split into periodic intervals in accordance with the going concern assumptions. Is the statement true or false?

(ii) If payment is made on the average due date, it results in loss of interest to creditors. Is the statement true or false?

(iii) During the year 2007-2008, a medium size manufacturing company wrote down its inventories to net realisable value by Rs. 5,00,000. Is a separate disclosure necessary in final accounts?

(iv) A, B and C are partners with profit sharing ratio 5:3:2. A wants to retire, B and C agreed to continue at 2:1. Find the profit gaining ratio between B and C.

(v) If there appears a sports fund, the expenses incurred on sports activities will be taken to income and expenditure account. State whether the statement is true or false.

(vi) All significant accounting policies adopted in preparation and presentation of financial statements must be disclosed. State whether the statement is true or false.

(vii) A, B and C share profits and losses in the proportion of 6/14, 5/14 and 3/14 respectively: They agree to take D into partnership and give him $1/8^{th}$ share. Compute new profit sharing ratio between A B, C and D.

(viii) As per the decision in Garner vs. Murray the loss on account of insolvency of a partner should be borne by the solvent partners in their profit sharing ratio. State the validity of the statement.

(ix) A Ltd. take over B Ltd. on April 01, 2007 and discharges consideration for the business as follows:

(a) Issued 42,000 fully paid equity shares of Rs. 10 each at par to the equity shareholders of B Ltd.

(b) Issued fully paid up 15% preference shares of Rs. 100 each to discharge the preference shareholders (Rs. 1,70,000) of B Ltd. at a premium of 10%.

(c) It is agreed that the debentures of B Ltd. (Rs. 50,000) will be converted into equal number and amount of 13% debentures of A Ltd.

Calculate the amount of purchase consideration.

Theory question

20. (i) Fixed capital and fluctuating capital of partners.

(ii) Conditions to be fulfilled by a joint stock company for issue of sweat equity shares.

(iii) Contents of a 'liquidator's final statement of account'.

(iv) Classification of advances in case of banking company.

(v) Computation of 'premium income'; 'claim expenses' and 'commission expenses' in case of an insurance company.

(vi) Characteristics of 'Double accounts system of presentation of financial information'.

(vii) How will you choose a pre-packaged accounting software? Explain in brief.

(viii) Describe the method of calculation of profit or loss on disposal of investments.

(ix) Explain the purpose and status of the conceptual framework for preparation and presentation of financial statements in brief.

(x) Write short note on red ink interest in the context of account current.

Theory Question Based on Accounting Standards

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

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

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

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

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

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

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

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

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

(i) Ordinary activities.

(ii) Extraordinary Activities.

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

Practical Problems based on Accounting Standards

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

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

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

(Accounting year 1.1.2007 – 31.12.2007)

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

(c) At the end of the financial year ending on 31st December, 2008, a company finds that there are twenty law suits outstanding which have not been settled till the date of approval of accounts by the Board of Directors. The possible outcome as estimated by the Board is as follows:

	Probability	Loss (Rs.)
In respect of five cases (Win)	100%	–
Next ten cases (Win)	60%	–
Lose (Low damages)	30%	1,20,000
Lose (High damages)	10%	2,00,000
Remaining five cases		
Win	50%	–
Lose (Low damages)	30%	1,00,000
Lose (High damages)	20%	2,10,000

Outcome of each case is to be taken as a separate entity. Ascertain the amount of contingent loss and the accounting treatment in respect thereof.

(d) An equipment is leased for 3 years and its useful life is 5 years. Both the cost and the fair value of the equipment are Rs. 3,00,000. The amount will be paid in 3 instalments and at the termination of lease lessor will get back the equipment. The unguaranteed residual value at the end of 3 years is Rs. 40,000. The (internal rate of return) IRR of the investment is 10%. The present value of annuity factor of Re. 1 due at the end of 3rd year at 10% IRR is 2.4868. The present value of Re. 1 due at the end of 3rd year at 10% rate of interest is 0.7513.

(i) State with reason whether the lease constitutes finance lease.

(ii) Calculate unearned finance income.

23. (i) A firm of contractors obtained a contract for construction of bridges across river Revathi. The following details are available in the records kept for the year ended 31st March, 2009.

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

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

(ii) The Board of Directors decided on 31.3.2008 to increase the sale price of certain items retrospectively from 1st January, 2008. In view of this price revision with effect from 1st January 2008, the company has to receive Rs. 15 lakhs from its customers in respect of sales made from 1st January, 2008 to 31st March, 2008 and the Accountant cannot make up his mind whether to include Rs. 15 lakhs in the sales for 2007-2008.

(iii) ABC Ltd. is constructing a fixed asset. Following are the expenses incurred on the construction:

Materials	Rs. 10,00,000
Direct Expenses	Rs. 2,50,000
Total Direct Labour	Rs. 5,00,000
(1/10th of the total labour time was chargeable to the construction)	
Total office & administrative expenses	Rs. 8,00,000
(5% is chargeable to the construction)	
Depreciation on the assets used for the construction of this assets	Rs. 10,000

Calculate the cost of fixed assets.

(iv) Top & Top Limited has set up its business in a designated backward area which entitles the company to receive from the Government of India a subsidy of 20% of the cost of investment. Having fulfilled all the conditions under the scheme, the company on its investment of Rs. 50 crore in capital assets, received Rs. 10 crore from the Government in January, 2008 (accounting period being 2007-2008). The company wants to treat this receipt as an item of revenue and thereby reduce the losses on profit and loss account for the year ended 31st March, 2008.

Keeping in view the relevant Accounting Standard, discuss whether this action is justified or not.

24. (i) X Co. Limited purchased goods at the cost of Rs.40 lakhs in October, 2007. Till March, 2008, 75% of the stocks were sold. The company wants to disclose closing stock at Rs.10 lakhs. The expected sale value is Rs.11 lakhs and a commission at 10% on sale is payable to the agent. Advise, what is the correct closing stock to be disclosed as at 31.3.2008.

(ii) Arjun Ltd. sold farm equipments through its dealers. One of the conditions at the time of sale is, payment of consideration in 14 days and in the event of delay interest is chargeable @ 15% per annum. The Company has not realized interest from the dealers in the past. However, for the year ended 31.3.2008, it wants to recognise interest due on the balances due from dealers. The amount is ascertained at Rs.9 lakhs. Decide whether the income by way of interest from dealers is eligible for recognition as per AS 9.

(iii) AB Ltd. launched a project for producing product X in October, 2006. The Company incurred Rs.20 lakhs towards Research and Development expenses upto 31st March, 2008. Due to prevailing market conditions, the Management came to conclusion that the product cannot be manufactured and sold in the market for the next 10 years. The Management hence wants to defer the expenditure write off to future years.

Advise the Company as per the applicable Accounting Standard.

(iv) J Ltd. purchased machinery from K Ltd. on 30.09.2007. The price was Rs. 370.44 lakhs after charging 8% Sales-tax and giving a trade discount of 2% on the quoted price. Transport charges were 0.25% on the quoted price and installation charges come to 1% on the quoted price.

A loan of Rs. 300 lakhs was taken from the bank on which interest at 15% per annum was to be paid.

Expenditure incurred on the trial run was Materials Rs. 35,000, Wages Rs. 25,000 and Overheads Rs. 15,000.

Machinery was ready for use on 1.12.2007. However, it was actually put to use only on 1.5.2008. Find out the cost of the machine and suggest the accounting treatment for the expenses incurred in the interval between the dates 1.12.2007 to 1.5.2008. The entire loan amount remained unpaid on 1.5.2008.

25. (i) ABC Ltd. could not recover Rs. 10 lakhs from a debtor. The company is aware that the debtor is in great financial difficulty. The accounts of the company were finalized for the year ended 31.3.2008 by making a provision @ 20% of the amount due from the said debtor.

The debtor became bankrupt in April, 2008 and nothing is recoverable from him.

Do you advise the company to provide for the entire loss of Rs. 10 lakhs in the books of account for the year ended 31st March, 2008?

(ii) X Co. Ltd. signed an agreement with its employees union for revision of wages in June, 2008. The wage revision is with retrospective effect from 1.4.2004. The arrear wages upto 31.3.2008 amounts to Rs. 80 lakhs. Arrear wages for the period from 1.4.2008 to 30.06.2008 (being the date of agreement) amounts to Rs. 7 lakhs.

Decide whether a separate disclosure of arrear wages is required.

(iii) Ram Co. (P) Ltd. furnishes you the following information for the year ended 31.3.2008:

Depreciation for the year ended 31.3.2008 (under straight line method)	Rs. 100 lakhs
Depreciation for the year ended 31.3.2008 (under written down value method)	Rs. 200 lakhs
Excess of depreciation for the earlier years calculated under written down value method over straight line method	Rs. 500 lakhs

The Company wants to change its method of claiming depreciation from straight line method to written down value method.

Decide, how the depreciation should be disclosed in the Financial Statement for the year ended 31.3.2008.

SUGGESTED ANSWERS/HINTS

1. In the books of head office

Nagpur Branch Stock Account

		Rs.			Rs.
1.4.2007	To Balance b/d	24,000	31.3.08	By Bank A/c (Cash Sales)	1,80,000
31.3.2008	To Goods sent to Branch A/c	4,80,000		By Branch Debtors (Credit Sales)	2,80,000
	To Branch Debtors	6,000		By Stock shortage: Branch P&L A/c 1,500* Branch Adjustment A/c (Loading) 500	2,000
				By Balance c/d	48,000
		5,10,000			5,10,000

Nagpur Branch Debtors Account

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

Nagpur Branch Adjustment Account

To Branch Stock A/c (loading of loss)	500*	By Stock Reserve A/c	6,000
To Stock Reserve	12,000	By Goods sent to Branch A/c	1,20,000
To Gross Profit c/d	1,13,500		
	1,26,000		1,26,000
To Branch Stock A/c		By Gross Profit b/d	1,13,500

(Cost of loss)	1,500		
To Branch Expenses	56,000		
To Net Profit			
(Transferred to General P & L A/c)	56,000		
	1,13,500		1,13,500

*Balancing figure.

Working Notes:

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

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

   = Rs.53,500 + Rs.1,500 + Rs.1,000 = Rs.56,000
6. Gross Profit

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

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

2. FGH Ltd.

Departmental Trading and Profit and Loss Account

for the year ended 31st March, 2008

		I	J	K	Total			I	J	K	Total
		Rs.	Rs.	Rs.	Rs.			Rs.	Rs.	Rs.	Rs.
To	Opening stock	5,000	8,000	19,000	32,000	By	Sales			80,000	80,000
To	Material consumed	16,000	20,000		36,000	By	Inter-departmental transfer	30,000	60,000		90,000
To	Direct labour	9,000	10,000		19,000	By	Closing stock	5,000	20,000	5,000	30,000
To	Inter-departmental transfer		30,000	60,000	90,000						
To	Gross profit	5,000	12,000	6,000	23,000						
		35,000	80,000	85,000	2,00,000			35,000	80,000	85,000	2,00,000
To	Salaries and staff welfare	9,000	6,000	3,000	18,000	By	Gross profit b/d	5,000	12,000	6,000	23,000
To	Rent	3,000	1,800	1,200	6,000	By	Net loss	7,000			7,000
To	Net profit		4,200	1,800	6,000						
		12,000	12,000	6,000	30,000			12,000	12,000	6,000	30,000
To	Net loss (I)				7,000	By	Stock reserve b/d (J + K)				5,000
To	Stock reserve (J+K) (Refer W.N.)				3,000	By	Net profit (J + K)				6,000
To	Balance transferred to Profit and loss account				1,000						
					11,000						11,000

Working Note:

Calculation of unrealized profit on closing stock

	Rs.
Stock reserve of J department	
Cost	30,000
Transfer from I department	30,000
	60,000
Stock of J department	20,000

Proportion of stock of I department = Rs. 20,000 $\times \frac{\text{Rs.30,000}}{\text{Rs.60,000}}$ = Rs.10,000

Stock reserve =Rs.10,000 $\times \frac{20}{120}$ = Rs.1667 (approx.)

Stock reserve of K department	Rs.
Stock transferred from J department	5,000
Less: Profit (stock reserve) 5,000 × 20%	1,000
Cost to J department	4,000

Proportion of stock of I department =Rs. 4,000 $\times \frac{\text{Rs.30,000}}{\text{Rs.60,000}}$ = Rs.2,000

Stock reserve = Rs.2,000 $\times \frac{20}{120}$ = Rs.333 (approx.)

Total stock reserve = Rs.1,000 + Rs.333 = Rs.1,333

3. (i) Adjustment for raising and writing off of goodwill

	Raised in old profit sharing ratio		Total	Written off in new ratio	Difference
	X & Co.	Y & Co.			
	3:2	5:3			
	Rs.	Rs.	Rs.	Rs.	Rs.
A.	45,000	---	45,000 Cr.	46,000 Dr.	1,000 Dr.
B.	30,000	25,000	55,000 Cr.	57,500 Dr.	2,500 Dr.
C	---	15,000	15,000 Cr.	11,500 Dr.	3,500 Cr.
	75,000	40,000	1,15,000	1,15,000	Nil

(ii) Balance Sheet of X Y & Co.(New firm) as on 31.3.2008

Liabilities	Rs.	Assets	Rs.
Capital Accounts:		Vehicle	74,000
A	1,72,000	Machinery	1,00,000
B	2,15,000	Building	2,00,000
C	43,000	Stock	70,000
Current Accounts:		Debtors	1,31,000
A	22,000	Cash & Bank	70,000
C	18,000		
Creditors	1,75,000		
	6,45,000		6,45,000

Working Notes:

1. Balance of Capital Accounts at the time of amalgamation of firms

X & Co. Profit and loss sharing ratio 3:2	A's Capital Rs..	B's Capital Rs.
Balance as per Balance Sheet	1,50,000	1,00,000
Add: Reserves	30,000	20,000
Revaluation profit (Building)	30,000	20,000
Less: Revaluation loss (Machinery)	(12,000)	(8,000)
Provision for doubtful debt.	(3,000)	(2,000)
	1,95,000	1,30,000

Y & Co. Profit and loss sharing ratio 5:3	B's Capital Rs.	C's Capital Rs.
Balance as per Balance sheet	75,000	50,000
Add: Reserves	25,000	15,000
Less: Revaluation (vehicle)	(10,000)	(6,000)
Provision for doubtful debts	(2,500)	(1,500)
	87,500	57,500

2. Balance of Capital Accounts in the balance sheet of the new firm as on 31.3.2008

		A Rs.	B Rs.	C Rs.
Balance b/d:	X & Co.	1,95,000	1,30,000	--
	Y & Co.	--	87,500	57,500

	1,95,000	2,17,500	57,500
Adjustment for goodwill	(1,000)	(2,500)	3,500
	1,94,000	2,15,000	61,000
Total capital Rs. 4,30,000 (B's capital* i.e. Rs.2,15,000 x 2) to be contributed in 4:5:1 ratio.	1,72,000	2,15,000	43,000
Transfer to Current Account	22,000	---	18,000

4. In the General Ledger

Sales Ledger Adjustment Account

Dr.					Cr.
		Rs.			Rs.
1.4.2007	To Balance b/d	1,41,880	1.4.2007	By Balance b/d	2,240
31.3.2008	To General ledger adjustment A/c:		31.3.2008	By General Ledger adjustment A/c:	
	Sales (Cr.)	7,28,000		Sales return	10,000
	Cash paid to customers	1,840		Cash from customers	6,24,000
	Bills receivable dishonoured	6,000		Discount allowed	11,200
	To Balance c/d	13,720		Transfer to bought ledger	20,800
				Bill receivable received	40,000
				By Balance c/d	1,83,200
		8,91,440			8,91,440

Bought Ledger Adjustment Account

Dr.					Cr.
		Rs.			Rs.
1.4.07	To Balance b/d	10,000	1.4.07	By Balance b/d	96,000
31.3.08	To General ledger adjustment A/c:		31.3.08	By General ledger adjustment A/c:	
	Purchases returns	20,000		Purchases	5,40,000

* B's Capital Rs.21,500 being one-half of the total capital of the firm.

	Cash paid	4,80,000	By Balance c/d	10,400
	Transfer from sales ledger	20,800		
	Discount received	7,200		
	Bills payable accepted	22,400		
To	Balance c/d	86,000		
		6,46,400		6,46,400

5. In the Books of ABC Ltd.

Hire Purchase Trading Account

for the year ended 31st March, 2008

Dr.							Cr.
			Rs.				Rs.
1.1.2007	To	Hire purchase stock	18,000	1.1.2007	By	Stock reserve (1/3 of Rs. 18,000)	6,000
1.1.2007 to 31.3.2008	To	Goods sold on hire Purchase	1,74,000	1.1.2007 to 31.3.2008	By	Hire purchase sales	1,32,000
	To	Loss on repossession of goods (W.N. 5)	1,600		By	Goods sold on hire purchase (1/3 of Rs. 1,74,000)	58,000
31.3.2008	To	Stock reserve	20,000		By	Profit on sale of repossessed goods (W.N. 4)	900
	To	Profit and loss account (Transfer of profit)	43,300	31.3.2008	By	Hire purchase stock (W.N. 3)	60,000
			2,56,900				2,56,900

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

Hire Purchase Trading Account

for the year ended 31st March, 2008

Dr.							Cr.
			Rs.				Rs.
1.1.2007	To	Hire purchase stock	18,000	1.1.2007	By	Stock reserve (1/3 of Rs.	6,000

1.1.2007	To	Hire purchase debtors	10,000			18,000)	
to 31.3.2008	To	Goods sold on hire purchase	1,74,000	1.1.2007 to 31.3.2008	By	Cash (1,21,000 + 2,800)	1,23,800
	To	Cash (Overhauling charges)	500		By	Goods sold on hire purchase	58,000
31.3.2008	To	Stock reserve	20,000			(1/3 of Rs. 1,74,000)	
	To	Profit and loss account (Transfer of profit)	43,300	31.3.2008	By	Hire purchase stock	60,000
					By	Hire purchase debtors	18,000
			2,65,800				2,65,800

Working Notes:

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

Dr. Cr.

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

2. Memorandum shop stock account

Dr. Cr.

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

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

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

4. Goods Repossessed account

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

5.

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

6.

Mr. A in Account Current with Mr. X
(Interest upto 15th March, 2008 @ 10% p.a.)

Dr.											Cr.
Date		Particulars	Amount	Days	Product	Date		Particulars	Amount	Days	Product
2008						2008					
Jan. 01	To	Balance b/d	4,000	75	3,00,000	Jan. 29	By	Purchase account	1,200	46	55,200
Jan. 15	To	Sales account	2,230	60	1,33,800	Feb. 10	By	Cash account	1,000	34	34,000
Mar. 13	To	Red Ink product (Rs. 2,000 $\times$ 29)			58,000	Mar. 13	By	Bills Receivable account	2,000		
Mar. 15	To	Interest account $\left(\frac{\text{Rs.}4{,}02{,}600\times 10\times 1}{100\times 366}\right)$	110			Mar. 15	By	Balance of product			4,02,600
							By	Balance c/d (amount to be paid)	2,140		
			6,340		4,91,800				6,340		4,91,800

7. (a) Computation of liabilities of underwriters (No. of shares):

	A & Co.	B & Co.	C & Co.
Gross liability	12,00,000	12,00,000	12,00,000
Less: Firm underwriting	1,00,000	1,00,000	1,00,000
	11,00,000	11,00,000	11,00,000
Less: Marked applications	7,25,000	8,40,000	13,10,000
	3,75,000	2,60,000	(2,10,000)
Less: Unmarked applications distributed to A & Co. and B & Co. in equal ratio	1,12,500	1,12,500	Nil
	2,62,500	1,47,500	(2,10,000)
Less: Surplus of C & Co. distributed to A & Co. and B & Co. in equal ratio	1,05,000	1,05,000	2,10,000
Net liability (excluding firm underwriting)	1,57,500	42,500	Nil
Add: Firm underwriting	1,00,000	1,00,000	1,00,000
Total liability (No. of shares)	2,57,500	1,42,500	1,00,000

(b) Computation of amounts payable by underwriters:

Liability towards shares to be subscribed @ 12 per share	30,90,000	17,10,000	12,00,000
Less: Commission (5% on 12 lakhs shares @ 10 each)	6,00,000	6,00,000	6,00,000
Net amount to be paid by underwriters	24,90,000	11,10,000	6,00,000

8.

In the Books of A Ltd.

Journal Entries

			Rs.	Rs.
(i)	Share Final Call A/c	Dr.	2,00,000	
	To Share Capital A/c			2,00,000
	(Being the final call of Rs. 2.50 each on 80,000 equity shares made)			
(ii)	Bank A/c	Dr.	2,00,000	
	To Share Final Call A/c			2,00,000
	(Being the amount due on final call received)			
(iii)	General Reserves	Dr.	3,00,000	

	Securities Premium A.c	Dr.	1,00,000	
	To Bonus to Share holders A/c			4,00,000
	(Being the appropriation made as above to facilitate issue of fully paid up bonus shares at the rate of one share for every two shares held)			
(iv)	Bonus to Shareholders A/c	Dr.	4,00,000	
	To Equity Share Capital A/c			4,00,000
	(Being the issuance of 40,000 fully paid up shares of Rs. 10 each by way of bonus)			

Balance Sheet (after bonus issue)

Liabilities	Amount	Assets	Amount
Authorised Share Capital		Bank	2,00,000
1,50,000 equity shares of Rs. 10 each	15,00,000	Sundry Assets	17,00,000
Issued and Subscribed			
1,20,000 Equity Shares of Rs. 10 each fully paid	12,00,000		
Of the above, 40,000 equity shares are allotted as fully paid up by way of bonus shares			
Reserves and Surplus			
Capital Redemption Reserve	1,50,000		
Securities Premium	50,000		
Development Rebate Reserve	2,30,000		
Investment Allowance Reserve	2,50,000		
Plant Revaluation Reserve	20,000		
	19,00,000		19,00,000

9. In the books of Alpha Ltd.

Journal Entries

Date	Particulars		Amount Dr. Rs.	Amount Cr. Rs.
1.5.08	Bank A/c	Dr.	1,50,00,000	
	To Debenture Application A/c			1,50,00,000
	(Application money received on 1,50,000 debentures @ Rs. 100 each)			
1.6.08	Debenture Application A/c	Dr.	1,50,00,000	
	Underwriters A/c	Dr.	50,00,000	

	To 15% Debentures A/c			2,00,00,000
	(Allotment of 1,50,000 debentures to applicants and 50,000 debentures to underwriters)			
	Underwriting Commission	Dr.	4,00,000	
	To Underwriters A/c			4,00,000
	(Commission payable to underwriters @ 2% on Rs. 2,00,00,000)			
	Bank A/c	Dr.	46,00,000	
	To Underwriters A/c			46,00,000
	(Amount received from underwriters in settlement of account)			
30.9.08	Debenture Interest A/c	Dr.	10,00,000	
	To Bank A/c			10,00,000
	(Interest paid on debentures for 4 months @ 15% on Rs. 2,00,00,000)			
30.10.08	15% Debentures A/c	Dr.	1,20,00,000	
	To Equity Share Capital A/c			20,00,000
	To Securities Premium A/c			1,00,00,0000
	(Conversion of 60% of debentures into shares of Rs. 60 each with a face value of Rs. 10)			
31.3.09	Debenture Interest A/c	Dr.	7,50,000	
	To Bank A/c			7,50,000
	(Interest paid on debentures for the half year)			

Working Note :

Calculation of Debenture Interest for the half year ended 31st March, 2009

On Rs. 80,00,000 for 6 months @ 15%	= Rs. 6,00,000
On Rs. 1,20,00,000 for 1 months @ 15%	= Rs. 1,50,000
	Rs. 7,50,000

10. Journal Entries for Buy-back of shares of Gun Shot Ltd.

(i)	Bank A/c	Dr.	3,20,000	
	To Non-trade Investments			3,00,000
	To Profit & Loss A/c			20,000
	(Being the entry for sale of Non-trade Investments)			
(ii)	Shares Buy back A/c (16,000 x Rs. 20)	Dr.	3,20,000	
	To Bank A/c			3,20,000
	(Being purchase of 16,000 shares @ Rs.20 per share)			
(iii)	Equity Share Capital A/c (16,000 x Rs.10)	Dr.	1,60,000	
	Buy-back Premium (16,000 x Rs.10)	Dr.	1,60,000	
	To Shares Buy-back A/c			3,20,000
	(Being cancellation of shares bought back)			
(iv)	Securities Premium A/c	Dr.	1,00,000	
	General Reserve	Dr.	60,000	
	To Buy-back Premium			1,60,000
	(Being adjustment of buy-back premium)			
(v)	General Reserve	Dr.	1,60,000	
	To Capital Redemption Reserve			1,60,000
	(Being the entry for transfer of General Reserve to Capital Redemption Reserve to the extent of face value of equity shares bought back)			

11. In the Books of Vayu Ltd.

Realisation Account

		Rs.			Rs.
To	Sundry Assets (5,80,000 – 10,000)	5,70,000	By	Gratuity Fund	20,000
To	Preference Shareholders		By	Sundry Creditors	80,000
	(Premium on Redemption)	10,000	By	Hari Ltd.	

To	Equity Shareholders (Profit on Realisation)	50,000		(Purchase Consideration)	5,30,000
		6,30,000			6,30,000

Equity Shareholders Account

		Rs.			Rs.
To	Preliminary Expenses	10,000	By	Share Capital	3,00,000
To	Equity Shares of Hari Ltd.	4,20,000	By	General Reserve	80,000
			By	Realisation Account (Profit on Realisation)	50,000
		4,30,000			4,30,000

Preference Shareholders Account

		Rs.			Rs.
To	9% Preference Shares of Hari Ltd.	1,10,000	By	Preference Share Capital	1,00,000
			By	Realisation Account (Premium on Redemption of Preference Shares)	10,000
		1,10,000			1,10,000

Hari Ltd. Account

		Rs.			Rs.
To	Realisation Account	5,30,000	By	9% Preference Shares	1,10,000
			By	Equity Shares	4,20,000
		5,30,000			5,30,000

In the Books of Hari Ltd.
Journal Entries

		Dr. Rs.	Cr. Rs.
Goodwill Account	Dr.	50,000	

Building Account	Dr.	1,50,000	
Machinery Account	Dr.	1,60,000	
Stock Account	Dr.	1,57,500	
Debtors Account	Dr.	1,00,000	
Bank Account	Dr.	20,000	
To Gratuity Fund Account			20,000
To Sundry Creditors Account			80,000
To Provision for Doubtful Debts Account			7,500
To Liquidators of Vayu Ltd. Account			5,30,000
(Being Assets and Liabilities takenover as per agreed valuation).			
Liquidators of Vayu Ltd. A/c	Dr.	5,30,000	
To 9% Preference Share Capital A/c			1,10,000
To Equity Share Capital A/c			4,00,000
To Securities Premium A/c			20,000
(Being Purchase Consideration satisfied as above).			

Balance Sheet of Hari Ltd. (after absorption)
as at 31st March, 2008

Liabilities	Rs.	Assets		Rs.
Share Capital :		Fixed Assets:		
2,100 9% Preference Shares of Rs.100 each	2,10,000	Goodwill		1,00,000
1,40,000 Equity Shares of Rs. 10 each fully paid	14,00,000	Building		4,50,000
		Machinery		6,60,000
(1,100 Preference Shares and 40,000 Equity Shares were issued in consideration other than for cash)		Current Assets:		
		Stock		4,07,500
Reserve and Surplus:		Debtors	3,00,000	
Securities Premium	20,000	Less: Provision for bad debts	7,500	2,92,500
General Reserve	1,00,000	Cash and Bank		70,000
Current Liabilities:		Miscellaneous		
Gratuity Fund	70,000	Expenses to the		

		extent not written off	
Sundry Creditors	2,10,000	Preliminary expenses	30,000
	20,10,000		20,10,000

Working Notes:

Purchase Consideration:	
Goodwill	50,000
Building	1,50,000
Machinery	1,60,000
Stock	1,57,500
Debtors	92,500
Cash at Bank	20,000
	6,30,000
Less: Liabilities	
Gratuity	20,000
Sundry Creditors	80,000
Net Assets	5,30,000
To be satisfied as under:	
10% Preference Shareholders of Vayu Ltd.	1,00,000
Add: 10% Premium	10,000
1,100 9% Preference Shares of Hari Ltd.	1,10,000
Equity Shareholders of Vayu Ltd. to be satisfied by issue of 40,000 Equity Shares of Hari Ltd. at 5% Premium	4,20,000
Total	5,30,000

12. In the Books of Max Ltd.

Particulars		Dr. Amount Rs.	Cr. Amount Rs.
01.04.2008			
Equity share capital A/c	Dr.	15,00,000	
To Equity share capital A/c			15,00,000
(Being sub-division of one share of Rs. 100			

each into 10 shares of Rs. 10 each)			
Equity share capital A/c	Dr.	7,50,000	
To Capital reduction A/c			7,50,000
(Being reduction of capital by 50%)			
Capital reduction A/c	Dr.	13,500	
To Bank A/c			13,500
(Being payment in cash of 10% of arrear of preference dividend)			
Bank A/c	Dr.	78,400	
To Own debentures A/c			76,800
To Capital reduction A/c			1,600
(Being profit on sale of own debentures transferred to capital reduction A/c)			
12% Debentures A/c	Dr.	1,20,000	
To Own debentures A/c			1,15,200
To Capital reduction A/c			4,800
(Being profit on cancellation of own debentures transferred to capital reduction A/c)			
12% Debentures A/c	Dr.	2,80,000	
Capital reduction A/c	Dr.	20,000	
To Machinery A/c			3,00,000
(Being machinery taken up by debentureholders for Rs. 2,80,000)			
Creditors A/c	Dr.	65,000	
Capital reduction A/c	Dr.	29,000	
To Debtors A/c			61,000
To Stock A/c			33,000
(Being assets and liabilities revalued)			
Capital reduction A/c	Dr.	4,33,000	
To Goodwill A/c			20,000
To Discount on debentures A/c			2,000
To Profit and Loss A/c			4,11,000
(Being the balance of capital reduction transferred to capital reserve account)			
Capital reduction A/c	Dr.	15,000	
To Bank A/c			15,000
(Being penalty paid for avoidance of capital			

	commitments)			
	Capital reduction A/c	Dr.	2,45,900	
	To Capital reserve A/c			2,45,900
	(Being penalty paid for avoidance of capital commitments)			
02.04.2008	Business Purchase A/c	Dr.	13,20,000	
	To Liquidators of Mini Ltd.			13,20,000
	(Being the purchase consideration payable to Mini Ltd.)			
	Fixed Assets A/c	Dr.	7,60,000	
	Stock A/c	Dr.	6,80,000	
	Debtors A/c	Dr.	4,40,000	
	Cash at Bank A/c	Dr.	1,30,000	
	To Sundry Creditors A/c			2,25,000
	To 12% Debentures A/c of Mini Ltd.			2,00,000
	To Profit and Loss A/c			15,000
	To General reserve A/c Rs. (1,70,000 + 80,000*)			2,50,000
	To Business purchase A/c			13,20,000
	(Being the take over of all assets and liabilities of Mini Ltd. by Max Ltd.)			
	Liquidators of Mini Ltd. A/c	Dr.	13,20,000	
	To Equity Share Capital			10,00,000
	To 9% Preference share capital			3,20,000
	(Being the purchase consideration discharged)			
	12% Debentures of Mini Ltd. A/c	Dr.	2,00,000	
	To 12% Debentures A/c			2,00,000
	(Being Max Ltd. issued their 12% Debentures in against of every Debentures of Mini Ltd.)			

Balance Sheet of Max Ltd. as at 2.4.2008

Liabilities	Rs.	Assets	Rs.
Share Capital:		Fixed Assets	19,60,000
Equity Share Capital	17,50,000	Stock	10,40,000
9% Preference share capital	8,20,000	Debtors	10,30,000

* Rs. 80,000 is the balancing figure adjusted to general reserve A/c as per AS 14 "Accounting for Amalgamation".

Profit and Loss A/c	15,000	Cash in hand/Bank	2,05,900
General Reserve	4,30,000		
Capital Reserve	2,45,900		
12% Debentures	4,00,000		
Sundry Creditors	5,75,000		
	42,35,900		42,35,900

Working Notes:

1. Purchase Consideration

Equity share capital $10{,}000 \times \frac{50}{5} \times \text{Rs.}10$ = 10,00,000

9% Preference share capital $4{,}000 \times \frac{4}{5} \times \text{Rs.}100$ = 3,20,000

Rs. 13,20,000

2. General Reserve

	Rs.
Share Capital of Mini Ltd. (Equity + Preference)	14,00,000
Less: Share Capital issued by Max Ltd.	13,20,000
General reserve (resulted due to absorption)	80,000
Add: General reserve of Mini Ltd.	1,70,000
General reserve of Max Ltd.	1,80,000
	4,30,000

13. Liquidators' Final Statement of Account

Receipts	Rs.	Payments	Rs.
Cash	4,13,000	Return to contributors:	
Realisation from:		Preference dividend	33,000
Calls in arrears	10,000	Preference shareholders	3,00,000
Final call of Rs. 5 per		Calls in advance	5,000
equity share of Rs. 50 each (Rs. 5 × 1,000)	5,000	Equity shareholders of Rs. 100 each (3,000 × Rs. 30)	90,000
	4,28,000		4,28,000

Working Note:

	Rs.
Cash account balance	4,13,000

Less:	Payment for dividend	33,000	
	Preference shareholders	3,00,000	
	Calls in advance	5,000	3,38,000
			75,000
Add: Calls in arrears			10,000
			85,000
Add: Amount to be received from equity shareholders of Rs. 50 each (1,000 × 20)			20,000
Amount disposable			1,05,000

Number of equivalent equity shares:

3,000 shares of Rs. 100 each = 6,000 shares of Rs. 50 each

1,000 shares of Rs. 50 each = 1,000 shares of Rs. 50 each

= 7,000 shares of Rs. 50 each

Final payment to equity shareholders = $\frac{\text{Amount left for distribution}}{\text{Total number of equivalent equity shares}}$

= Rs. 1,05,000 / 7,000 shares = Rs. 15 per share to equity shareholders of Rs. 50 each.

Therefore for equity shareholders of Rs. 100 each $\left(\text{Rs.}15 \times \frac{100}{50}\right)$

= Rs. 30 per share to equity shareholders of Rs. 100 each.

Calls in advance must be paid first, so as to pay the shareholders on prorata basis. Equity shareholders of Rs. 50 each have to pay Rs. 20 and receive Rs. 15 each. As a result, they are required to pay net Rs. 5 per share.

14. (a) Computation of Capital Base

	Rs.	Rs.
Fixed Assets	4,00,00,000	
Less:Customers' Contribution	4,00,000	3,96,00,000
Add: Cost of Intangible Assets		
(Preliminary Expenses)		10,00,000
Investments against Contingencies Reserve		40,00,000
Monthly average of Current Assets		40,00,000
	(A)	4,86,00,000

Less:		
Amount written off on account of Depreciation		1,60,00,000
Loans advanced by Electricity Board		60,00,000
10% Debentures		16,00,000
Security Deposits by Customers		1,50,00,000
Balance of Tariffs and Dividend Control Reserve		12,00,000
Balance of Development Reserve		20,00,000
	(B)	4,18,00,000
Capital Base (A) – (B)		68,00,000

(b) Computation of Reasonable Return

Yield 10% (i.e. 8% + 2%) on Capital Base		6,80,000
Income from Reserve Fund Investments – 6% on	Rs. 1,20,00,000	7,20,000
(Investments other than of Contingencies reserve)		
1/2% of Loans from Electricity Board		30,000
1/2% of Development Reserve		10,000
1/2% of Debentures		8,000
Reasonable Return		14,48,000

(c) Computation of Surplus

Post tax Profit	20,40,000
Less: Reasonable Return	14,48,000
Surplus	5,92,000

(d) Disposal of Surplus

20% of Reasonable return = Rs. 14,48,000 × 20/100 = 2,89,600

(1) Excess of 20% of Reasonable Return to be Credited to Customers Benefit Account:
Rs.5,92,000 – Rs. 2,89,600 (Amount refundable to consumers) 3,02,400

(2) Balance of Rs. 2,89,600 has to be disposed of as follows:

(a) 1/3 of the surplus not exceeding 5% of Reasonable Return at the disposal of the company – 5% of 14,48,000

	or 1/3 of 2,89,600, whichever is less	72,400
(b)	1/2 of the balance to be credited to Tariff and Dividend Control Reserve	1,08,600
(c)	The balance to be credited to Customers Rebate Account (in addition to Rs. 3,02,400 shown above)	1,08,600
	Total Surplus	5,92,000
Amount to be refunded to customers (Rs. 3,02,400 + Rs. 1,08,600)		4,11,000
Amount to be transferred to Tariff and Dividend Control Reserve		1,08,600
Amount at disposal of the company (Rs. 14,48,000 + Rs. 72,400)		15,20,400
Net Profit		20,40,000

15. (a) Journal of Indian Insurance Co. Ltd.

(Rupees in crores)

2007			Dr. Rs	Cr. Rs.
Dec. 31	Marine Revenue A/c	Dr.	3.30	
	To Unexpired Risks Reserve A/c			3.30
	(Being the difference between closing provision of Rs. 18.30 crores (18 + 7 – 6.7) and opening provision of Rs. 15 crores charged to marine revenue account)			
	Fire Revenue A/c	Dr.	1.85	
	To Unexpired Risks Reserve A/c			1.85
	(Being the difference between closing provision of Rs. 21.85 crores [(43 + 5 – 4.3)/2] and opening provision of Rs. 20 crores charged to fire revenue account)			
	Unexpired Risks Reserve A/c	Dr.	0.50	
	To Miscellaneous Revenue A/c			0.50
	(Being the excess of opening balance of Rs. 5 crores over the required closing balance of Rs. 4.5 crores [(12 + 4 – 7)/2] credited to miscellaneous revenue account).			

(b) Unexpired Risks Reserve A/c

(Rs in crores)

2007		Marine Rs.	Fire Rs.	Miscel-laneous Rs.	2007		Marine Rs.	Fire Rs.	Miscel-laneous Rs.
Dec. 31	To Revenue A/c	–	–	0.50	Jan 1	By Balance b/d	15.00	20.00	5.00
	To Balance c/d	18.30	21.85	4.50	Dec.31	By Revenue A/c	3.30	1.85	–
		18.30	21.85	5.00			18.30	21.85	5.00

Note : Alternatively, the opening balances of unexpired risk reserves may be reversed in the beginning of year by transfer to Revenue account and fresh reserve of full required amount may be created at the end of the year which will be carried forward as closing balances.

16. Calculation of amount of provision to be made in the Profit and Loss Account

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

17. Smith Library Society

Income and Expenditure Account

for the year ended 31st March, 2008

Dr. Expenditure	Rs.	Rs.	Income	Cr. Rs.
To Electric charges		7,200	By Entrance fees (25% of Rs. 30,000)	7,500
To Postage and stationary		5,000		

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

	Rs.	Rs.		Rs.	Rs.
To Telephone charges		5,000	By Membership subscription	2,00,000	
To Rent	88,000		Less: Received in advance	10,000	1,90,000
Add: Outstanding	4,000	92,000	By Sale proceeds of old papers		1,500
To Salaries	66,000		By Hire of lecture hall		20,000
Add: Outstanding	3,000	69,000	By Interest on securities (W.N.2)	8,000	
To Depreciation (W.N.1)			Add: Receivable	500	8,500
Electrical fittings	15,000		By Deficit- excess of expenditure over income		16,700
Furniture	5,000				
Books	46,000	66,000			
		2,44,200			2,44,200

Balance Sheet of Smith Library Society
as on 31st March, 2008

Liabilities	Rs.	Rs.	Asset	Rs.	Rs.
Capital fund	7,93,000		Electrical fittings	1,50,000	
Add: Entrance fees	22,500		Less: Depreciation	15,000	1,35,000
	8,15,500		Furniture	50,000	
Less: Excess of expenditure over income	16,700	7,98,800	Less:Depreciation	5,000	45,000
			Books	4,60,000	
Outstanding expenses:			Less Depreciation	46,000	4,14,000
Rent	4,000		Investment:		
Salaries	3,000	7,000	Securities	1,90,000	
Membership subscription in advance		10,000	Accrued interest	500	1,90,500
			Cash at bank		20,000
			Cash in hand		11,300
		8,15,800			8,15,800

Working Notes:

1. Depreciation

	Rs.
Electrical fittings 10% of Rs. 1,50,000	15,000
Furniture 10% of Rs. 50,000	5,000
Books 10% of Rs. 4,60,000	46,000

2. Interest on Securities

Interest @ 5% p.a. on Rs. 1,50,000 for full year	7,500	
Interest @ 5% p.a. on Rs. 40,000 for half year	1,000	8,500
Less: Received		8,000
Receivable		500

18. Computation of claim for loss of stock:

	Rs.
Stock on the date of fire i.e. 31.12.2008 (Refer working note)	30,500
Less: Salvaged stock	3,000
Loss of stock	27,500

Amount of claim

$$\frac{\text{Insured value}}{\text{Total cost of stock on the date of fire}} \times \text{loss of stock}$$

$$\frac{\text{Rs.}25{,}000}{\text{Rs.}30{,}500} \times \text{Rs.}27{,}500 = 22{,}541$$

Working Note:

Memorandum trading account can be prepared for the period from 1.10.2008 to 31.12.2008 to compute the value of stock on 31.12.2008.

Memorandum Trading Account
for period from 1.10.2008 to 31.12.2008

	Rs.	Rs.		Rs.
To Opening stock		33,000	By Sales	1,40,000
(Rs. 29,700x100/90)			By Closing stock	30,500
To Purchases	75,000		(balancing figure)	
Less: Cost of plant	5,000	70,000		
To Wages	33,000			
Less: Wages paid for plant	500	32,500		
To Gross profit		35,000		
(33.33% on cost or 25% on sales)				
		1,70,500		1,70,500

19. (i) True- The economic life of an enterprise is artificially split into periodic intervals in accordance with the accounting period assumption or the periodicity concept. The going concern assumption assumes that an enterprise will continue in operation for indefinite period of time.

(ii) False- Average due date is 'no loss no gain' date to either party. i.e. neither the debtor nor the creditor stands to lose or gain anything by way of interest.

(iii) Although the case under consideration does not relate to extraordinary item, but the nature and amount of such item may be relevant to users of financial statements in understanding the financial position and performance of an enterprise and in making projections about financial position and performance. Para 12 of AS 5 (Revised in 1997) on Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies states that :

"When items of income and expense within profit or loss from ordinary activities are of such size, nature or incidence that their disclosure is relevant to explain the performance of the enterprise for the period, the nature and amount of such items should be disclosed separately."

Circumstances which may give to separate disclosure of items of income and expense in accordance with para 12 of AS 5 include the write-down of inventories to net realisable value as well as the reversal of such write-downs.

(iv) B : 2/3 less 3/10 = 11/30

C: 1/3 less 2/10 = 4/30

Gaining ratio = B : C

11 : 4

(v) False- If there exists a specific sports fund, the expenditure incurred in carrying out the purpose of the fund i.e. incurred on sports activities will be deducted from that fund only.

(vi) True – Disclosure of significant accounting policies must form part of the financial statements and these policies must be disclosed separately, at one place in annual report e.g., policies relating to valuation of inventory, depreciation accounting, etc.

(vii) Calculation of new profit sharing ratio

D is to get 1/8th share in profit

The remaining profit of the firm = 1 – 1/8 = 7/8

Remaining profit will be shared by A, B and C in their old profit sharing ratio. Thus, the new profit sharing ratio of A, B and C will be calculated as follows:

A	7/8	×	6/14	=	3/8
B	7/8	×	5/14	=	5/16
C	7/8	×	3/14	=	3/16

Therefore, the new profit sharing ratio is 3/8 : 5/16 : 3/16 : 1/8 or 6: 5: 3: 2

(viii) False: According to the rule of Garner vs. Murray, the loss on account of insolvency of a partner should be borne by the solvent partners in the ratio of their capitals standing in the balance sheet, just before the dissolution of the partnership firm.

(ix)

Particulars	Rs.	Rs.
Equity Shares (42,000 x 10)		4,20,000
Preference Share Capital	1,70,000	
Add: Premium on Redemption	17,000	1,87,000
Purchase Consideration		6,07,000

20. (i) Partners capital accounts can be maintained either on 'fixed capital system' or on 'fluctuating capital system'. In case of fixed capital system, two accounts for each partner i.e. partner's capital account and partner's current account are maintained. The partner's capital account is credited with the original amount of capital introduced by the partners into business. It is to be credited subsequently with extra capital introduced by the partners or debited with the amount of capital permanently withdrawn by the partners. No other adjustments are made in this account. The partner's current account is maintained for making all entries relating to interest, share of profit, drawings, etc. The balance in this account will go on fluctuating but the balance of the capital account will remain fixed. That is why the system is termed as 'fixed capital system'.

In case of fluctuating capital system, only one account is maintained for each partner. This account is termed as his 'capital account'. All entries relating to introduction of fresh capital, drawings, interest, profit etc. are made in this account. The balance in this capital account, therefore, goes on fluctuating. The system is, therefore, called as 'fluctuating capital system'.

(ii) The Companies (Amendment) Act, 1999 introduced through section 79A a new type of equity shares called 'Sweat Equity Shares. The expression 'sweat equity shares' means equity shares issued by a company to its employees or directors at a discount or for consideration other than cash for providing know-how or making available rights in the nature of intellectual property rights or value additions by whatever name called.

Notwithstanding anything contained in section 79, which deals with the power of a company to issue shares at a discount, a company may issue sweat equity shares of a class of shares already issued, if the following conditions are fulfilled, namely:-

(i) the issue of sweat equity shares is authorised by a special resolution passed by the company in the general meeting.

(ii) the resolution specifies the number of shares, current market price, the consideration if any, and the class or classes of directors or employees to whom such equity shares are to be issued.

(iii) not less than one year has, at the time of the issue, elapsed since the date on which the company was entitled to commence business.

(iv) the sweat equity shares of company, whose equity shares are listed on a recognised stock exchange, are issued in accordance with the regulations made by the Securities and Exchange Board of India in this behalf. But in the case of company whose equity shares are not listed on any recognised stock exchange, the sweat equity shares are issued in accordance with the guidelines as may be prescribed.

All the limitations, restrictions and provisions relating to equity shares are applicable to sweat equity shares also.

(iii) The statement prepared by the liquidator showing receipts and payments of cash in case of voluntary winding up is called "Liquidators' statement of account" (Form No. 156 Rule 329 of the Companies Act, 1956). There is no double entry involved in the preparation of liquidator's statement of account. It is only a statement though presented in the form of an account.

While preparing the liquidator's statement of account, receipts are shown in the following order :

(a) Amount realised from assets are included in the prescribed order.

(b) In case of assets specifically pledged in favour of creditors, only the surplus from it, if any, is entered as 'surplus from securities'.

(c) In case of partly paid up shares, the equity shareholders should be called up to pay necessary amount (not exceeding the amount of uncalled capital) if creditors' claims/claims of preference shareholders can't be satisfied with the available amount. Preference shareholders would be called upon to contribute (not exceeding the amount as yet uncalled on the shares) for paying of creditors.

(d) Amounts received from calls to contributories made at the time of winding up are shown on the Receipts side.

(e) Receipts per Trading Account are also included on the Receipts side.

Payments made to redeem securities and cost of execution and payments per Trading Account are deducted from total receipts.

Payments are made and shown in the following order :

(a) Legal charges;

(b) Liquidator's expenses;

(d) Debentureholders (including interest up to the date of winding up if the company is insolvent and to the date of payment if it is solvent);

(f) Creditors :

(i) Preferential (in actual practice, preferential creditors are paid before debenture holders having a floating charge);

(ii) Unsecured creditors;

(g) Preferential shareholders (Arrears of dividends on cumulative preference shares should be paid up to the date of commencement of winding up); and

(h) Equity shareholders.

Liquidator's statement of account of the winding up is prepared for the period starting from the commencement of winding up to the close of winding up. If winding up of company is not concluded within one year after its commencement, Liquidator's statement of account pursuant to section 551 of the Companies Act, 1956 (Form No. 153) is to be filed by a Liquidator within a period of two months of the conclusion of one year and thereafter until the winding up is concluded at intervals of not more than one year or at such shorter intervals, if any, as may be prescribed.

(iv) Banks have to classify their advances into four broad groups:

(i) Standard Assets—Standard assets is one which does not disclose any problems and which does not carry more than normal risk attached to the business. Such an asset is not a NPA as discussed earlier.

(ii) Sub-standard Assets—Sub-standard asset is one which has been classified as NPA for a period not exceeding 18 months. In the case of term loans, those where instalments of principal are overdue for period exceeding one year should be treated as sub-standard. In other words, such an asset will have well-defined credit weaknesses that jeopardise the liquidation of the debt and are characterised by the distinct possibility that the bank will sustain some loss, if deficiencies are not corrected.

(iii) Doubtful Assets—A doubtful asset is one which has remained NPA for a period exceeding 18 months. In the case of term loans, those where instalments of principal have remained overdue for a period exceeding 18 months should be treated as doubtful. A loan classified as doubtful has all the weaknessses inherent in that classified as sub-standard with added characteristic that the weaknesses make collection or liquidation in full, on the basis of currently known facts, conditions and values, highly questionable and improbable.

(iv) Loss Assets—A loss asset is one where loss has been identified by the bank or internal or external auditors or the RBI inspectors but the amount has not been written off, wholly or partly.

The classification of advances should be done taking into account (i) Degree of well defined credit worthiness and (ii) Extent of dependence on collateral security.

The above classification is meant for the purpose of computing the amount of provision to be made in respect of advances and not for the purpose of presentation of advances in the balance sheet.

(v) Premium income : The payment made by the insured as consideration for the grant of insurance is known as premium. The amount of premium income to be credited to revenue account for a year may be computed as :

	Rs.
Premium received on risks undertaken during the year	
(direct & re-insurance accepted)	–
Add : Receivable at the end of year (direct & re-insurance accepted)	–
Less : Receivable at the beginning of year (direct & re-insurance accepted)	–
Less : Premium on re-insurance ceded:	–
Paid during the year	–
Add : Payable at the end of year	–
Less : Payable at the beginning of year	–
Premium income	–

Claims expenses : A claim occurs when a policy falls due for payment. In the case of a life insurance business, it will arise either on death or maturity of policy that is, on the expiry of the specified term of years. In the case of general insurance business, a claim arises only when the loss occurs or the liability arises.

The amount of claim to be charged to revenue account may be worked out as under:

	Rs.
Claims settled during the year—direct & re-insurance accepted	–
(including legal fees, survey charges etc.)	
Add : Payments to co-insurers	–
Less :Received from co-insurers and re-insurers	–
Net payment	–
Add : Estimated liability at the end of the year	–
(After deducting recoverable from co-insurers and re-insurers)	
Less : Estimated liability at the beginning of the year	–
(after deducting recoverable from co-insurers and re-insurers)	
Claims expense	–

Commission expenses : Insurance Regulatory and Development Authority Act, 1999 regulates the commission payable on policies to agents. Commission expense to be charged to revenue account is computed as follows :

	Rs.
Commission paid (direct & re-insurance accepted)	–
Add : Commission payable at the end of the year (direct & re-insurance accepted)	–
Less : Commission payable at the beginning of the year (direct & re-insurance accepted)	–
Commission expense	–

(vi) Double accounts system is the name given to the system of preparing the final accounts of certain statutory companies formed by special Acts of parliament, usually public utility undertakings (for example Electricity Companies). The double accounts system is not a special method of keeping accounts, rather a special method of presenting accounts which are kept under the normal double entry system. Under this system, separate accounts in respect of capital and revenue are prepared in order to show clearly the capital receipts and the manner in which the amounts thereof have been invested. The final accounts prepared under the double accounts system normally consist of :

(i) Revenue Account

(ii) Net Revenue Account

(iii) Capital Account (Receipts and Expenditure on capital account)

(iv) General Balance Sheet.

The Revenue account is analogous to the Profit & Loss Account of a company with some exceptions. The Net Revenue Account resembles with appropriation portion of the Profit & Loss Account of a company. The Balance Sheet is presented in two parts namely Capital Account and General Balance Sheet. The Capital Account shows the total amount of capital raised and its sources and also the manner and extent to which this capital has been applied in the acquisition of fixed assets for the purpose of carrying on the business. The General balance sheet includes the other items.

The Double accounts system in its pure form does no longer exist but the statements submitted to State Governments by electricity companies generally follow the principle of double accounts system. It may be noted that for presenting accounts to the shareholders, electricity companies normally follow Schedule VI of the Companies Act, 1956.

(vii) Consideration for selection of pre-packaged accounting software:

There are many accounting softwares available in the market. To choose the accounting software appropriate to the need of the organisation is a difficult task. Some of the criteria for selection could be the following:

1. Fulfilment of business requirements: Some packages have few functionalities more than the others. The purchaser may try to match his requirement with the available solutions.
2. Completeness of reports: Some packages might provide extra reports or the reports matches the requirement more than the others.
3. Ease of use: Some packages could be very detailed and cumbersome compare to the others.
4. Cost : The budgetary constrainsts could be an important deciding factor. A package having more features cannot be opted because of the prohibitive costs.
5. Reputation of the vendor: Vendor support is essential for any software. A stable vendor with reputation and good track records will always be preferred.
6. Regular updates: Law is changing frequently. A vendor who is prepared to give updates will be preferred to a vendor unwilling to give updates.

(viii) On disposal of an investment, the difference between the carrying amount and the disposal proceeds, net of expenses is recognised in the profit and loss statement. When a part of the holding of an individual investment is disposed, the carrying amount is required to be allocated to that part on the basis of the average carrying amount of the total holding of the investment.

(ix) Purpose of the Conceptual Framework:

The framework sets out the concepts underlying the preparation and presentation of general-purpose financial statements prepared by enterprises for external users. The main purpose of the framework is:

(a) To assist enterprises in preparation of their financial statements in compliance with the accounting standards and in dealing with the topics not yet covered by any accounting standard.

(b) To assist ASB in its task of development and review of accounting standards.

(c) To assist ASB in promoting harmonisation of regulations, accounting standards and procedures relating to the preparation and presentation of financial statements by providing a basis for reducing the number of alternative accounting treatments permitted by accounting standards.

(d) To assist auditors in forming an opinion as to whether financial statements conform to the accounting standards.

(e) To assist the users in interpretation of financial statements.

Status of the Conceptual Framework:

The framework applies to general-purpose financial statements usually prepared annually for external users, by all commercial, industrial and business enterprises, whether in public or private sector. The special purpose financial reports, for example prospectuses and computations prepared for tax purposes are outside the scope of the framework. Nevertheless, the framework may be applied in preparation of such reports, to the extent not inconsistent with their requirements.

Nothing in the framework overrides any specific Accounting Standard. In case of conflict between an accounting standard and the framework, the requirements of the Accounting Standard will prevail over those of the framework.

(x) In an Account Current, interest is calculated on the amount of a bill from the date of transaction to the closing date of the period concerned. In case the due date of the bill falls after the closing date of the account, then no interest is allowed for that period. However, it is customarily followed that interest from the date of closing to the due date is written in Red-Ink in the appropriate side of the Account Current. This interest is called Red-Ink Interest. This Red-Ink interest is treated as negative interest. In actual practice, however, the product of such bill [value of the bill x (due date – closing date)], is written in ordinary ink on the opposite side of the account on which the bill is entered.

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

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

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

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

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

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

(b) the amount of advances received; and

(c) the amount of retentions.

An enterprise should present:

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

(a) The nature of the event;

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

Purpose	Nature	Interest to be charged to profit and loss account Rs. in lakhs	Interest to be charged to profit and loss account Rs. in lakhs
Modernisation and renovation of plant and machinery	Qualifying asset	$**52.20 \times \frac{406}{580} = 36.54$	$52.20 \times \frac{116}{580} = 10.44$
Advance to supplies for additional assets	Qualifying asset	$**52.20 \times \frac{58}{580} = 5.22$	
Working Capital	Not a qualifying asset		
		41.76	10.44

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

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

(ii) Computation of Basic Earnings Per Share

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

	Year 2007 Rs.	Year 2008 Rs.
EPS for the year 2007 as originally reported		
$= \dfrac{\text{Net profit of the year attributable to equity shareholders}}{\text{Weighted average number of equity shares outstanding during the year}}$		
= (Rs. 20,00,000 / 10,00,000 shares)	2.00	
EPS for the year 2007 restated for rights issue		
= [Rs. 20,00,000 / (10,00,000 shares × 1.04*)]	1.92 (approx.)	
EPS for the year 2008 including effects of rights issue		
$\dfrac{\text{Rs. } 30{,}00{,}000}{(10{,}00{,}000 \text{ shares} \times 1.04 \times 3/12) + (12{,}50{,}000 \text{ shares} \times 9/12)}$		
$\dfrac{\text{Rs. } 30{,}00{,}000}{11{,}97{,}500 \text{ shares}}$		2.51 (approx.)

Working Notes:

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

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

* Refer working note 2.

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

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

2. Computation of adjustment factor

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

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

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

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

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

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

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

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

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

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

= Rs. 56,000

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

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

= Rs. 72,000

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

(iv) (i) Present value of residual value = Rs. 40,000 × 0.7513 = Rs. 30,052

Present value of lease payments = Rs. 3,00,000 – Rs. 30,052 = Rs. 2,69,948.

The present value of lease payments being 89.98% $\left(\frac{2,69,948}{3,00,000} \times 100\right)$ of the fair value, i.e. being a substantial portion thereof, the lease constitutes a finance lease.

(ii) Calculation of unearned finance income

	Rs.
Gross investment in the lease [(Rs.1,08,552* × 3) + Rs. 40,000]	3,65,656
Less: Cost of the equipment	3,00,000
Unearned finance income	65,656

Note: - In the above solution, annual lease payment has been determined on the basis that the present value of lease payments plus residual value is equal to the fair value (cost) of the asset.

23. (i) (a) Amount of foreseeable loss

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

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

(b)

	(Rs in lakhs)
Contract work-in-progress i.e. cost incurred to date are Rs. 605 lakhs	
Work certified	500
Work not certified	105
	605

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

* Annual lease payments = $\frac{\text{Rs. }2,69,948}{2.4868} = \text{Rs. }1,08,552$ (approx.)

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

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

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

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

= [605 – 100 – 540] Rs. in lakhs

Amount due to customers = Rs. 35 lakhs

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

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

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

(ii) Price revision was effected during the current accounting period 2007-2008. As a result, the company stands to receive Rs. 15 lakhs from its customers in respect of sales made from 1st January, 2008 to 31st March, 2008. If the company is able to assess the ultimate collection with reasonable certainty, then additional revenue arising out of the said price revision may be recognised in 2007- 2008 vide Para 10 of AS 9.

(iii) Calculation of the cost of construction of Assets

Particulars	Rs.
Direct Materials	1,000,000
Direct Labour	50,000
Direct Expenses	250,000
Office & Administrative Expenses	40,000
Depreciation	10,000
Cost of the Asset	1,350,000

(iv) As per para 10 of AS 12 'Accounting for Government Grants', where the government grants are of the nature of promoters' contribution, i.e. they are given with reference to the total investment in an undertaking or by way of contribution towards its total capital outlay (for example, central investment subsidy scheme) and no repayment is ordinarily expected in respect thereof, the grants are treated as capital reserve which can be neither distributed as dividend nor considered as deferred income.

In the given case, the subsidy received is neither in relation to specific fixed asset nor in relation to revenue.Thus it is inappropriate to recognise government grants in the profit and loss statement, since they are not earned but represent an incentive provided by government without related costs. The correct treatment is to credit the subsidy to capital reserve. Therefore, the accounting treatment followed by the company is not proper.

24. (i) As per Para 5 of AS 2 "Valuation of Inventories", the inventories are to be valued at lower of cost and net realizable value.

In this case, the cost of inventory is Rs.10 lakhs. The net realizable value is 11,00,000 × 90% = Rs.9,90,000. So, the stock should be valued at Rs.9,90,000.

(ii) As per AS 9 "Revenue Recognition", where the ability to assess the ultimate collection with reasonable certainty is lacking at the time of raising any claim, the revenue recognition is postponed to the extent of uncertainty inverted. In such cases, the revenue is recognized only when it is reasonably certain that the ultimate collection will be made.

In this case, the company never realized interest for the delayed payments make by the dealers. Hence, it has to recognize the interest only if the ultimate collection is certain. The interest income hence is not to be recognized.

(iii) As per Para 41 of AS 26 "Intangible Assets", expenditure on research should be recognized as an expense when it is incurred. An intangible asset arising from development (or from the development phase of an internal project) should be recognized if, and only if, an enterprise can demonstrate all of the conditions specified in para 44 of the standard. An intangible asset (arising from development) should be derecognised when no future economic benefits are expected from its use according to para 87 of the standard. Therefore, the manager cannot defer the expenditure write off to future years.

Hence, the expenses amounting Rs. 20 lakhs incurred on the research and development project has to be written off in the current year ending 31st March, 2008.

(iv)

	Rs. In Lakhs	Rs. in lakhs
Quoted price (refer to working note)	350.00	
Less: 2% Trade Discount	7.00	
	343.00	
Add: 8% Sales tax (8% × Rs. 343 lakhs)	27.44	370.44

Transport charges (0.25% × Rs. 350 lakhs)		0.88	(approx.)
Installation charges (1% × Rs. 350 lakhs)		3.50	
Financing cost (15% on Rs.300 Lakhs) for the period 30.9.2007 to 1.12.2007		7.50	
Trial Run Expenses			
Material	0.35		
Wages	0.25		
Overheads	0.15	0.75	
Total cost		383.07	

Interest on loan for the period 1.12.2007 to 1.05.2008 is Rs. 300 lakhs $\times\frac{15}{100}\times\frac{5}{12}$

= Rs.18.75 lakhs

This expenditure may be charged to Profit and Loss Account or deferred for amortization between say three to five years. Assumed that no other expenses are incurred on the machine during this period.

Working Note:

Let the quoted price 'X'

Less: Trade Discount 0.02X.

Actual Price = 0.98X.

Sale Tax @8% = 1.08 × 0.98X

$$\text{or X} = \frac{\text{Rs. 370.44 lakhs}}{1.08 \times 0.98} = \text{Rs. 350 lakhs}$$

25. (i) As per AS 4 'Contingencies and Events occurring after the Balance Sheet Date', adjustments to assets and liabilities are required for events occurring after the balance sheet date that provide additional information materially affecting the determination of the amounts relating to conditions existing at the Balance Sheet date.

In the given case, bankruptcy of the debtor in April, 2008 and consequent non-recovery of debt is an event occurring after the balance sheet date which materially affects the determination of profits for the year ended 31.3.2008. Therefore, the company should be advised to provide for the entire amount of Rs. 10 lakhs according to para 8 of AS 4.

(ii) It is given that revision of wages took place in June, 2008 with retrospective effect from 1.4.2004. The arrear wages payable for the period from 1.4.2004 to 30.6.2008 cannot be taken as an error or omission in the preparation of financial statements and hence this expenditure cannot be taken as a prior period item.

Additional wages liability of Rs. 87 lakhs (from 1.4.2004 to 30.6.2008) should be included in current year's wages.

It may be mentioned that additional wages is an expense arising from the ordinary activities of the company. Although abnormal in amount, such an expense does not qualify as an extraordinary item. However, as per Para 12 of AS 5 (Revised),' Net Profit or loss for the Period, Prior Period Items and Changes in the Accounting Policies', when items of income and expense within profit or loss from ordinary activities are of such size, nature or incidence that their disclosure is relevant to explain the performance of the enterprise for the period, the nature and amount of such items should be disclosed separately.

However, wages payable for the current year (from 1.4.2008 to 30.6.2008) amounting Rs. 7 lakhs is not a prior period item, hence need not be disclosed separately. This may be shown as current year wages.

(iii) When a change in the method of depreciation is made, depreciation should be calculated in accordance with the new method from the date of the asset coming into use. The deficiency or surplus arising from retrospective recomputation should be adjusted in the accounts in the year in which the method of depreciation is changed. The deficiency should be charged to profit and loss account. Similarly, any surplus should be credited in the statement of profit and loss. Such change is a change in the accounting policy, and its effect should be quantified and disclosed.

In the given case, the deficiency of Rs. 500 lakhs would be charged to the profit and loss account of 31.3.2008. In the notes to account, the fact of change in method of depreciation should be elaborated along with the effect of Rs. 500 lakhs. The current depreciation charge of 200 lakhs determined in accordance with the written down value method should be debited to the profit and loss account.

Note: Accounting Standards 1, 2, 3, 4, 5, 6, 7, 9, 10, 11, 12, 13, 14, 16, 19, 20, 26, 29 applicable for June, 2009 Examination

APPENDIX

Announcement

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

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

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

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

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

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

Provisions

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

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

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

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

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

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

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

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