PAPER – 1 : ADVANCED ACCOUNTING

Question No. 1 is compulsory.

*Answer any **five** questions from the remaining **six** questions.*

Working notes should form part of the answer.

Wherever necessary, suitable assumptions may be made by the candidate.

Question 1

(a) NDA Corporation is engaged in research on a new process design for its product. It had incurred an expenditure of `a 530 lakhs on research upto 31st March, 09.

The development of the process began on 1st April, 09 and Development phase expenditure was ` 360 lakhs upto 31st March, 10 which meets assets recognition criteria.

From 1st April, 10, the company will implement the new process design which will result in after tax saving of ` 80 lakhs per annum for the next five years.

The cost of capital of company is 10%.

Explain:

(1) Accounting treatment for research expenses.

(2) The cost of internally generated intangible asset as per AS 26.

(3) The amount of amortization of the assets. (The present value of annuity factor of ` 1 for 5 years @ 10% = 3.7908)

(b) As on 31st March 2009, Strong Bank Ltd. has a balance of ` 27 crores in "rebate on bills discounted" account. The bank provides you the following further information:

(1) During the financial year ending 31st March 2010, Strong Bank Ltd. discounted bills of exchange of ` 4,000 crores charging interest @ 15% p.a. and the average period of discount being 146 days.

(2) Bills of exchange of ` 600 crores were due for realization from the acceptors/customers after 31st March 2010, the average period outstanding after 31st March 2010, being 73 days.

You are required to pass necessary journal entries in the books of Strong Bank Ltd. for the above transactions.

(c) On 20th October, 2009, the godown and business premises of Aman Ltd. were affected by fire. From the salvaged accounting records, the following information is available.

	`
Stock of goods @ 10% lower than cost as on 31st March,09	*2,16,000*
Purchases less returns (1.4.09 to 20.10.09)	*2,80,000*
Sales less returns (1.4.09 to 20.10.09)	*6,20,000*

Additional information:

(1) Sales upto 20th October, 09 includes ` 80,000 for which goods had not been dispatched.

(2) Purchases upto 20th October, 09 did not include ` 40,000 for which purchase invoices had not been received from suppliers, though goods have been received in Godown.

(3) Past records show the gross profit rate of 25%.

(4) The value of goods salvaged from fire ` 31,000.

(5) Aman Ltd. has insured their stock for ` 1,00,000.

Compute the amount of claim to be lodged to the insurance company.

(d) On 25th September, 2009, Planet Advertising Limited obtained advertisement rights for World Cup Hockey Tournament to be held in Nov./Dec., 2009 for ` 520 lakhs.

They furnish the following information:

(1) The company obtained the advertisements for 70% of available time for ` 700 lakhs by 30th September, 09.

(2) For the balance time they got bookings in October, 09 for ` 240 lakhs.

(3) All the advertisers paid the full amount at the time of booking the advertisements.

(4) 40% of the advertisements appeared before the public in Nov. 09 and balance 60% appeared in the month of December, 09.

You are required to calculate the amount of profit/loss to be recognized for the month November and December, 2009 as per Accounting Standard-9. (4 ´ 5 = 20 Marks)

Answer

(a) (i) Research Expenditure - According to para 41 of AS 26 'Intangible Assets', the expenditure on research of new process design for its product ` 530 lakhs should be charged to Profit and Loss Account in the year in which it is incurred. It is presumed that the entire expenditure is incurred in the financial year 2008-09. Hence, it should be written off as an expense in that year itself.

(ii) Cost of internally generated intangible asset - The question states that the development phase expenditure amounting ` 360 lakhs incurred upto 31st March, 2010 meets asset recognition criteria. As per AS 26 for measurement of such internally generated intangible asset, fair value can be estimated by discounting estimated future net cash flows.

Savings (after tax) from implementation of new design for next 5 years	80 lakhs p.a.
Company's cost of capital	10 %

Annuity factor @ 10% for 5 years	3.7908
Present value of net cash flows (` 80 lakhs x 3.7908)	303.26 lakhs

The cost of an internally generated intangible asset would be lower of cost value ` 360 lakhs or present value of future net cash flows `303.26 lakhs.

Hence, cost of an internally generated intangible asset will be ` 303.26 lakhs.

The difference of ` 56.74 lakhs (i.e. ` 360 lakhs – ` 303.26 lakhs) will be amortized by the enterprise for the financial year 2009-10.

(iii) Amortisation - The company can amortise ` 303.26 lakhs over a period of five years by charging ` 60.65 lakhs per annum from the financial year 2010-11 onwards.

(b) In the books of Strong Bank Ltd.

Journal Entries

Particulars		*Debit (`)*	*Credit (`)*
Rebate on bills discounted A/c	Dr.	27	
To Discount on bills A/c			27
(Being the transfer of opening balance in 'Rebate on bills discounted A/c' to 'Discount on bills A/c')			
Bills purchased and discounted A/c	Dr.	4,000	
To Discount on bills A/c			240
To Clients A/c			3,760
(Being the discounting of bills of exchange during the year)			
Discount on bills A/c	Dr.	18	
To Rebate on bills discounted A/c			18
(Being the unexpired portion of discount in respect of the discounted bills of exchange carried forward)			
Discount on bills A/c	Dr.	249	
To Profit and Loss A/c			249
(Being the amount of income for the year from discounting of bills of exchange transferred to Profit and loss A/c)			

Working Notes:

1. Discount received on the bills discounted during the year

$$\text{` } 4{,}000 \text{ crores} \times \frac{15}{100} \times \frac{146}{365} = \text{` } 240 \text{ crores}$$

2. Calculation of rebate on bill discounted

` 600 crores $\times \frac{15}{100} \times \frac{73}{365}$ = ` 18 crores

(It is assumed that discounting rate of 15% is used for the bill of ` 600 crores also)

3. Income from bills discounted transferred to Profit and Loss A/c would be calculated by preparing Discount on bills A/c

Discounted on bills A/c

` in crores

Date	*Particulars*	*Amount*	*Date*	*Particulars*	*Amount*
31 March 2010	To Rebate on bills discounted	18	1st April, 2009	By Rebate on bills discounted	27
"	To Profit and Loss A/c (Bal.Fig.)	249	2009-10	By Bills purchased and discounted	240
		267			267

PS: In the first sentence of the question the date 31st March, 2010 printed therein may be read as 31st March, 2009 and accordingly the journal entries have been provided on this basis.

(c) Memorandum Trading A/c

(1.4.09 to 20.10.09)

Particulars	(`)	*Particulars*	(`)
To Opening stock (Refer W.N.)	2,40,000	By Sales (`6,20,000 – `80,000)	5,40,000
To Purchases (` 2,80,000 + ` 40,000)	3,20,000	By Closing stock (balancing figure)	1,55,000
To Gross profit (` 5,40,000 x 25%)	1,35,000		
	6,95,000		6,95,000

	`
Stock on the date of fire (i.e. on 20.10.2009)	1,55,000
Less: Stock salvaged	(31,000)
Stock destroyed by fire	1,24,000

Insurance claim = $\frac{\text{Loss of stock}}{\text{Value of stock on the date of fire}} \times$ Amount of policy

= $\frac{1,24,000}{1,55,000} \times 1,00,000$ = ` 80,000

Working Note:

Stock as on 1st April, 2009 was valued at 10% lower than cost.

Hence, original cost of the stock as on 1st April, 2009 would be

$$= \frac{2,16,000}{90} \times 100 = \text{` } 2,40,000$$

(d) As per para 12 of AS 9 'Revenue Recognition', in a transaction involving the rendering of services, performance should be measured either under the completed service contract method or under the proportionate completion method, whichever relates the revenue to the work accomplished. Further, appendix to AS 9 states that revenue from advertising should be recognized when the service is completed. The service as regards advertisement is deemed to be completed when the related advertisement appears before the public.

In the given problem, 40% of the advertisement appeared before the public in November, 2009 and balance 60% in December, 2009.

Total profit will be computed as follows:

	` in lakhs
Advertisement for 70% of available time obtained by 30th September, 2009	700
Advertisement for 30% of available time obtained in by October, 2009	240
Total	940
Less: Cost of advertisement rights	(520)
Profit	420

The profit amounting ` 420 lakhs should be apportioned in the ratio of 40:60 for the months of November and December, 2009. Thus, the company should recognise ` 168 lakhs (i.e. ` 420 lakhs x 40%) in November, 09 and rest ` 252 lakhs (i.e. ` 420 lakhs x 60%) in December, 2009.

Question 2

P, Q, R are three doctors who are running a Polyclinic. Their capital on 31st March, 2009 was ` 1,00,000 each. They agreed to admit X, Y and Z as partners w.e.f. 1st April 2009. The terms for sharing profits & losses were as follows:

(a) 70% of the visiting fee is to go to the specialist concerned.

(b) 50% of the chamber fee will be payable to the individual specialist.

(c) 40% of operation fee and fee for pathological reports, X-rays and ECG will accrue in favour of the doctor concerned.

(d) Balance of profit or loss is shared equally.

(e) All the partners are entitled for 6% interest on capital employed.

They further agreed that:

(i) X, Y and Z brought in ` 20,000 each as goodwill. Goodwill is shared by the existing partners equally.

(ii) X, Y and Z brought in ` 50,000 each as capital. Each of the original partners also contributed ` 50,000 by way of capital.

The receipts for the year after admission of new partners were:

Name of doctors	Particulars	Visiting Fees (`)	Chambers Fees (`)	Fees for reports, operation etc. (`)
P	General Physician	1,50,000	2,00,000	-
Q	Gynecologist	25,000	1,75,000	1,00,000
R	Cardiologist	-	1,00,000	75,000
X	Child Specialist	1,00,000	1,50,000	-
Y	Pathologist		-	1,00,000
Z	Radiologist		40,000	2,00,000
	Total	2,75,000	6,65,000	4,75,000

Expenses for the year were as follows:

Particulars	`
Medicines, injections and other consumables	1,00,000
Printing and stationery	5,000
Telephone expenses	5,000
Rent	42,000
Power and light	10,000
Nurses salary	20,000
Attendants wages	20,000
Total	2,02,000
Depreciation:	
X-Ray machines	15,000
ECG equipments	5,000
Furniture	5,000
Surgical equipments	5,000
Total Depreciation	30,000

You are requested to:

(i) Pass necessary journal entries on admission of partners.

(ii) Prepare the Profit and Loss Account of the polyclinic for the year ended 31st March, 2010.

(iii) Prepare capital accounts of all the partners at the end of the financial year 2009-10. Also show the distribution of profit among partners. *(16 Marks)*

Answer

(a) (i) Journal Entries (on admission of partners)

Date	*Particulars*		*Debit (`)*	*Credit (`)*
1st April, 2009	X's capital A/c	Dr.	20,000	
	Y's capital A/c	Dr.	20,000	
	Z's capital A/c	Dr.	20,000	
	To P's capital A/c			20,000
	To Q's capital A/c			20,000
	To R's capital A/c			20,000
	(Being goodwill adjusted through capital accounts)			
	Bank A/c	Dr.	2,10,000	
	To X's capital A/c (20,000 + 50,000)			70,000
	To Y's capital A/c (20,000 + 50,000)			70,000
	To Z's capital A/c (20,000 + 50,000)			70,000
	(Being goodwill and capital brought in by new partners)			
	Bank A/c	Dr.	1,50,000	
	To P's capital A/c			50,000
	To Q's capital A/c			50,000
	To R's capital A/c			50,000
	(Being capital brought in by existing partners)			

(ii) Profit & Loss A/c

for the year ended 31st March, 2010

Particulars	(`)	Particulars	(`)
To Medicines, injections and other consumables	1,00,000	By Visiting fee	2,75,000
To Printing and stationery	5,000	By Chamber fee	6,65,000

To Telephone expenses	5,000	By Fee for report, operation etc.	4,75,000
To Rent	42,000		
To Power and light	10,000		
To Nurses salary	20,000		
To Attendants wages	20,000		
To Depreciation			
X-ray machine 15,000 ECG equipment 5,000 Furniture 5,000 Surgical equipment 5,000	30,000		
To Interest on capital (W.N.3)	39,600		
To Net profit transferred to partners' capital accounts	11,43,400		
	14,15,000		14,15,000

(iii) Partners' Capital A/cs

for the year ended 31st March, 2010

Debit side

Particulars	*P*	*Q*	*R*	*X*	*Y*	*Z*
	`	`	`	`	`	`
To P, Q & R A/cs (Goodwill)	-	-	-	20,000	20,000	20,000
To Balance c/d	4,56,600	3,96,600	3,31,600	2,69,400	1,64,400	2,24,400
	4,56,600	3,96,600	3,31,600	2,89,400	1,84,400	2,44,400

Credit side

Particulars	*P*	*Q*	*R*	*X*	*Y*	*Z*
	`	`	`	`	`	`
By Balance b/d	1,00,000	1,00,000	1,00,000	-	-	-
By X, Y & Z A/cs (Goodwill)	20,000	20,000	20,000	-	-	-
By Bank	50,000	50,000	50,000	70,000	70,000	70,000
By Interest on capital	10,200	10,200	10,200	3,000	3,000	3,000
By Fee (share) (W.N.1)	2,05,000	1,45,000	80,000	1,45,000	40,000	1,00,000
By Profit (share) (W.N.2)	71,400	71,400	71,400	71,400	71,400	71,400
	4,56,600	3,96,600	3,31,600	2,89,400	1,84,400	2,44,400

Working Notes:

1. Statement showing distribution of fee among partners

Partner Name	*Visiting fees (70%) (`.)*	*Chamber fees (50%) (`)*	*Operations fees (40%) (`)*	*Total (`)*
P	1,05,000	1,00,000	-	2,05,000
Q	17,500	87,500	40,000	1,45,000
R	-	50,000	30,000	80,000
X	70,000	75,000	-	1,45,000
Y	-	-	40,000	40,000
Z	-	20,000	80,000	1,00,000
	1,92,500	3,32,500	1,90,000	7,15,000

2. Statement showing distribution of profit among partners

	`
Profits as per profit and loss account	11,43,400
Less: Fee payable to partners	7,15,000
Profit to be divided equally among partners	4,28,400

Share of each partner in remaining profit = ` 4,28,400/6 = `71,400.

3. Interest on capital employed

	P	Q	R	X	Y	Z
	`	`	`	`	`	`
Opening balance	1,00,000	1,00,000	1,00,000	-	-	-
Add: Premium for goodwill shared equally by old partners	20,000	20,000	20,000	-	-	-
Add: Capital brought in cash	50,000	50,000	50,000	50,000	50,000	50,000
	1,70,000	1,70,000	1,70,000	50,000	50,000	50,000
Interest @ 6%	10,200	10,200	10,200	3,000	3,000	3,000

Total interest = ` 39,600.

Note: It is assumed that amount of premium for goodwill brought in by new partners X, Y and Z has not been withdrawn by old partners P, Q and R and it is still kept in the business.

Question 3

Balance Sheets as on 31st March, 2010

Liabilities	Gee Ltd.	Pee Ltd	Assets	Gee Ltd.	Pee Ltd.
	`	`		`	`
Equity share capital	25,00,000	15,00,000	Buildings	12,50,000	7,75,000
(` 10 per share)			Plant and machinery	16,25,000	8,50,000
14% Preference share capital	11,00,000	8,50,000	Furniture and fixtures	2,87,500	1,75,000
(` 100 each)	-	-	Investments	3,50,000	2,50,000
General reserve	2,50,000	2,50,000	Stock	6,25,000	4,75,000
Export profit reserve	1,50,000	1,00,000	Debtors	4,00,000	4,60,000
Investment allowance reserve	-	50,000	Bills receivables	50,000	55,000
Profit and loss account	3,75,000	1,25,000	Cash at bank	3,62,500	2,60,000
15% Debentures (` 100 each)	2,50,000	1,75,000			
Trade creditors	1,50,000	75,000			
Bills payables	75,000	1,00,000			
Other current liabilities	1,00,000	75,000			
	49,50,000	33,00,000		49,50,000	33,00,000

All the bills receivables of Pee Ltd. were having Gee Ltd.'s acceptances.

Gee Ltd. takes over Pee Ltd. on 1st April, 2010. The purchase consideration is discharged as follows:

(i) Issued 1,65,000 equity shares of ` 10 each at par to the equity shareholders of Pee Ltd.

(ii) Issued 15% preference shares of ` 100 each to discharge the preference shareholders of Pee Ltd. at 10% premium.

(iii) The debentures of Pee Ltd. will be converted into equivalent number of debentures of Gee Ltd.

(iv) The statutory reserves of Pee Ltd. are to be maintained for two more years.

(v) Expenses of amalgamation amounting to ` 10,000 will be borne by Gee Ltd.

Show the opening Journal entries and the opening balance sheet of Gee Ltd. as at 1st April, 2010 after amalgamation, on the assumption that the amalgamation is in the nature of the merger. *(16 Marks)*

Answer

(a) In the books of Gee Ltd.

Journal Entries

Particulars		*Debit* `	*Credit* `
Business purchase A/c (W.N.1)	Dr.	25,85,000	
To Liquidator of Pee Ltd.			25,85,000
(Being business of Pee Ltd. taken over)			
Building A/c	Dr.	7,75,000	
Plant and machinery A/c	Dr.	8,50,000	
Furniture and fixtures A/c	Dr.	1,75,000	
Investments A/c	Dr.	2,50,000	
Stock A/c	Dr.	4,75,000	
Debtors A/c	Dr.	4,60,000	
Bills receivables A/c	Dr.	55,000	
Cash at bank A/c	Dr.	2,60,000	
To General reserve A/c (W.N.2) (2,50,000-2,35,000)			15,000
To Export profit reserve A/c			1,00,000
To Investment allowance reserve A/c			50,000
To Profit and loss A/c			1,25,000
To 15% Debentures A/c (` 100 each)			1,75,000
To Trade creditors A/c			75,000
To Bills payables A/c			1,00,000
To Other current liabilities A/c			75,000
To Business purchase A/c			25,85,000
(Being assets and liabilities taken over)			
Liquidator of Pee Ltd.	Dr.	25,85,000	
To Equity share capital A/c			16,50,000
To 15% Preference share capital A/c			9,35,000
(Being purchase consideration discharged)			
General Reserve A/c	Dr.	10,000	
To Cash at bank			10,000
(Being expenses of amalgamation paid)			
15% Debentures in Pee Ltd. A/c	Dr.	1,75,000	
To 15% Debentures A/c			1,75,000
(Being debentures in Pee Ltd. discharged by issuing own 15% debentures)			

Bills payables A/c	Dr.	55,000	
To Bill receivables A/c			55,000
(Cancellation of mutual owing on account of bills of exchange)			

Opening Balance Sheet of Gee Ltd. (after absorption)

as on 1st April, 2010

Liabilities	*(`)*	*Assets*	*(`)*
Share capital		Fixed assets	
4,15,000 Equity share capital of `10 each (25,00,000 + 16,50,000)	41,50,000	Buildings (12,50,000 + 7,75,000)	20,25,000
15% Preference share capital of `100 each	9,35,000	Plant and machinery (16,25,000 + 8,50,000)	24,75,000
14% Preference share capital of Rs 100 each	11,00,000	Furniture and fixtures (2,87,500 + 1,75,000)	4,62,500
Reserves and Surplus		Investments (3,50,000 + 2,50,000)	6,00,000
General reserves (2,50,000+15,000-10,000)	2,55,000	Current assets, loans and advances	
Export profit reserve (1,50,000+1,00,000)	2,50,000	Stock (6,25,000+ 4,75,000)	11,00,000
Investment allowance reserve	50,000	Sundry debtors (4,00,000 + 4,60,000)	8,60,000
Profit and loss A/c (3,75,000+1,25,000)	5,00,000	Bills receivables (50,000 + 55,000 – 55,000)	50,000
Secured loans		Cash at bank (3,62,500 + 2,60,000 – 10,000)	6,12,500
15% Debentures (2,50,000+1,75,000)	4,25,000		
Current liabilities and provisions			
Trade creditors (1,50,000 + 75,000)	2,25,000		
Bills payable (75,000+1,00,000-55,000)	1,20,000		
Other current liabilities (1,00,000+75,000)	1,75,000		
	81,85,000		81,85,000

Working Notes:

1. Calculation of purchase consideration

	`
Equity shareholders of Pee Ltd. (1,65,000 x ` 10)	16,50,000
Preference shareholders of Pee Ltd. (8,50,000 x 110%)	9,35,000
Purchase consideration would be	25,85,000

2. Amount to be adjusted from general reserve

The difference between the amount recorded as share capital issued and the amount of share capital of transferor company should be adjusted in General Reserve.

Thus, General reserve will be adjusted as follows:

	`
Purchase consideration	25,85,000
Less: Share capital issued (` 15,00,000 + ` 8,50,000)	(23,50,000)
Amount to be adjusted from general reserve	2,35,000

Question 4

(a) *Sunlife General Insurance Company submits the following information for the year ended 31st March 2010:*

Particulars		*Direct Business* `	*Reinsurance* `
Premium received		*65,75,000*	*9,50,000*
Premium paid		*------*	*4,75,000*
Claims paid during the year		*42,50,000*	*5,00,000*
Claims payable	*1st April, 2009*	*6,25,000*	*87,000*
	31st March, 2010	*7,18,000*	*60,000*
Claims received		*---*	*3,25,000*
Claims receivable	*1st April, 2009*		*65,000*
	31st March, 2010		*1,10,000*
Expenses of management		*2,30,000*	
Commission			
On insurance accepted		*1,50,000*	*11,000*
On insurance ceded			*14,000*

The following additional information is also available:

(1) Expenses of management include ` 35,000 surveyor's fee and ` 45,000 legal expenses for settlement of claims.

(2) Reserve for unexpired risk is to be maintained @ 40%. The balance of reserve for unexpired risk as on 1.4.09 was ` 24,50,000.

You are required to prepare the Revenue Account for the year ended 31st March, 2010.

(8 Marks)

(b) KG Limited furnishes the following Balance Sheet as at 31st March, 2010.

Liabilities	*(` in lakhs)*	*Assets*	*(` in lakhs)*
Equity share capital (fully paid up shares of ` 10 each)	*1,200*	*Machinery*	*1,800*
Securities premium	*175*	*Furniture*	*226*
General reserve	*265*	*Investment*	*74*
Capital redemption reserve	*200*	*Stock*	*600*
Profit & loss A/c	*170*	*Debtors*	*260*
12% Debentures	*750*	*Cash at bank*	*740*
Sundry creditors	*745*		
Other current liabilities	*195*		
	3,700		*3,700*

On 1st April, 2010, the company announced the buy back of 25% of its equity shares @ ` 15 per share. For this purpose, it sold all of its investments for ` 75 lakhs.

On 5th April, 2010, the company achieved the target of buy back. On 30th April, 2010 the company issued one fully paid up equity share of ` 10 by way of bonus for every four equity shares held by the equity shareholders.

You are required to:

(1) Pass necessary journal entries for the above transactions.

(2) Prepare Balance Sheet of KG Limited after bonus issue of the shares. *(8 Marks)*

Answer

(a) Form B-RA (Prescribed by IRDA)

Sunlife General Insurance Company

Revenue Account for the year ended 31st March, 2010

Particulars	*Schedule*	*Amount (`)*
Premium earned (net)	1	66,80,000
Interest, dividend and rent		--

Other income		--
Total (A)		66,80,000
Claims incurred (Net)	2	45,26,000
Commission	3	1,47,000
Operating expenses related to insurance business	4	1,50,000
Bad debts		-
Total (B)		48,23,000
Operating profit from insurance business (A-B)		18,57,000

Schedules forming part of revenue account

Schedule 1 : Premium Earned (Net)

Particulars	`
Premium from direct business	65,75,000
Add: Premium on reinsurance accepted	9,50,000
Less: Premium on reinsurance ceded	(4,75,000)
Net premium	70,50,000
Adjustment for change in reserve for unexpired risks (W.N.2)	(3,70,000)
Total premium earned (net)	66,80,000

Schedule 2 : Claims Incurred (Net)

Particulars	`
Claims paid on direct business (W.N.1)	43,30,000
Add: Re-insurance accepted (W.N.1)	4,73,000
Less: Re-insurance ceded (W.N.1)	(3,70,000)
Net claims paid	44,33,000
Add: Claims outstanding at the end of the year	7,18,000
Less: Claims outstanding at the beginning of the year	(6,25,000)
Total claims incurred	45,26,000

Schedule 3 : Commission

Particulars	`
Commission paid on direct business	1,50,000
Add: Commission on reinsurance accepted	11,000
Less: Commission on reinsurance ceded	(14,000)
	1,47,000

Schedule 4 : Operating Expenses related to Insurance Business

Particulars	`
Expenses of management (2,30,000 – 35,000 – 45,000)	1,50,000
	1,50,000

Working Notes:

1. Claims incurred

Particulars	*Direct business (`)*	*Re-insurance accepted `*	*Re-insurance ceded `*
Paid/received	42,50,000	5,00,000	3,25,000
Add: Outstanding at the end of the year		60,000	1,10,000
Expenses in connection with settlement of claim (35,000 + 45,000)	80,000		
Less: Outstanding at the beginning of the year	____	(87,000)	(65,000)
	43,30,000	4,73,000	3,70,000

2. Change in reserve for unexpired risk

	(`)
Opening reserve as on 31st March, 2009	24,50,000
Less: Closing reserve as on 31st March, 2010 (` 70,50,000 x 40%)	(28,20,000)
	(3,70,000)

(b) In the books of KG Limited

Journal Entries

Date	Particulars		Dr. `	Cr. `
April 1, 2010	Bank A/c	Dr.	75	
	To Investment A/c			74
	To Profit on sale of investment			1
	(Being investment sold on profit)			
April 5	Equity shares buy back A/c	Dr.	450	
	To Bank A/c			450
	(Being the payment made on account of buy back)			

”	Equity share capital A/c	Dr.	300	
	Premium payable on buy back A/c	Dr.	150	
	To Equity shares buy back A/c			450
	(Being the amount due to equity shareholders on buy back)			
April 5	General reserve A/c	Dr.	265	
	Profit and Loss A/c	Dr.	35	
	To Capital redemption reserve A/c			300
	(Being amount equal to nominal value of buy back shares from free reserves transferred to capital redemption reserve account as per the law)			
April 30	Capital Redemption Reserve A/c	Dr.	225	
	To Bonus shares A/c (W.N.1)			225
	(Being the utilization of capital redemption reserve to issue bonus shares)			
”	Bonus shares A/c	Dr.	225	
	To Equity share capital A/c			225
	(Being issue of one bonus equity share for every four equity shares held)			
	Securities premium A/c	Dr.	150	
	To Premium payable on buy back			150
	(Being premium payable on buy back adjusted from securities premium account)			

Balance Sheet (After buy back and issue of bonus shares)

` in lakhs

Liabilities	*Amount*	*Assets*	*Amount*
Equity share capital (Fully paid up shares of `10 each)	1,125	Machinery Furniture	1,800 226
Capital Redemption Reserve (200+300-225)	275	Stock Debtors	600 260
Securities premium (175-150)	25	Cash at bank (W.N.2)	365
Profit & Loss A/c (170+1-35)	136		
12% Debentures	750		

Sundry creditors	745	
Other current liabilities	195	
	3,251	3,251

Working Notes:

1. Amount of bonus shares = 25% of (1,200 - 300) lakhs = ` 225 lakhs
2. Cash at bank after issue of bonus shares

	` in lakhs
Cash balance as on 1st April, 2010	740
Add: Sale of investments	75
	815
Less: Payment for buy back of shares	(450)
	365

Note: In the given solution, it is possible to adjust transfer to capital redemption reserve account or capitalization of bonus shares from any other free reserves also.

Question 5

(a) On 1st April, 2009 XY Ltd. has 15,000 equity shares of ABC Ltd. at a book value of ` 15 per share (face value ` 10 per share). On 1st June, 2009, XY Ltd. acquired 5,000 equity shares of ABC Ltd. for ` 1,00,000 on cum right basis. ABC Ltd. announced a bonus and right issue.

(1) Bonus was declared, at the rate of one equity share for every five shares held, on 1st July 2009.

(2) Right shares are to be issued to the existing shareholders on 1st September 2009. The company will issue one right share for every 6 shares at 20% premium. No dividend was payable on these shares.

(3) Dividend for the year ended 31.3.2009 were declared by ABC Ltd. @ 20%, which was received by XY Ltd. on 31st October 2009.

XY Ltd.

(i) Took up half the right issue.

(ii) Sold the remaining rights for ` 8 per share.

(iii) Sold half of its share holdings on 1st January 2010 at ` 16.50 per share. Brokerage being 1%.

You are required to prepare Investment account of XY Ltd. for the year ended 31st March 2010 assuming the shares are being valued at average cost. (8 Marks) *(b) Income and Expenditure Account for the year ended 31st March, 2010 of South Asia Club is given below:*

Expenditure	`	Income	`
To Salaries & wages	47,500	By Subscription	75,000
To Miscellaneous expenses	5,000	By Entrance fee	2,500
To Audit fee	2,500	By Contribution for annual	7,500
To Executive's honorarium	10,000	day (After deducting	
To Sports day expenses	5,000	expenses ` 7,500)	
To Printing & stationary	4,500		
To Interest on bank loan	1,500		
To Depreciation on sports equipment	3,000		
To Excess of income over expenditure	6,000		
	85,000		85,000

Following additional information are also available:

		31.3.2009 `	31.3.2010 `
(1)	Subscription received in advance	4,500	2,700
(2)	Subscription outstanding	6,000	7,500
(3)	Salaries outstanding	4,000	4,500
(4)	Sports equipment (After deducting depreciation)	26,000	27,000

(5) Cash in hand on 31-3-10 was ` 16,000.

(6) The club took a 5% loan of ` 30,000 from a bank during 2008-09 for which interest was not paid in the financial year 2009-10.

Prepare Receipts and Payments account of South Asia Club for the year ending 31st March 2010. (8 Marks)

Answer

(a) In the books of XY Ltd.

Investment in equity shares of ABC Ltd.

for the year ended 31st March, 2010

Date	Particulars	No.	Income `	Amount `	Date	Particulars	No.	Income `	Amount `
2009 April 1	To Balance b/d	15,000	-	2,25,000	2009 Sept. 1	By Bank A/c (W.N 3)	-	-	16,000

June 1	To Bank A/c	5,000	--	1,00,000	2009 Oct. 31	By Bank A/c (W.N. 5)	-	30,000	10,000
July 1	To Bonus Issue (W.N. 1)	4,000	-	-	2010 Jan. 1	By Bank A/c (W.N.4)	13,000	-	2,12,355
Sept.1	To Bank A/c (W.N. 2)	2,000	-	24,000	March 31	By Balance c/d (W.N. 6)	13,000	-	1,61,500
2010 March 31	To P & L A/c (W.N. 4)	-	-	50,855					
"	To P & L A/c	-	30,000	-					
		26,000	30,000	3,99,855			26,000	30,000	3,99,855

Working Notes:

1. Calculation of no. of bonus shares issued

$$\text{Bonus Shares} = \frac{15{,}000 \text{ shares} + 5{,}000 \text{ shares}}{5} \times 1 = 4{,}000 \text{ shares}$$

2. Calculation of right shares subscribed

$$\text{Right Shares} = \frac{15{,}000 \text{ shares} + 5{,}000 \text{ shares} + 4{,}000 \text{ shares}}{6} = 4{,}000 \text{ shares}$$

$$\text{Shares subscribed by XY Ltd.} = \frac{4{,}000}{2} = 2{,}000 \text{ shares}$$

Value of right shares subscribed = 2,000 shares @ ` 12 per share = ` 24,000

3. Calculation of sale of right entitlement

2,000 shares x ` 8 per share = ` 16,000

(Since shares are purchased cum right basis, therefore, amount received from sale of rights will be credited to investment a/c)

4. Calculation of profit on sale of shares

Total holding	=	15,000 shares	original
		5,000 shares	purchased
		4,000 shares	bonus
		2,000 shares	right shares
		26,000 shares	

50% of the holdings were sold

i.e. 13,000 shares (26,000 x1/2) were sold.

Cost of total holdings of 26,000 shares (on average basis)

= ` 2,25,000 + ` 1,00,000 + ` 24,000 –` 16,000 – ` 10,000

= ` 3,23,000

Average cost of 13,000 shares would be

$= \frac{3,23,000}{26,000} \times 13,000$ = ` 1,61,500

	`
Sale proceeds of 13,000 shares (13,000 x `16.50)	2,14,500
Less: 1% Brokerage	(2,145)
	2,12,355
Less: Cost of 13,000 shares	(1,61,500)
Profit on sale	50,855

5. Dividend received on investment held as on 1st April, 2009

= 15,000 shares x ` 10 x 20%

= ` 30,000 will be transferred to Profit and Loss A/c

Dividend received on shares purchased on 1st June, 2009

= 5,000 shares x ` 10 x 20% = Rs 10,000 will be adjusted to Investment A/c

Note: It is presumed that no dividend is received on bonus shares as bonus shares are declared on 1st July, 2009 and dividend pertains to the year ended 31.3.2009.

6. Calculation of closing value of shares (on average basis) as on 31st March, 2010

$13,000 \times \frac{3,23,000}{26,000}$ = ` 1,61,500.

Closing value of shares would be ` 1,61,500.

(b) In the books of South Asia Club

Receipt and Payment Account

for the year ended 31st March, 2010

Receipt	*Amount* `	*Payment*	*Amount* `
To Balance b/d (Bal.fig.)	12,300	By Salaries & Wages (W.N.2)	47,000
To Subscription (W.N.1)	71,700	By Miscellaneous Expenses	5,000

To Entrance fee	2,500	By Audit fee	2,500
To Contribution for annual day (` 7,500 + ` 7,500)	15,000	By Executive's honorarium	10,000
		By Sports Day Expenses	5,000
		By Printing & Stationary	4,500
		By Expenses of Annual Day	7,500
		By Sports Equipment (W.N.3)	4,000
		By Balance c/d	16,000
	1,01,500		1,01,500

Working Notes

(1) Subscription received during the year

		`
Subscription credited to Income and Expenditure A/c		75,000
Add: Outstanding subscription at the beginning of the year		6,000
Advance subscription received at the end of the year		2,700
		83,700
Less: Outstanding subscription at the end of the year	7,500	
Advance subscription received at the beginning of the year	4,500	12,000
Subscription received during the year		71,700

(2) Salaries & wages paid during the year

	`
Salaries debited to Income and Expenditure Account	47,500
Add: Outstanding salaries at the beginning of the year	4,000
Less: Outstanding salaries at the end of the year	(4,500)
Salaries paid during the year	47,000

(3) Sports equipment purchased during the year

Sports Equipment A/c

Particulars	*Amount* `	*Particulars*	*Amount* `
To Balance b/d	26,000	By Depreciation A/c	3,000
To Cash (Bal.Fig.)	4,000	By Balance c/d	27,000
	30,000		30,000

Question 6

(a) *From the following information of M/s Chennai Traders, you are required to prepare Hire Purchase Trading Account to ascertain the profit made during the financial year 2009-10.*

Chennai Traders sell goods on hire purchase basis at cost plus 25% . The following details are available:

		`
(1)	*Instalment not due on 31st March, 2009*	*4,50,000*
(2)	*Instalment due and collected during the financial year 2009-10*	*12,00,000*
(3)	*Instalment due but not collected during the financial year 2009-10 which includes ` 15,000 for which goods were repossessed*	*75,000*
(4)	*Instalment not due on 31st March, 2010 including ` 30,000 for which goods were repossessed*	*5,55,000*
(5)	*Instalment collected on repossessed stock*	*22,500*
(6)	*M/s Chennai Traders valued repossessed stock at 60% of original cost.*	

(8 Marks)

(b) *A company had 16,000, 12% debentures of ` 100 each outstanding as on 1st April, 2009, redeemable on 31st March, 2010. On that day, sinking fund was ` 14,98,000 represented by 2,000 own debentures purchased at the average price of ` 99 and 9% stocks face value of ` 13,20,000. The annual instalment was ` 56,800.*

On 31st March, 2010 the investments were realized at ` 98 and the debentures were redeemed. You are required to write up the following accounts for the year ending 31st March 2010:

(1) 12% Debentures account

(2) Debenture redemption sinking fund account. *(8 Marks)*

Answer

(a) In the books of M/s Chennai Traders

Hire Purchase Trading A/c (at invoice value)

Particulars	`	*Particulars*	`
To Goods with customer at cost (31st March, 2009)	4,50,000	By Stock reserve (Opening)	90,000
To Goods sold on Hire Purchase (W.N.3)	13,50,000	By Hire purchase sales	12,75,000
To Bad debts	3,000	By Goods sold on hire purchase (loading)	2,70,000

To	Loss on repossession	3,600	By	Goods with customer (at cost) (31st March, 2010)	5,25,000
To	Stock reserve (Closing)	1,05,000			
To	Profit & Loss A/c				
	(Transfer of H.P. profit)	2,48,400			
		21,60,000			21,60,000

Working Notes:

1. Hire purchase sales

	`
Installments due and collected	12,00,000
Add: Installments due but not collected	75,000
	12,75,000

2. Loss on repossessed goods

	`
Hire purchase price of repossessed goods	
Installments collected	22,500
Installments due	15,000
Installments not due	30,000
	67,500
	`
Cost of repossessed goods (`67,500 x 100/125)	54,000
Valuation of repossessed goods (`54,000 x 60/100)	32,400
Less: Cost of installments due + Installments not yet due	
(` 15,000 + 30,000) x 100/125	36,000
Loss on repossession	3,600

3. Goods taken from shop stock :

	`
Hire purchase sales (12,00,000+75,000)	12,75,000
Add: Stock with customer as on 31st March 2010	
(5,55,000 – 30,000)	5,25,000
Less: Stock with Customer as on 31st March, 2009	(4,50,000)
	13,50,000

Loading on goods taken from shop stock

= ` 13,50,000 x (25/125)= ` 2,70,000

4.	Bad Debt	`
	Installment due but not collected	15,000
	Add: Installment not yet due at cost	24,000
		39,000
	Less: Cost of installments due and not yet due	(36,000)
		3,000

In other words `15,000 x (25/125) = ` 3,000

Note: It is presumed that all the figures given in the question is at invoice price

(b) 12% Debentures Account

Date	*Particulars*	`	*Date*	*Particulars*	`
31st March, 2010	To Own debentures A/c	2,00,000	1st April, 2009	By Balance b/d	16,00,000
	To Bank A/c	14,00,000			
		16,00,000			16,00,000

Debenture Redemption Sinking Fund Account					
Date	*Particulars*	`	*Date*	*Particulars*	`
31st March, 2010	To 9% Stock A/c (loss) (W.N.5)	6,400	1st April, 2010	By Balance b/d	14,98,000
	To General reserve A/c (Bal.fig.)	16,93,200	31st March, 2010	By Profit and loss A/c	56,800
				By Interest on sinking fund A/c (W.N.3)	1,42,800
				By Own debentures A/c (W.N.4)	2,000
		16,99,600			16,99,600

Working Notes:

1. Amount of stock as on 1st April, 2009

	`
Sinking fund balance as on 1st April, 2009	14,98,000
Less: Own debentures	(1,98,000)
	13,00,000

2. Sales value of 9% stock

   = Face value / ` per stock

   = ` 13,20,000 / ` 100 = 13,200 stock

   Sales value = 13,200 stock x ` 98 per stock

   = ` 12,93,600

3. Interest credited to Sinking Fund

   (i) Interest on 9% stock (` 13,20,000 x 9%) ` 1,18,800

   (ii) Interest on own debentures (2,000 Debentures x ` 100 x 12%) ` 24,000

   ` 1,42,800

4. Own debentures account

		`			`
1st April, 2009	To Balance b/d	1,98,000	31st March, 2010	By 12% debenture A/c	2,00,000
31st March, 2010	To Sinking fund A/c	2,000			
		2,00,000			2,00,000

5. 9% Stock account

		`			`
1st April, 2009	To Balance b/d (Face value ` 13,20,000) (W.N.1)	13,00,000	31st March, 2010	By Bank account (W.N.2)	12,93,600
				By Sinking fund (loss on sales)	6,400
		13,00,000			13,00,000

PAPER – 1 : ADVANCED ACCOUNTING

Question 7

Answer any four *questions:*

(a) *"While calculating diluted earning per share, effect is given to all dilutive potential equity shares that were outstanding during that period." Explain. Also calculate the diluted earnings per share from the following information:*

Net profit for the current year	`	*85,50,000*
No. of equity shares outstanding		*20,00,000*
No. of 8% convertible debentures of ` 100 each		*1,00,000*
Each debenture is convertible into 10 equity shares		
Interest expenses for the current year	`	*6,00,000*
Tax relating to interest expenses		*30%*

(b) *Gupta Traders keep their ledgers on the self balancing system. They provide you the following information for the year ended 31st March, 2010:*

	`
Debtors balance on 1st April, 2009	*1,37,250*
Credit sales	*68,100*
Returns inward	*1,200*
Returns outward	*1,800*
Cash received from customers	*76,800*
Discount received	*2,010*
Acceptances received	*25,500*
Bills receivable dishonoured	*3,600*
Bad debts written off	*7,500*

You are required to prepare General Ledger Adjustment A/c in Sales Ledger of Gupta Traders.

(c) *What is employee stock option plan? Explain the importance of such plans in the modern time.*

(d) *A Ltd. purchased a machinery for ` 40 lakhs. (Useful life 4 years and residual value ` 8 lakhs) Government grant received is ` 16 lakhs.*

Show the Journal Entry to be passed at the time of refund of grant and the value of the fixed assets, if:

(1) *the grant is credited to fixed assets.*

(2) *the grant is credited to Deferred Grant A/c.*

(e) "Recently a growing trend has developed for outsourcing the accounting function". Explain the advantages and disadvantages of outsourcing the accounting functions.

(4 x 4 = 16 Marks)

Answer

(a) "In calculating diluted earnings per share, effect is given to all dilutive potential equity shares that were outstanding during the period." As per para 26 of AS 20 'Earnings per Share', the net profit or loss for the period attributable to equity shareholders and the weighted average number of shares outstanding* during the period should be adjusted for the effects of all dilutive potential equity shares for the purpose of calculation of diluted earnings per share.

Computation of diluted earnings per share

$$\frac{\text{Adjusted net profit for the current year}}{\text{Weighted average number of equity shares}}$$

Adjusted net profit for the current year

	Rs.
Net profit for the current year (assumed to be after tax)	85,50,000
Add: Interest expense for the current year	6,00,000
Less: Tax relating to interest expense (30% of Rs. 6,00,000)	1,80,000
Adjusted net profit for the current year	89,70,000

Weighted average number of equity shares

Number of equity shares resulting from conversion of debentures

$$= \frac{1,00,000 \times 100}{10} = 10,00,000 \text{ Equity shares}$$

Weighted average number of equity shares used to compute diluted earnings per share

= [(20,00,000 x 12) + (10,00,000 x 9**)]/12 = 27,50,000 shares

$$\text{Diluted earnings per share} = \frac{89,70,000}{27,50,000 \text{ shares}} = ` \ 3.26 \text{ per share}$$

---

* Weighted average number of equity shares outstanding during the period is increased by the weighted average number of additional equity shares which would have been outstanding assuming the conversion of all dilutive potential equity shares.

** Interest on debentures for full year amounts to Rs. 8,00,000 (i.e. 8% of Rs.1,00,00,000). However, interest expense amounting Rs.6,00,000 has been given in the question. It may be concluded that debentures have been issued during the year and interest has been provided for 9 months.

(b) In the books of Gupta Traders

General Ledger Adjustment A/c in the Sales Ledger

Date	*Particulars*	*Amount*	*Date*	*Particulars*	*Amount*
		`			`
1 April, 2009 to 31st March, 2010	To Sales Ledger Adjustment A/c (in general ledger): Returns inward	1,200	1 April, 09 1 April, 2009 to 31st March, 2010	By Balance b/d By Sales Ledger Adjustment Account (in General Ledger):	1,37,250
	Cash (received from customers)	76,800		Sales B/R dishonoured	68,100 3,600
	Bills receivables	25,500			
	Bad debts	7,500			
31st March 2010	To Balance c/d	97,950			
		2,08,950			2,08,950

Note: Returns outward and discount received would be shown in the General Ledger Adjustment Account of Purchases Ledger.

(c) Employee Stock Option Plan: It is a plan under which the enterprise grants employee stock options. Employee stock option is a contract that gives the employees of the enterprise the right, but not the obligation, for a specified period of time to purchase or subscribe the shares of the company at a fixed or determinable price.

Employee stock option plans encourage employees to have higher participation in the company. The importance of these plans is as follows:

1. Stock options provide an opportunity to employees to contribute in the growth of the company.
2. Stock option creates long term wealth in the hands of the employees.
3. They are important means to attract, retain and motivate the best available talent for the company.
4. It creates a common sense of ownership between the company and its employees.

(d) In the books of A Ltd.

Journal Entries (at the time of refund of grant)

If the grant is credited to fixed assets:

I	Fixed assets A/c	Dr.	` 12 lakhs	
	To Bank A/c			` 12 lakhs
	(Being grant refunded)			

II The balance of fixed assets after two years depreciation will be ` 16 lakhs (W.N.1) and now it will become (` 16 lakhs + ` 12 lakhs) = ` 28 lakhs on which depreciation will be charged for remaining two years. Depreciation = (28-8)/2 = ` 10 lakhs p.a. will be charged for next two years.

If the grant is credited to Deferred Grant Account:

As per para 14 of AS 12 'Accounting for Government Grants,' income from Deferred Grant Account is allocated to Profit and Loss account usually over the periods and in the proportions in which depreciation on related assets is charged. Accordingly, in the first two years (` 16 lakhs /4 years) = ` 4 lakhs x 2 = ` 8 lakhs were credited to Profit and Loss Account and ` 8 lakhs was the balance of Deferred Grant Account after two years.

Therefore, on refund in the 3rd year, following entry will be passed:

I	Deferred Grant A/c	Dr.	` 8 lakhs	
	Profit & Loss A/c	Dr.	` 4 lakhs	
	To Bank A/c			` 12 lakhs
	(Being Government grant refunded)			

II Deferred grant account will become Nil. The fixed assets will continue to be shown in the books at ` 24 lakhs (W.N.2) and depreciation will continue to be charged at ` 8 lakhs per annum.

Working Notes:

1. Balance of Fixed Assets after two years but before refund (under first alternative)

Fixed assets initially recorded in the books

= ` 40 lakhs – ` 16 lakhs = ` 24 lakhs

Depreciation = (` 24 lakhs – ` 8 lakhs)/4 years

= ` 4 lakhs per year

Value of fixed assets after two years but before refund of grant

= ` 24 lakhs – (` 4 lakhs x 2 years) = ` 16 lakhs

2. Balance of Fixed Assets after two years but before refund (under second alternative)

   Fixed assets initially recorded in the books = ` 40 lakhs

   Depreciation = (` 40 lakhs – ` 8 lakhs)/4 years

   = ` 8 lakhs per year

   Book value of fixed assets after two years = ` 40 lakhs – (` 8 lakhs x 2 years)

   = ` 24 lakhs

Note: It is assumed that value of fixed assets is to be given after refund of government grant.

(e) Recently a growing trend has developed for outsourcing the accounting function to a third party. The consideration for doing this is to save cost and to utilise the expertise of the outsourced party.

Advantages

1. The organisation that outsources is able to save time to concentrate on the core area of business activity.
2. Storage and maintenance of the data is in the hands of professional people.
3. The organisation is able to utilise the expertise of the third party.
4. The organisation is not bothered about people leaving the organisation in key accounting positions.

Disadvantages

1. The third party may unable to meet the standards desirable.
2. The cost may ultimately be higher.
3. The data of the organisation are handed over to the third party. This raises two issues of security and confidentiality.
4. Delays in obtaining services.