PAPER – 5 : ADVANCED ACCOUNTING

PART – I : RELEVANT ANNOUNCEMENTS, AMENDMENTS AND NOTIFICATIONS

A. Applicable for May, 2012 examination

1. Limited Revisions due to Issuance of AS 30 and 31

As per the announcement issued by the Accounting Standard Board of the ICAI regarding applicability of AS 30 (dated 11th February, 2011) in respect of the financial statements, it has been clarified that to the extent of accounting treatments covered by any of the existing notified accounting standards (for eg. AS 11, AS 13 etc,) the existing notified accounting standards would continue to prevail over AS 30.

2. Amendment to Accounting Standard 11 of Companies (Accounting Standards) Rules, 2006

Ministry of Corporate Affairs vides its notification number G.S.R. (E) has partially amended the notification number GSR No. 225(E) dated 31.03.2009. Through this notification, the MCA has extended the option (for the enterprises) to capitalize the exchange differences arising on reporting of long term foreign currency monetary items till 31st March 2012 instead of 31st March 2011.

3. Sale of Investments held under Held to Maturity (HTM) category

Securities acquired by banks with the intention to hold them up to maturity may be classified under Held to Maturity (HTM) category. Banks are, however, allowed to shift investments to/from HTM with the approval of the Board of Directors once a year. Such shifting is normally allowed at the beginning of the accounting year and no further shifting to/from HTM is allowed during the remaining part of that accounting year. However, securities under HTM category are intended to be held till maturity and accordingly are not required to be marked to market.

RBI has decided vide a notification that if the value of sales and transfers of securities to/from HTM category exceeds 5 per cent of the book value of investments held in HTM category at the beginning of the year, bank should disclose the market value of the investments held in the HTM category and indicate the excess of book value over market value for which provision is not made. This disclosure is required to be made in 'Notes to Accounts' in banks' audited Annual Financial Statements.

4. Enhancement of Rates of Provisioning for Non-Performing Assets and Restructured Advances

RBI vide its notification RBI 2010-11/529 DBOD.No.BP.BC. 94/21.04.048/2011-12 dated May 18, 2011 has revised provisioning requirements for the following categories of non-performing advances and restructured advances for all Scheduled Commercial Banks (Excluding RRBs) as under:

1. Sub-Standard Advances: Advances classified as "sub-standard" will attract a provision of 15 per cent as against the existing 10 per cent. The "unsecured

exposures" classified as sub-standard assets will attract an additional provision of 10 per cent, *i.e.,* a total of 25 per cent as against the existing 20 per cent. However, "unsecured exposures" in respect of Infrastructure loan accounts classified as sub-standard, in case of which certain safeguards such as escrow accounts are available will attract an additional provision of 5 per cent only i.e. a total of 20 per cent as against the existing 15 per cent.

2. Doubtful Advances: Doubtful Advances will continue to attract 100% provision to the extent the advance is not covered by the realisable value of the security to which the bank has a valid recourse and the realisable value is estimated on a realistic basis. However, in respect of the secured portion, following provisioning requirements will be applicable:

   (i) The secured portion of advances which have remained in "doubtful" category up to one year will attract a provision of 25 per cent (as against the existing 20 per cent);

   (ii) The secured portion of advances which have remained in "doubtful" category for more than one year but upto 3 years will attract a provision of 40 per cent (as against the existing 30 per cent); and

   (iii) The secured portion of advances which have remained in "doubtful" category for more than 3 years will continue to attract a provision of 100%.

3. Restructured Advances:

   (i) Restructured accounts classified as standard advances will attract a provision of 2 per cent in the first two years from the date of restructuring. In cases of moratorium on payment of interest/principal after restructuring, such advances will attract a provision of 2 per cent for the period covering moratorium and two years thereafter (as against existing provision of 0.25-1.00 per cent, depending upon the category of advances); and

   (ii) Restructured accounts classified as non-performing advances, when upgraded to standard category will attract a provision of 2 per cent in the first year from the date of upgradation (as against existing provision of 0.25-1.00 per cent, depending upon the category of advances).

4. All other instructions on provisioning will remain unchanged.

   Rates of Provisioning for Non-Performing Assets and Restructured Advances are summarized as follows:

Category of Advances	Existing Rate (%)	Revised Rate (%)
Sub- standard Advances		
· Secured Exposures	10	15

· Unsecured Exposures	20	25
· Unsecured Exposures in respect of Infrastructure loan accounts where certain safeguards such as escrow accounts are available.	15	20
Doubtful Advances – Unsecured Portion	100	100
Doubtful Advances – Secured Portion		
· For Doubtful upto 1 year	20	25
· For Doubtful > 1 year and upto 3 years	30	40
· For Doubtful > 3 years	100	100
Loss Advances	100	100
Restructured accounts classified as standard advances in the first two years from the date of restructuring; and in cases of moratorium on payment of interest/principal after restructuring – period covering moratorium and two years thereafter.	0.25 to 1.00 (depending upon the category of advance)	2
Restructured accounts earlier classified as NPA and later upgraded to standard category in the first year from the date of upgradation	0.25 to 1.00 (depending upon the category of advance)	2

B. Not Applicable for May, 2012 Examination

(i) Schedule VI revised by the Ministry of Corporate Affairs

The Ministry of Corporate Affairs (MCA) has revised Schedule VI to the Companies Act, 1956 on the 28th February, 2011 pertaining to the preparation of Balance Sheet and Profit and Loss Account under the Companies Act, 1956. This revised Schedule VI has been framed as per the existing non-converged Indian Accounting Standards notified under the Companies (Accounting Standards), Rules, 2006. The Revised Schedule VI shall come into force for the Balance Sheet and Profit and Loss Account to be prepared for the financial year commencing on or after 1.4.2011. However, the revised Schedule VI is not made applicable for May, 2012 examination.

(ii) Ind ASs issued by the Ministry of Corporate Affairs

The Ministry of Corporate Affair (MCA) has issued 35 Converged Indian Accounting Standards (known as 'Ind-AS'), without announcing the applicability date. The issuance of Ind-AS is a significant step towards the implementation of converged standards in India. However, Ind ASs are not made applicable for May, 2012 examination.

PART – II : QUESTIONS AND ANSWERS

QUESTIONS WITH HINTS

Employee Stock Option Plans

1. On 1st April, 2010, a company offered 100 shares to each of its 500 employees at ₹ 50 per share. The employees are given a month to accept the offer. The shares issued under the plan shall be subject to lock-in on transfer for three years from the grant date. The market price of shares of the company on the grant date is ₹ 60 per share. Due to post-vesting restrictions on transfer, the fair value of shares issued under the plan is estimated at ₹ 56 per share.

   On 30th April, 2010, 400 employees accepted the offer and paid ₹ 50 per share purchased. Nominal value of each share is ₹ 10.

   Record the issue of share in the books of the company under the aforesaid plan.

Buy –Back of Shares

2. Kuber Ltd. furnishes you with the following Balance Sheet as at 31st March, 2011:

	(₹ in crores)	
Sources of funds:		
Authorised share capital:		100
Issued share capital:		
12% Redeemable preference shares of ₹ 100 each fully paid	75	
Equity shares of ₹ 10 each fully paid	25	100
Reserves and surplus:		
Capital reserve	15	
Securities premium	25	
Revenue reserves	260	300
		400
Funds employed in:		
Fixed assets: Cost	100	
Less: Provision for depreciation	(100)	nil
Investment at cost (market value ₹ 400 Cr.)		100
Current assets	340	
Less: Current liabilities	(40)	
		300
		400

   The company redeemed preference shares on 1st April, 2011. It also bought back 50 lakhs equity shares of ₹ 10 each at ₹ 50 per share. The payments for the above were made out of the huge bank balances, which appeared as part of current assets.

You are asked to :

(i) Pass journal entries to record the above.

(ii) Prepare balance sheet (after reconstruction).

(iii) Value an equity share on net asset basis.

Underwriting of Shares

3. Ram Limited invited applications from public for 10,00,000 equity shares of ₹ 10 each at a premium of ₹ 5 per share. The entire issue was underwritten by the underwriters X, Y, Z and T to the extent of 30%, 30%, 20% and 20% respectively with the provision of firm underwriting of 30,000, 20,000, 10,000 and 10,000 shares respectively. The underwriters were entitled to the maximum 2.5% commission.

   The company received applications for 7,00,000 shares from public, out of which applications for 1,90,000, 1,00,000, 2,10,000 and 80,000 shares were marked in favour of X, Y, Z and T respectively.

   Calculate the gross liability of each underwriter in terms of shares. Also ascertain the underwriting commission, payable to or by different underwriters.

Redemption of Debentures

4. A company had 32,000, 12% debentures of ₹ 100 each outstanding as on 1st April, 2010, redeemable on 31st March, 2011. On that day, sinking fund was ₹ 29,96,000 represented by 4,000 own debentures purchased at the average price of ₹ 99 and 9% stocks face value of ₹ 26,40,000. The annual instalment was ₹ 1,13,600.

   On 31st March, 2011 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 2011:

   (1) 12% Debentures account

   (2) Debenture redemption sinking fund account.

Amalgamation

5. Star and Moon had been carrying on business independently. They agreed to amalgamate and form a new company Neptune Ltd. with an authorised share capital of ₹ 2,00,000 divided into 40,000 equity shares of ₹ 5 each.

   On 31st December, 2011, the respective Balance Sheets of Star and Moon were as follows :

	Star	Moon
	₹	₹
Fixed Assets	3,17,500	1,82,500
Current Assets	1,63,500	83,875
	4,81,000	2,66,375

Less: Current Liabilities	2,98,500	90,125
Representing Capital	1,82,500	1,76,250

Additional Information :

(a) Revalued figures of Fixed and Current Assets were as follows :

	Star	Moon
	₹	₹
Fixed Assets	3,55,000	1,95,000
Current Assets	1,49,750	78,875

(b) The debtors and creditors—include ₹ 21,675 owed by Star to Moon.

The purchase consideration is satisfied by issue of the following shares and debentures:

(i) 30,000 equity shares of Neptune Ltd., to Star and Moon in the proportion to the profitability of their respective business based on the average net profit during the last three years which were as follows :

	Star	Moon
2009 Profit	₹2,24,788	₹1,36,950
2010 (Loss)/Profit	₹ (1,250)	₹1,71,050
2011 Profit	₹1,88,962	₹1,79,500

(ii) 15% debentures in Neptune Ltd., at par to provide an income equivalent to 8% return on capital employed in their respective business as on 31st December, 2011 after revaluation of assets.

You are requested to:

(1) Compute the amount of debentures and shares to be issued to Star and Moon.

(2) A Balance Sheet of Neptune Ltd., showing the position immediately after amalgamation.

Internal Reconstruction of a Company

6. Crystal Limited decided to reconstruct its business as it has accumulated huge losses. The following is the Balance Sheet of the company as on 31.03.2011 before reconstruction:

Balance Sheet as on 31.03.2011

Particulars	₹	Particulars	₹
3,00,000 Equity shares of ₹ 10		Goodwill	5,20,000
each fully paid up	30,00,000	Patents	1,50,000
1,60,000, 6% Preference shares		Land & building	17,00,000
of ₹ 10 each fully paid up	16,00,000	Plant & machinery	2,00,000

6% Debentures (secured against land & building)	15,00,000	Investments (at cost)	2,20,000
		Sundry debtors	17,40,000
Bank overdraft	5,80,000	Stock	17,00,000
Sundry creditors	12,00,000	Profit & loss A/c	18,50,000
Provision for income tax	2,00,000		
	80,80,000		80,80,000

Following scheme of reconstruction is approved by all interested parties and the Court:

(1) All equity shares are reduced to ₹ 3 each and preference shares to ₹ 7 each.

(2) Debentureholders agreed to take over a part of land and building, book value of which is ₹ 7,00,000, towards their 50% claim. Rate of interest of balance 50% debentures will be increased to 9%.

(3) Goodwill and Patent will be written off.

(4) 10% of Sundry Debtors to be provided for bad debts.

(5) Stock to be written off by ₹ 2,60,000.

(6) 50% of balance Land & Building sold for ₹ 6,00,000 and remaining Land & Building valued at ₹ 6,00,000.

(7) Investments to be sold for ₹ 2,00,000.

(8) There are pending contracts amounting to ₹ 10,00,000. These contracts are to be cancelled on payment of penalty @ 5% of pending contract amount.

(9) The income tax liability of the company is settled at ₹ 3,06,000. Provision for income tax will be raised accordingly.

(10) 1/3 of sundry creditors decided to forgo their claim.

(11) After making all the above adjustments, balance amount available through scheme, will be utilized to write off the value of plant & machinery to that extent.

You are required to pass the Journal Entries and draw up the Balance Sheet of the company after reconstruction.

Liquidation of a company

7. The following is the Balance Sheet of Shah Ltd. which is in the hands of the liquidator:

Balance Sheet as at 31.12.2011

Liabilities	₹	Assets	₹
Share Capital:		Fixed assets	2,00,000
1,000, 6% Preference Shares of ₹ 100 each, fully paid	1,00,000	Stock	1,20,000

2,000 Equity shares of ₹ 100 each, fully paid	2,00,000	Book debts	2,40,000
2,000 Equity shares of ₹ 100 each ₹ 75 paid up	1,50,000	Cash in hand	40,000
Loan from bank (on security of stock)	1,00,000	Profit and loss account	3,00,000
Trade creditors	3,50,000		
	9,00,000		9,00,000

The assets realized the following amounts (after all costs of realization and liquidator's commission amounting to ₹ 5,000 paid out of cash in hand).

	₹
Fixed assets	1,68,000
Stock	1,10,000
Book debts	2,30,000

Calls on partly paid shares were made but the amounts due on 200 shares were found to be irrecoverable.

Prepare Liquidator's Final Statement of Receipts and Payments.

Financial Statements of Banking Companies

8. In the following transactions of the Unique Bank Ltd., you are required to indicate the necessary journal entries as well as their treatment in the Profit & Loss Account and Balance Sheet in respect of the year ended 31.12.2011:

(a) The following bills were discounted @ 5%:

	Discounted on	Amount ₹	Due date inclusive of 3 days of grace
(i)	28.12.2011	50,000	31.1.2012
(ii)	29.7.2011	1,00,000	30.11.2011
(iii)	29.10.2011	4,00,000	30.4.2012
(iv)	31.12.2011	30,000	3.3.2012

(b) The Bank has accepted Bills on behalf of its customers amounting to ₹ 2,00,000 at nominal commission of 2%.

(c) The Bank has advanced an amount of ₹ 5,00,000 having a covering for the same through bills worth ₹ 2,00,000 and goods on key-loan basis ₹4,00,000.

Financial Statements of Insurance Companies

9. From the following balances extracted from the books of Great General Insurance Company Limited as on 31.3.2011, you are required to prepare Revenue Accounts in

respect of Fire and marine Insurance business for the year ended 31.3.2011 to and a Profit and Loss Account for the same period :

	₹		₹
Directors' Fee	80,000	Interest received	19,000
Dividend received	1,00,000	Fixed Assets (1.4.2010)	90,000
Provision for Taxation		Income-tax paid during	
(as on 1.4. 2010)	85,000	the year	60,000

	Fire	Marine
	₹	₹
Outstanding Claims on 1.4.2010	28,000	7,000
Claims paid	1,00,000	80,000
Reserve for Unexpired Risk on 1.4.2010	2,00,000	1,40,000
Premiums Received	4,50,000	3,30,000
Agent's Commission	40,000	20,000
Expenses of Management	60,000	45,000
Re-insurance Premium (Dr.)	25,000	15,000

The following additional points are also to be taken into account :

(a) Depreciation on Fixed Assets to be provided at 10% p.a.

(b) Interest accrued on investments ₹ 10,000.

(c) Closing provision for taxation on 31.3.2011 to be maintained at ₹ 1,24,138

(d) Claims outstanding on 31.3.2011 were Fire Insurance ₹ 10,000; Marine Insurance ₹ 15,000.

(e) Premium outstanding on 31.3.2011 were Fire Insurance ₹ 30,000; Marine Insurance ₹ 20,000.

(f) Reserve for unexpired risk to be maintained at 50% and 100% of net premium in respect of Fire and Marine Insurance respectively.

(g) Expenses of management due on 31.3.2011 were ₹ 10,000 for Fire Insurance and ₹ 5,000 in respect of marine Insurance.

Financial Statements of Electricity Company

10. Electric Supply Ltd. rebuilt and re-equipped one of their Mains at a cash cost of ₹ 40,00,000. The old Mains thus superseded cost ₹ 15,00,000. The capacity of the new Main is double that of the old Main. ₹ 70,000 was realised from sale of old materials.

Four old motors valued at ₹ 2,00,000 salvaged from the old Main were used in the reconstruction. The cost of Labour and Materials are respectively 30% and 25% higher now than when the old Main was built. The proportion of Labour to Materials in the Main then and now is 2 : 3.

Show the Journal entries for recording the above transactions.

Departmental Accounts

11. Department L sells goods to Department M at a profit of 25% on cost and to Department N at 10% profit on cost. Department M sells goods to L and N at a profit of 15% and 20% on sales, respectively. Department N charges 20% and 25% profit on cost to Department L and M, respectively.

Department Managers are entitled to 10% commission on net profit subject to unrealised profit on departmental sales being eliminated. Departmental profits after charging Managers' commission, but before adjustment of unrealised profit are as under :

	₹
Department L	1,08,000
Department M	81,000
Department N	54,000

Stock lying at different departments at the end of the year are as under :

	Dept. L ₹	Dept. M ₹	Dept. N ₹
Transfer from Department L	—	45,000	33,000
Transfer from Department M	42,000	—	36,000
Transfer from Department N	18,000	15,000	—

Find out the correct departmental Profits after charging Managers' commission.

Branch Accounts

12. Using the Stock and Debtors system, find out the profit or loss made at the Raipur Branch in 2011.

	₹
Stock (1st January) invoice price	12,000
Debtors (1st January)	6,200
Goods sent to the Branch (invoice price)	35,000
Goods returned by the Branch (invoice price)	10,000
Sales:	
Credit	21,000
Cash	20,000

Goods returned by customers	600
Cash received from debtors	19,800
Discount allowed to them	300
Cash sent for expenses at the Branch	6,100
Shortage of goods at the Branch (invoice price)	400

Goods are invoiced to the Branch at the selling price so as to show a profit of 30% on invoice price.

Accounting for Foreign Branch

13. An Indian company has a branch at New York. Its Trial Balance as at 30th September, 2011 is as follows:

	Dr.	Cr.
	US $	US $
Plant and machinery	12,000	–
Furniture and fixtures	800	–
Stock (October 1, 2010)	5,600	–
Purchases	24,000	–
Sales	–	41,600
Goods sent from Indian Company (H.O.)	8,000	–
Wages	200	–
Carriage inward	100	–
Salaries	600	–
Rent, rates and taxes	200	–
Insurance	100	–
Trade expenses	100	–
Head Office A/c	–	11,400
Trade debtors	2,400	–
Trade creditors	–	1,700
Cash at bank	500	–
Cash in hand	100	–
	54,700	54,700

The following further information is given :

(1) Wages outstanding – $ 100.

(2) Depreciate Plant and Machinery and Furniture and Fixtures @ 10% p.a. on WDV.

(3) The Head Office sent goods to Branch for ₹ 3,94,000.

(4) The Head Office shows an amount of ₹ 4,30,000 due from Branch.

(5) Stock on 30th September, 2011 – $ 5,200.

(6) There were no in transit items either at the start or at the end of the year.

(7) On September 1, 2009, when the fixed assets were purchased, the rate of exchange was ₹ 38 to one $.

On October 1, 2010, the rate was ₹ 39 to one $.

On September 30, 2011, the rate was ₹ 41 to one $.

Average rate during the year was ₹ 40 to one $.

Prepare

(a) Trial balance incorporating adjustments given converting dollars into rupees.

(b) Trading and Profit and Loss Account for the year ended 30th September, 2011 and Balance Sheet as on that date depicting the profitability and net position of the Branch as would appear in the books of Indian company for the purpose of incorporating in the main Balance Sheet.

Partnership: Dissolution of a firm

14. X, Y and Z share profits and losses in the ratio of 5:3:2. Their firm was dissolved due to misconduct of Y and their balance sheet on that date was as under:

Balance Sheet as at 31-3-2011

Liabilities		₹	Assets	₹
Capital Accounts :			Land and Building	2,00,000
X	3,00,000		Plants	2,00,000
Y	2,00,000		Sundry Debtors	50,000
Z	1,00,000	6,00,000	Stock	1,50,000
Current Accounts:			Bills receivable:	50,000
X	50,000		Cash	1,00,000
Y	30,000	80,000	Current Account:	
Sundry Creditors		40,000	Z	50,000
Bills payable		80,000		
		8,00,000		8,00,000

The whole business of the firm was sold to Omega Limited, on that day on the following terms:

(i) Omega Limited will issue the following securities in consideration for transfer of business:

10,000 equity shares @ ₹15 each, 15,000 preference shares @ ₹15 each; and 20,000 debentures @ ₹ 14.725.

(ii) The agreed value of assets and liabilities of partnership firm are as follows:

Land & Building – ₹ 3,00,000, Plants – ₹ 1,50,000, Sundry Debtors – ₹ 47,500, Stock – ₹ 1,40,000, Bills Receivable – ₹ 50,000, Sundry Creditors – ₹ 38,000 and Bills Payable – ₹ 80,000.

It is mutually decided that preference shares and debentures will be distributed in profit sharing ratio and cash brought in by the partner (if any) will be shared equally by the remaining partners before distribution of equity shares. Equity shares are distributed on residual basis at the end.

Prepare the necessary accounts, to close the books of the firm.

Partnership: Amalgamation of Firms

15. M and N are partners of M & Co. sharing Profit and Losses in the ratio of 3:1 and N and A are partners of A & Co., sharing profits and losses in the ratio of 2:1. On 31st March, 2011, they decide to amalgamate and form a new firm M/s MNA & Co., wherein M, N and A would be partners sharing profits and losses in the ratio of 3:2:1. The Balance Sheets of two firms on the above date are as under:

Liabilities	*M & Co.* ₹	*A & Co.* ₹	*Assets*	*M & Co.* ₹	*A & Co.* ₹
Capitals:			Fixed assets:		
M	7,20,000	----	Building	1,50,000	1,80,000
N	4,80,000	6,00,000	Plant & machinery	4,50,000	4,80,000
A	----	3,00,000	Office equipment	60,000	18,000
Reserves	1,50,000	4,50,000	Current assets:		
Sundry creditors	3,60,000	3,48,000	Stock-in-trade	3,60,000	4,20,000
Due to M & Co.	----	3,00,000	Sundry debtors	4,80,000	6,00,000
Bank overdraft	2,40,000	-----	Bank balance	90,000	2,70,000
			Cash in hand	60,000	30,000
			Due from A & Co.	3,00,000	-
	19,50,000	19,98,000		19,50,000	19,98,000

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

(a) Plant and machinery of M & Co. was valued at ₹ 7,50,000 and that of A & Co. at ₹ 6,00,000.

(b) Building of M & Co. was valued at ₹ 3,00,000.

(c) Goodwill valued of M & Co. at ₹ 3,60,000 and A & Co. at ₹ 1,80,000, but the same will not appear in the books of MNA & Co.

(d) All stock in trade is to be appreciated by 20%.

(e) Partners of new firm will bring the necessary cash to pay other partners to adjust their capitals according to the profit sharing ratio.

(f) Provisions for doubtful debts has to be carried forward at ₹ 36,000 in respect of debtors of M & Co. and ₹ 78,000 in respect of debtors of A & Co.

You are required to prepare the Balance Sheet of new firm and capital accounts of the partners in the books of old firms.

Partnership: Conversion to a Company

16. Amol and Vinod, sharing profits and losses equally, directed to convert their business into a limited company on 31st December, 2011 when their balance sheet stood as follows:

Liabilities	₹	₹	*Assets*	₹
Sundry creditors		96,000	Sundry debtors	1,20,000
Loan creditors		80,000	Bills receivable	20,000
Bank overdraft		32,000	Stock in trade	72,000
Reserve fund		12,000	Patents	16,000
Capital accounts:			Plant and machinery	32,000
Amol	80,000		Land and building	1,20,000
Vinod	80,000	1,60,000		
		3,80,000		3,80,000

(a) The goodwill of the firm was to be valued at two years' purchase of the profits of the previous three years.

(b) The loan creditor was agreed to accept 7½% redeemable preference shares in settlement of his claim.

(c) Land and buildings and plant and machinery were to be valued at ₹2 00,000 and ₹ 48,000 respectively.

(d) The vendors were to be allotted equity shares of the value of ₹ 2,10,000.

(e) The past working results of the firm showed that they had made profits of ₹ 60,000 in 2009, ₹72,000 in 2010 and ₹84,000 in 2011 after setting aside ₹ 4,000 to reserve fund each year.

You are required to show realisation account and partners' capital accounts in the books of the firm assuming that all the transactions are duly completed.

AS-4

17. (a) You are an accountant preparing accounts of A Ltd. as on 31.3.2011. After year

end the following events have taken place in April, 2011:

(i) A fire broke out in the premises damaging, uninsured stock worth ₹ 10 lakhs (Salvage value ₹ 2 lakhs).

(ii) A suit against the company's advertisement was filed by a party claiming damage of ₹ 20 lakhs.

(iii) Dividend proposed @ 20% on share capital of ₹ 100 lakhs.

Describe, how above will be dealt with in the account of the company for the year ended on 31.3.2011.

(Hint: Para 14-16 of AS 4)

AS-5

(b) The company has to pay delayed cotton clearing charges over and above the negotiated price for taking delayed delivery of cotton from suppliers' godown. Upto 2009-10, the company has regularly included such charges in the valuation of closing stock. This being in the nature of interest the company has decided to exclude it from closing stock valuation for the year 2010-11. This would result into decrease in profit by ₹ 7.60 lakhs. State, how would you deal with the above in the annual accounts of a company for the year ended 31st March, 2011?

(Hint: Para 29 of AS 5)

AS-11

18. (a) Aman Ltd. borrowed US $ 5,00,000 on 31-12-2010 which will be repaid (settled) as on 30-6-2011. Aman Ltd. prepares its financial statements ending on 31-3-2011. Rate of exchange between reporting currency (Rupee) and foreign currency (US $) on different dates are as under:

31-12-2010	1 US $ = ₹ 44.00
31-3-2011	1 US $ = ₹ 44.50
30-6-2011	1 US $ = ₹ 44.75

(i) Calculate borrowings in reporting currency to be recognised in the books on above mentioned dates & also show journal entries for the same.

(ii) If borrowings was repaid (settled) on 28-2-2011 on which date exchange rate was 1 US$= ₹ 44.20 than what entry should be passed?

(Hint: Para 9, 11 & 13 of AS 11)

AS-12

(b) Viva Ltd. received a specific grant of ₹ 30 lakhs for acquiring the plant of ₹ 150 lakhs during 2007-08 having useful life of 10 years. The grant received was credited to deferred income in the balance sheet. During 2010-11, due to non-compliance of conditions laid down for the grant, the company had to refund the whole grant to the Government. Balance in the deferred income on that date was ₹ 21 lakhs and written down value of plant was ₹ 105 lakhs.

(i) What should be the treatment of the refund of the grant and the effect on cost of the fixed asset and the amount of depreciation to be charged during the year 2010-11 in profit and loss account?

(ii) What should be the treatment of the refund, if grant was deducted from the cost of the plant during 2007-08 assuming plant account showed the balance of ₹ 84 lakhs as on 1.4.2010?

(Hint: Para 21 of AS 21)

AS-16

(c) A company capitalizes interest cost of holding investments and adds to cost of investment every year, thereby understating interest cost in profit and loss account. Comment on the accounting treatment done by the company in context of the relevant AS.

(Hint: Para 2 & 3 of AS 16)

AS-19

19. (a) A Ltd. sold machinery having WDV of ₹ 40 lakhs to B Ltd. for ₹ 50 lakhs and the same machinery was leased back by B Ltd. to A Ltd. The lease back is operating lease.

Comment if –

(a) Sale price of ₹50 lakhs is equal to fair value.

(b) Fair value is ₹ 60 lakhs.

(c) Fair value is ₹ 45 lakhs and sale price is ₹ 38 lakhs.

(d) Fair value is ₹ 40 lakhs and sale price is ₹50 lakhs.

(e) Fair value is ₹46 lakhs and sale price is ₹ 50 lakhs

(f) Fair value is ₹35 lakhs and sale price is ₹39 lakhs.

(Hint: Para 50 of AS 19)

AS-20

(d) (i) Explain the concept of 'weighted average number of equity shares outstanding during the period'. State how would you compute, based on AS-20, the weighted average number of equity shares in the following case:

		No. of shares
1st April, 2010	Balance of equity shares	7,20,000
31st August, 2010	Equity shares issued for cash	2,40,000
1st February, 2011	Equity shares bought back	1,20,000
31st March, 2011	Balance of equity shares	8,40,000

(ii) Compute adjusted earning per share and basic EPS based on the following information:

Net profit 2009-10	₹ 7,20,000
Net profit 2010-11	₹ 24,00,000
No. of equity shares outstanding until 31st December, 2010	8,00,000

Bonus issue on 1st January, 2011, 2 equity shares for each equity share outstanding at 31st December, 2010.

(Hints: (i) Para 15 & 16 of AS 20; (ii) Para 44 of AS 20)

AS-26

20. (a) Hera Ltd. has got the license to manufacture particular medicines for 10 years at a license fee of ₹ 200 lakhs. Given below is the pattern of expected production and expected operating cash inflow:

Year	Production in bottles (in lakhs)	Net operating cash flow (₹ in lakhs)
1	300	900
2	600	1800
3	650	2300
4	800	3200
5	800	3200
6	800	3200
7	800	3200
8	800	3200
9	800	3200
10	800	3200

Net operating cash flow has increased for third year because of better inventory management and handling method. Suggest the amortization method.

(Hint: Para 72 of AS 26)

AS-29

(b) Shyam Ltd. (a Public Sector Company) provides consultancy and engineering services to its clients. In the year 2010-11, the Government has set up a commission to decide about the pay revision. The pay will be revised with respect from 1-1-2006 based on the recommendations of the commission. The company makes the provision of ₹ 680 lakhs for pay revision in the financial year 2010-11 on the estimated basis as the report of the commission is yet to come. As per the contracts with the client on cost plus job, the billing is done on the actual payment made to the employees and allocated to jobs based on hours booked by these employees on each job.

The company discloses through notes to accounts

"Salaries and benefits include the provision of ₹ 680 lakhs in respect of pay revision. The amount chargeable from reimbursable jobs will be billed as per the contract when the actual payment is made".

The accountant feels that the company should also book/recognise the income by ₹ 680 lakhs in Profit and Loss Account as per the terms of the contract. Otherwise, it will be the violation of matching concept & understatement of profit.

(Hint: Para 46 of AS 29)

SUGGESTED ANSWERS/HINTS

1. Fair value of an option = ₹ 56 – ₹ 50 = ₹ 6

Number of shares issued = 400 employees x 100 shares/employee = 40,000 shares

Fair value of ESPP = 40,000 shares x ₹ 6 = ₹ 2,40,000

Vesting period = 1 month

Expenses recognized in 2010-11 = ₹ 2,40,000

Date	*Particulars*		*₹*	*₹*
30.04.2010	Bank (40,000 shares x ₹ 50)	Dr.	20,00,000	
	Employees compensation expense A/c	Dr.	2,40,000	
	To Share Capital (40,000 shares x ₹10)			4,00,000
	To Securities Premium (40,000 shares x ₹ 46)			18,40,000
	(Being option accepted by 400 employees & payment made @ ₹ 56 share)			

2 (a) Journal of Kuber Ltd.

		(₹ in crores)	
		Dr.	*Cr.*
12% Redeemable preference share capital A/c	Dr.	75	
To Bank A/c			75
(Being redemption of 12% preference shares pursuant to capital re-organisation)			

Revenue reserves A/c	Dr.	75	
To Capital redemption reserve A/c			75
(Being amount equal to par value of preference shares redeemed out of profits, transferred to capital redemption reserve A/c)			
Equity share capital A/c	Dr.	5	
Revenue reserves A/c	Dr.	20	
To Bank A/c			25
(Being buy-back of 50 lakhs equity shares of ₹ 10 each from the members at a price of ₹ 50 per share, premium paid out of revenue reserves A/c)			
Revenue reserves A/c	Dr.	5	
To Capital redemption reserve A/c			5
(Being transfer to capital redemption reserve, as required by Section 77AA, on buy-back of equity shares out of revenue reserves)			

Kuber Ltd.

Balance Sheet (after reconstruction)

				(₹n crores)
		Schedule		
I	SOURCES OF FUNDS			
	(1) Shareholders' funds:			
	(a) Capital	A	20	
	(b) Reserves and surplus	B	280	
				300
	TOTAL			300
II	APPLICATION OF FUNDS			
	(1) Fixed assets			
	(a) Gross block		100	
	(b) *Less*: Depreciation		(100)	
	(c) Net block			-
	(2) Investments (market value : ₹ 400 crores)			100
	(3) Current assets (340 – 75 – 25)		240	
	Less: Current liabilities		(40)	
	Net current assets			200
	TOTAL			300

Schedules to Balance Sheet

			(₹ *in crores)*
A.	Share Capital		
	Authorised:		100
	Issued, Subscribed and Paid up:		
	200 lakhs equity shares of ₹ 10 each fully paid up		20
			20
	50 lakhs Equity Shares of ₹ 10 each have been bought back out of reserves at ₹ 50 per share also		
	12% 75 lakhs Redeemable Preference Shares of ₹ 100 each fully paid up, have been redeemed on 1st April, 2011		
B.	Reserves and surplus		
	(1) Capital reserve		15
	(2) Capital redemption reserve		
	As per last account	-	
	Add: Transfer from revenue reserves (75 + 5)	80	80
	(3) Securities premium		25
	(4) Revenue reserves		
	As per last account	260	
	Less: Transfer to capital redemption reserve	(80)	
		180	
	Less: Premium paid on buy-back	(20)	160
			280

Net asset value of an equity share

	(₹ *in crores)*
Investments (at market value)	400
Net current assets	200
Net assets available to equity shareholders	600
No. of equity shares = 2 crores	
Value of an equity share $= \frac{\text{600 crores}}{\text{2 crores}}$ = ₹ 300	

Note: In the absence of any other information, it has been assumed that shares have been bought back out of free reserves.

3. **Liability of Underwriters (No. of Shares)**

	Total	X	Y	Z	T
Gross Liability	10,00,000	3,00,000	3,00,000	2,00,000	2,00,000
Less: Unmarked Applications 700000 – 580000=	(1,20,000)	(36,000)	(36,000)	(24,000)	(24,000)
Balance	8,80,000	2,64,000	2,64,000	1,76,000	1,76,000
Less : Marked Application	(5,80,000)	(1,90,000)	(1,00,000)	(2,10,000)	(80,000)
Balance	3,00,000	74,000	1,64,000	(34,000)	96,000
Less: Firm Underwriting (A)	(70,000)	(30,000)	(20,000)	(10,000)	(10,000)
Balance	2,30,000	44,000	1,44,000	(44,000)	86,000
Adjustment (30: 30: 20)	-	(16,500)	(16,500)	44,000	(11,000)
Net Liability (B)	2,30,000	27,500	1,27,500	-	75,000
Total Liability including firm underwriting(A+B)	3,00,000	57,500	1,47,500	10,000	85,000

			₹
X	3,00,000 shares x ₹ 15 x 2.5%	=	1,12,500
Y	3,00,000 shares x ₹ 15 x 2.5%	=	1,12,500
Z	2,00,000 x ₹ 15 x 2.5%	=	75,000
T	2,00,000 x ₹ 15 x 2.5%	=	75,000
	Total	=	3,75,000

4. **12% Debentures Account**

Date	*Particulars*	₹	*Date*	*Particulars*	₹
31st March, 2011	To Own debentures A/c	4,00,000	1st April, 2010	By Balance b/d	32,00,000
	To Bank A/c	28,00,000			
		32,00,000			32,00,000

Debenture Redemption Sinking Fund Account

Date	*Particulars*	₹	*Date*	*Particulars*	₹
31st March, 2011	To 9% Stock A/c (loss) (W.N.5)	12,800	1st April, 2011	By Balance b/d	29,96,000
	To General reserve A/c (Bal.fig.)	33,86,400	31st March, 2011	By Profit and loss A/c	1,13,600

				By Interest on sinking fund A/c (W.N.3)	2,85,600
				By Own debentures A/c (W.N.4)	4,000
		33,99,200			33,99,200

Working Notes:

1. Investment in stock as on 1st April, 2010

	₹
Sinking fund balance as on 1st April, 2010	29,96,000
Less: Own debentures	(3,96,000)
	26,00,000

2. Sales value of 9% stock

= Face value / ₹ per stock = ₹ 26,40,000 / ₹ 100 = 26,400 stock

Sales value = 26,400 stock x ₹ 98 per stock = ₹ 25,87,200

3. Interest credited to Sinking Fund A/c

(i)	Interest on 9% stock (₹ 26,40,000 x 9%)	₹ 2,37,600
(ii)	Interest on own debentures (4,000 Debentures x ₹ 100 x 12%)	₹ 48,000
		₹ 2,85,600

4. Own debentures account

		₹			₹
1st April, 2010	To Balance b/d	396,000	31st March, 2011	By 12% Debentures A/c	4,00,000
31st March, 2011	To Sinking fund A/c	4,000			
		4,00,000			4,00,000

5. 9% Stock account

		₹			₹
1st April, 2010	To Balance b/d (Face value ₹ 26,40,000) (W.N.1)	26,00,000	31st March, 2011	By Bank account (W.N.2)	25,87,200

				By Sinking fund (loss on sales)	12,800
		26,00,000			26,00,000

5. (1) Computation of Amount of Debentures and Shares to be issued:

	Star	Moon
	₹	₹
(i) Average Net Profit		
$\frac{2,24,788 - 1,250 + 1,88,962}{3} =$	1,37,500	
$\frac{1,36,950 + 1,71,050 + 1,79,500}{3} =$		1,62,500
(ii) Equity Shares Issued		
(a) Ratio of distribution		
Star : Moon		
1,375 1,625		
(b) Number		
Star : 13,750		
Moon : 16,250		
30,000		
(c) Amount		
13,750 shares of ₹ 5 each =	68,750	
16,250 shares of ₹ 5 each =		81,250
(iii) Capital Employed (after revaluation of assets)		
Fixed Assets	3,55,000	1,95,000
Current Assets	1,49,750	78,875
	5,04,750	2,73,875
Less: Current Liabilities	2,98,500	90,125
	2,06,250	1,83,750
(iv) Debentures Issued		
8% Return on capital employed	16,500	14,700
15% Debentures to be issued to provide		

equivalent income :

Star : 16,500 × $\frac{100}{15}$ =	1,10,000	
Moon : 14,700 × $\frac{100}{15}$ =		98,000

(2) Balance Sheet of Neptune Ltd.

As at 31st December, 2011

Liabilities	*Amount*	*Assets*	*Amount*
	₹		₹
Share Capital:		Fixed Assets	5,50,000
Authorised		Current Assets	2,06,950
40,000 Equity Shares of ₹ 5 each	2,00,000		
Issued and Subscribed			
30,000 Equity Shares of ₹ 5 each	1,50,000		
(all the above shares are allotted as fully paid-up pursuant to a contract without payments being received in cash)			
Reserves and Surplus			
Capital Reserve	32,000		
Secured Loans			
15% Debentures	2,08,000		
Unsecured Loans	–		
Current Liabilities and Provisions			
Current Liabilities	3,66,950		
Provisions	–		
	7,56,950		7,56,950

Working Notes :

		Star	Moon	Total
		₹	₹	₹
(1)	Purchase Consideration			
	Equity Shares Issued	68,750	81,250	1,50,000
	15% Debentures Issued	1,10,000	98,000	2,08,000
		1,78,750	1,79,250	3,58,000
(2)	Capital Reserve			
	(a) Net Assets Taken Over			
	Fixed Assets	3,55,000	1,95,000	5,50,000
	Current Assets	1,49,750	57,200*	2,06,950
		5,04,750	2,52,200	7,56,950
	Less : Current Liabilities	2,76,825**	90,125	3,66,950
		2,27,925	1,62,075	3,90,000
	(b) Purchase Consideration	1,78,750	1,79,250	3,58,000
	(c) Capital Reserve [(a) - (b)]	49,175		
	(d) Goodwill [(b) - (a)]		17,175	
	(e) Capital Reserve [Final Figure(c) - (d)]			32,000

* 78,875 - 21,675

** 2,98,500 - 21,675

6. **Journal Entries in the books of Crystal Limited**

			Dr. (₹)	Cr. (₹)
1.	Equity share capital A/c (₹ 10)	Dr.	30,00,000	
	To Equity share capital A/c (₹ 3)			9,00,000
	To Capital reduction A/c			21,00,000
	(Reduction of equity share of ₹ 10 each to shares of ₹ 3 each as per the reconstruction scheme)			
2.	6% Preference share capital A/c (₹ 10)	Dr.	16,00,000	
	To 6% Preference share capital A/c (₹ 7)			11,20,000

	To Capital reduction A/c			4,80,000
	(Reduction of preference share of ₹ 10 each to shares of ₹ 7 each as per the reconstruction scheme)			
3.	6 % Debentures A/c	Dr.	15,00,000	
	To Land & building A/c			7,00,000
	To 9% Debentures A/c			7,50,000
	To Capital reduction A/c			50,000
	(50% claim of debentureholders discharged by transfer of a part of land & building having book value ₹ 7,00,000 and rate of interest of balance 50% debentures increased to 9% as per the reconstruction scheme).			
4.	Bank A/c	Dr.	6,00,000	
	To Land & building A/c			5,00,000
	To Capital reduction A/c			1,00,000
	(50% of balance land & building having book value ₹ 5,00,000 sold as per the reconstruction scheme)			
5.	Land & building A/c	Dr.	1,00,000	
	To Capital Reduction A/c			1,00,000
	(50% of balance land & building having book value ₹ 5,00,000, valued at ₹ 6,00,000, as per the reconstruction scheme)			
6.	Bank A/c	Dr.	2,00,000	
	Capital reduction A/c	Dr.	20,000	
	To Investment A/c			2,20,000
	(All the investment sold as per the reconstruction scheme)			
7.	Sundry creditors A/c	Dr.	4,00,000	
	To Capital reduction A/c			4,00,000
	(1/3 of sundry creditors decided to forgo their claim as per the reconstruction scheme)			
8.	Capital reduction A/c	Dr.	32,10,000	
	To Goodwill A/c			5,20,000

	To Patents A/c			1,50,000
	To Provision of doubtful debts A/c			1,74,000
	To Stock A/c			2,60,000
	To Bank A/c			50,000
	To Provision for income tax A/c			1,06,000
	To Profit & loss A/c			18,50,000
	To Plant & machinery A/c (Bal. fig.)			1,00,000
	(Written off goodwill, patent, profit & loss, part value of stock, plant & machinery, penalty paid for cancellation of contracts and provision made for doubtful debts, income tax, as per the reconstruction scheme)			

Balance Sheet of Crystal Ltd. (and reduced) as on 31.03.2011

Liabilities	₹	Assets		₹
3,00,000 Equity shares of ₹ 3 each fully paid up	9,00,000	Land & building (₹ 5,00,000 + ₹ 1,00,000)		6,00,000
1,60,000 6% Preference shares of ₹ 7 each fully paid up	11,20,000	Plant & machinery (₹ 2,00,000 – ₹ 1,00,000)		1,00,000
		Sundry Debtors	17,40,000	
9% Debenture (secured against land & building)	7,50,000	*Less*: Provision for doubtful debts	(1,74,000)	15,66,000
Sundry Creditors (₹ 12,00,000 – ₹4,00,000)	8,00,000	Stock (₹ 17,00,000 - ₹ 2,60,000) (Refer W.N.)		14,40,000
Provision for income tax (₹ 2,00,000 + ₹1,06,000)	3,06,000	Cash at bank		1,70,000
	38,76,000			38,76,000

Working Note:

Bank A/c

	₹		₹
To Land & building A/c	5,00,000	By Balance b/d	5,80,000
To Capital reduction A/c	1,00,000	By Capital reduction A/c	50,000
To Investment A/c	2,00,000	By Balance c/d	1,70,000
	8,00,000		8,00,000

7. **Liquidator's Final Statement of Receipts and Payments A/c**

	₹	₹		₹
To Cash in hand		40,000	By Liquidator's remuneration and expenses	5,000
To Assets realised:			By Trade creditors	3,50,000
Fixed assets	1,68,000		By Preference shareholders	1,00,000
Stock (1,10,000 – 1,00,000)	10,000		By Equity shareholders @ ₹ 10 on 2,000 shares	20,000
Book debts	2,30,000			
		4,08,000		
To Cash - proceeds of call on 1,800 equity shares @ ₹ 15		27,000		
		4,75,000		4,75,000

Working Note:

Return per equity share

	₹	₹	₹
Cash available before paying preference shareholders (₹ 4,48,000 – ₹ 3,55,000)	93,000		
Add: Notional calls 1,800 shares (2,000-200) × ₹ 25	45,000		
	1,38,000		
Less: Preference share capital	(1,00,000)		
Available for equity shareholders	38,000		
Return per share= $\frac{₹\ 38{,}000}{3{,}800\ (4{,}000 - 200)} = ₹\ 10$			
and Loss per Equity Share ₹ (100-10) = ₹ 90			

Calls to be made @ ₹ 15 per share (₹ 90-75) on 1,800 shares.

8. **Unexpired discount 31.12.2011 to be calculated as under:**

		₹
On ₹ 50,000 @ 5% for 31 days	$\left(50{,}000 \times \frac{5}{100} \times \frac{31}{366}\right)$	212
On ₹ 4,00,000 @ 5% for 121 days	$\left(4{,}00{,}000 \times \frac{5}{100} \times \frac{121}{366}\right)$	6,612

On ₹ 30,000 @ 5% for 63 days	$\left(30,000 \times \frac{5}{100} \times \frac{63}{366}\right)$	258
		7,082

Note:- Year 2012 is a leap year.

In the books of Unique Bank Ltd.
Journal Entries

Date	Particulars		Dr.	Cr.
			₹	₹
2011, 1 July	Interest and discount A/c	Dr.	7,082	
	To Rebate on bills discounted A/c			7,082
	(Proportionate discount on unexpired bills adjusted at the end of the year)			
Dec. 31	Customers' liability for acceptance A/c	Dr.	2,00,000	
	Customers' current A/c	Dr.	4,000	
	To B/P A/c (acceptance on behalf of customer)			2,000,00
	To Commission A/c			4,000
	(Bills accepted on customers' behalf and earned commission @ 2%)			
Dec. 31	Loans and advances A/c	Dr.	5,00,000	
	To Cash A/c			5,00,000
	(Amount advanced on security of bills and goods on key-loan basis)			

Treatment in Profit and Loss Account and Balance Sheet

(i) Discount earned (up to 31.12.2011) will be credited to 'P & L A/c' and unexpired discount of ₹ 7,082 will, be credited to 'Rebate on Bills Discounted A/c,' which will appear on the liability side of the Balance Sheet.

(ii) Commission earned will be credited to P & L A/c whereas customers' liability for acceptance will appear on the asset side of the Balance Sheet in Schedule (9) and Acceptance on behalf of customer will appear in the liability side in Schedule(5) as contra items, and

(iii) Loans and advances will appear in the assets side of the Balance Sheet.

9. Form B – RA (Prescribed by IRDA)

Great General Insurance Co. Ltd

Revenue Account for the year ended 31st March, 2011

Fire and Marine Insurance Businesses

	Schedule	*Fire Current Year*	*Marine Current Year*
		₹	₹
Premiums earned (net)	1	4,27,500	1,40,000
Interest, Dividends and Rent – Gross		—	—
Double Income Tax refund		—	—
Profit on sale of motor car		—	—
Total (A)		4,27,500	1,40,000
Claims incurred (net)	2	82,000	88,000
Commission	3	40,000	20,000
Operating expenses related to Insurance business	4	70,000	50,000
Bad debts		—	—
Indian and Foreign taxes		—	—
Total (B)		1,92,000	1,58,000
Profit from Marine Insurance business (A-B)		2,35,500	(18,000)

Schedules forming part of Revenue Account

Schedule –1

Premiums earned (net)	*Fire Current Year*	*Marine Current Year*
	₹	₹
Premiums from direct business written	4,80,000	3,50,000
Less: Premium on reinsurance ceded	(25,000)	(15,000)
Total Premium earned	4,55,000	3,35,000
Less: Change in provision for unexpired risk	(27,500)	(1,95,000)
	4,27,500	1,40,000
Schedule – 2		
Claims incurred (net)	82,000	88,000
Schedule – 4		
Operating expenses related to insurance business		
Expenses of Management	70,000	50,000

Form B-PL

Great General Insurance Co. Ltd.

Profit and Loss Account for the year 31st March, 2011

Particulars	*Schedule*	*Current Year*	*Previous Year*
		₹	₹
Operating Profit/(Loss)			
(a) Fire Insurance		2,35,500	
(b) Marine Insurance		(18,000)	
(c) Miscellaneous Insurance		—	
Income From Investments			
(a) Interest, Dividend & Rent–Gross		1,29,000	
(b) Profit on sale of investments			
Less : Loss on sale of investments			
Other Income (To be specified)			
Total (A)		3,46,500	
Provisions (Other than taxation)		—	
Depreciation		9,000	
Other Expenses –Director's Fee		80,000	
Total (B)		89,000	
Profit Before Tax		2,57,500	
Provision for Taxation		99,138	
Profit After Tax		1,58,362	

Working Notes:

		Fire	*Marine*
		₹	₹
1.	Claims under policies less reinsurance		
	Claims paid during the year	1,00,000	80,000
	Add: Outstanding on 31st March, 2011	10,000	15,000
		1,10,000	95,000
	Less : Outstanding on 1st April, 2010	(28,000)	(7,000)
		82,000	88,000

2.	Expenses of management		
	Expenses paid during the year	60,000	45,000
	Add: Outstanding on 31st March, 2011	10,000	5,000
		70,000	50,000
3.	Premiums less reinsurance		
	Premiums received during the year	4,50,000	3,30,000
	Add: Outstanding on 31st March, 2011	30,000	20,000
		4,80,000	3,50,000
	Less : Reinsurance premiums	(25,000)	(15,000)
		4,55,000	3,35,000

4. Reserve for unexpired risks is 50% of net premium for fire insurance and 100% of net premium for marine insurance.

5. Provision for taxation account

	₹		₹
31.3.2011 To Bank A/c (taxes paid)	60,000	1.4.2010 By Balance b/d	85,000
31.3.2011 To Balance c/d	1,24,138	31.3.2011 By P & L A/c	99,138
	1,84,138		1,84,138

10. Electric Supply Ltd.

Journal Entries

		Dr.	Cr.
		₹	₹
New Main Account	Dr.	20,95,000	
Replacement Account	Dr.	19,05,000	
To Bank Account			40,00,000
(Being current cost of replacement charged to replacement account and the balance amount capitalised)			
New Main Account	Dr.	2,00,000	
To Replacement Account			2,00,000
(Being the value of motors salvaged from old main used in the reconstruction of main)			
Bank Account	Dr.	70,000	
To Replacement Account			70,000
(Being the amount realised from sale of old materials credited to replacement account)			

Revenue Account	Dr.	16,35,000	
To Replacement Account			16,35,000
(Being the net current cost of replacement transferred to revenue account)			

Working Notes:

1. Current cost of replacement

	Cost of existing main	*Increase in cost*		*Current cost*
		Rate	*Amount*	
	₹		₹	₹
Materials (3/5 × ₹ 15 lacs)	9,00,000	25%	2,25,000	11,25,000
Labour (2/5 × ₹15 lacs)	6,00,000	30%	1,80,000	7,80,000
Estimated current cost for replacement of present main (amount to be charged to replacement account)				19,05,000

2. Additional cost of reconstruction of main (to be capitalised)

	₹
Cash cost of re-building new main	40,00,000
Less: Estimated current cost for replacement of existing old main	19,05,000
Additional cost in new main to be capitalised (excluding old motors used	20,95,000

3. Replacement Account

	₹		₹
To Bank A/c	19,05,000	By New Main A/c	2,00,000
		By Bank A/c	70,000
		By Replacement A/c	
		Balancing figure	16,35,000
	19,05,000		19,05,000

11. Calculation of Correct Profit

	Department L	*Department M*	*Department N*
	₹	₹	₹
Profit after charging managers' commission	1,08,000	81,000	54,000

Add back : Managers' commission (1/9)	12,000	9,000	6,000
	1,20,000	90,000	60,000
Less :Unrealised profit on stock (Working Note)	(12,000)	(13,500)	(6,000)
Profit before Manager's commission	1,08,000	76,500	54,000
Less :Commission for Department Manager @10%	(10,800)	(7,650)	(5,400)
Departmental net profit	97,200	68,850	48,600

Working Note :

Calculation of unrealised profit on stock

	Dept. L	*Dept. M*	*Dept N*	*Total*
	₹	₹	₹	₹
Department L		$\frac{25}{125}\times$ 45,000=9,000	$\frac{10}{110}\times$33,000 =3,000	12,000
Department M	42,000×15%=6,300		36,000×20% =7,200	13,500
Department N	$\frac{20}{120}\times$18,000 =3,000	$\frac{25}{125}$ x 15,000 =3,000		6,000

12. Branch Stock Account

Particulars	₹	*Particulars*	₹
To Balance b/d	12,000	By Cash A/c (Cash sales)	20,000
To Goods sent to Branch A/c	35,000	By Branch Debtors (credit sales)	21,000
To Branch Debtors (Sales Returns)	600	By Goods sent to Branch A/c (Returns)	1,000
		By Shortage of goods	400
		By Balance c/d (Bal. fig.)	5,200
	47,600		47,600

Branch Debtors Account

Particulars	₹	*Particulars*	₹
To Balance b/d	6,200	By Branch stock A/c (Sales Returns)	600
To Branch Stock (Credit sales)	21,000	By Cash A/c	19,800

		By Discount	300
		By Balance c/d (Bal. fig.)	6,500
	27,200		27,200

Branch Expenses Account

Particulars	₹	*Particulars*	₹
To Cash A/c	6,100	By Branch P/L A/c (Bal. fig.)	6,400
To Discount A/c	300		
	6,400		6,400

Goods Sent to Branch Account

Particulars	₹	*Particulars*	₹
To Branch Stock A/c (Returns)	1,000	By Branch Stock A/c	35,000
To Branch Adjustment A/c (Loading) (35,000× 30%)	10,500	By Branch Adj. A/c (Loading) (1,000 × 30%)	300
To Trading A/c (Bal. fig.)	23,800		
	35,000		35,000

Branch Adjustment Account

Particulars	₹	*Particulars*	₹
To Shortage of goods (Loading) (400 × 30%)	120	By Branch Stock Reserve (12,000 × 30%)	3,600
To Branch Stock Reserve A/c (5,200 × 30%)	1,560	By Goods sent to Branch (Net loading) (10,500 – 300)	10,200
To Gross profit transferred to P/L A/c (Bal. fig.)	12,120		
	13,800		13,800

Branch Profit and Loss Account

Particulars	₹	*Particulars*	₹
To Branch Expenses A/c	6,400	By Gross Profit transferred from Branch Adjustment A/c	12,120
To Shortage of Goods (cost) (400 × 70%)	280		
To Net Profit	5,440		
	12,120		12,120

13. (a) In the books of an Indian Company

Trial Balance (in Rupees) of New York Branch

as on 30th September, 2011

	Dr.	*Cr. .*	*Conversion*	*Dr.*	*Cr.*
	US $	*US $*	*rate*	*(₹ '000)*	*(₹ '000)*
Plant and Machinery	10,800		41	4,42,800	
Depreciation on plant and machinery	1,200		41	49,200	
Furniture and fixtures	720		41	29,520	
Depreciation on furniture and fixtures	80		41	3,280	
Stock, October, 1, 2010	5,600		39	2,18,400	
Purchases	24,000		40	9,60,000	
Sales		41,600	40		16,64,000
Goods from Indian Co. (H.O.)	8,000			3,94,000	
Wages (200 + 100)	300		40	12,000	
Outstanding wages		100	41		4,100
Carriage inward	100		40	4,000	
Salaries	600		40	24,000	
Rent, rates and taxes	200		40	8,000	
Insurance	100		40	4,000	
Trade expenses	100		40	4,000	
Head Office A/c		11,400			4,30,000
Trade debtors	2,400		41	98,400	
Trade creditors		1,700	41		69,700
Cash at bank	500		41	20,500	
Cash in hand	100		41	4,100	
Exchange gain (bal. fig.)					1,08,400
	54,800	54,800		22,76,200	22,76,200

(b) Trading and Profit and Loss Account of New York Branch
for the year ended 30th September, 2011

	₹		₹
To Opening stock	2,18,400	By Sales	16,64,000
To Purchases	9,60,000	By Closing stock	2,13,200
To Goods from Head Office	3,94,000	(52,00 US $ × 41)	
To Wages	12,000		
To Carriage inward	4,000		
To Gross profit c/d	2,88,800		
	18,77,200		18,77,200
To Salaries	24,000	By Gross profit b/d	2,88,800
To Rent, rates and taxes	8,000		
To Insurance	4,000		
To Trade expenses	4,000		
To Depreciation on plant and machinery	49,200		
To Depreciation on furniture and fixtures	3,280		
To Net Profit c/d	1,96,320		
	2,88,800		2,88,800

Balance Sheet of New York Branch
as on 30th September, 2011

Liabilities	₹	₹	*Assets*	₹	₹
Head Office A/c	4,30,000		Plant and machinery	4,92,000	
Add : Net profit	1,96,320	6,26,320	*Less* : Depreciation	49,200	4,42,800
Foreign currency			Furniture and fixtures	32,800	
Translation reserve		1,08,400	*Less* : Depreciation	3,280	29,520
Trade creditors		69,700	Closing stock		2,13,200
Outstanding wages		4,100	Trade debtors		98,400
			Cash in hand		4,100
			Cash at bank		20,500
		8,08,520			8,08,520

Note: The above solution has been given assuming that the New York branch is a non-integral foreign operation of the Indian Company.

14. Realisation A/c

	₹	₹		₹
To Land & Building		2,00,000	By Sundry Creditors	40,000
To Plant		2,00,000	By Bills Payable	80,000
To Sundry Debtors		50,000	By Omega Limited (W.N.1)	6,69,500
To Stock		1,50,000		
To Bill Receivable		50,000		
To Cash		1,00,000		
To Profit transferred to Capital A/c:				
X	19,750			
Y	11,850			
Z	7,900	39,500		
		7,89,500		7,89,500

Omega Limited

	₹		₹
To Realisation A/c	6,69,500	By Equity Shares in Omega Ltd. A/c	1,50,000
		By Preference Shares in Omega Ltd. A/c	2,25,000
		By Debentures in Omega Ltd.	2,94,500
	6,69,500		6,69,500

Equity Shares in Omega Ltd. A/c

	₹		₹
To Omega Limited	1,50,000	By X's Capital in Omega Ltd. A/c	87,000
		By Y's Capital A/c	63,000
	1,50,000		1,50,000

Preference Shares in Omega Ltd. A/c

	₹		₹
To Omega Limited	2,25,000	By X's Capital A/c	1,12,500
		By Y's Capital A/c	67,500
		By Z's Capital A/c	45,000
	2,25,000		2,25,000

Debenture in Omega Ltd. A/c

	₹		₹
To Omega Limited	2,94,500	By X's Capital A/c	1,47,250
		By Y's Capital A/c	88,350
		By Z's Capital A/c	58,900
	2,94,500		2,94,500

Cash A/c

	₹		₹
To Z's Capital A/c	46,000	By X's Capital A/c	23,000
		By Y's Capital A/c	23,000
	46,000		46,000

Partners' Current Accounts

	X ₹	Y ₹	Z ₹		X ₹	Y ₹	Z ₹
To Balance b/d	-		50,000	By Balance b/d	50,000	30,000	-
To X's Capital A/c	69,750			By Realisation A/c	19,750	11,850	7,900
To Y's Capital A/c		41,850		By Z's Capital A/c			42,100
	69,750	41,850	50,000		69,750	41,850	50,000

Partners' Capital Accounts

	X ₹	Y ₹	Z ₹		X ₹	Y ₹	Z ₹
To Z's Current A/c	-	-	42,100	By Balance b/d	3,00,000	2,00,000	1,00,000
To Preference Shares in Omega Ltd. A/c	1,12,500	67,500	45,000	By X's Current A/c	69,750		
To Debentures A/c	1,47,250	88,350	58,900	By Y's Current A/c		41,850	
To Cash A/c	23,000	23,000	-	By Cash A/c (bal. fig.)			46,000
To Equity Shares A/c	87,000	63,000	-				
	3,69,750	2,41,850	1,46,000		3,69,750	2,41,850	1,46,000

Working Notes:

1. Calculation of Purchase consideration

Net Payment Method

	₹
Equity Shares = 10,000 @ ₹ 15	1,50,000
Preference Shares = 15,000 @ ₹ 15	2,25,000
Debentures = 20,000 @ ₹ 14.725	2,94,500
	6,69,500

2. As whole business of the firm was sold to Omega Limited, cash balance of the firm ₹1,00,000 is also transferred to realisation account. Cash brought in by Z equal to Dr. balance appearing in his account, after distribution of preference shares and debentures in profit sharing ratio would be shared by X and Y equally. The balance amount payable to X and Y would be settled by transfer of equity shares in Omega Company.

15. Balance Sheet of M/s MNA & Co. as at 31st March, 2011

Liabilities		₹	*Assets*		₹
Capitals:			Building (₹3,00,000 + ₹ 1,80,000)		4,80,000
M	16,56,000		Plant & machinery (₹ 7,50,000+₹ 6,00,000)		13,50,000
N	11,04,000		Office equipment (₹ 60,000+₹ 18,000)		78,000
A	5,52,000	33,12,000	Stock-in-trade (₹ 4,32,000+₹ 5,04,000)		9,36,000
Sundry creditors (₹3,60,000+3,48,000)		7,08,000	Sundry debtors (₹4,80,000+₹ 6,00,000)	10,80,000	
Bank overdraft		2,40,000	*Less:* Provision for doubtful debts (₹ 36,000+₹ 78,000)	(1,14,000)	9,66,000
			Bank balance (₹90,000+₹2,70,000)		3,60,000
			Cash in hand		90,000*
		42,60,000			42,60,000

* ₹ 60,000+₹ 30,000+₹ 4,59,000+₹ 90,000 –₹ 5,49,000 = ₹ 90,000.

In the books of M & Co.

Partners' Capital Accounts

	Particulars	M ₹	N ₹		Particulars	M ₹	N ₹
To	Capital A/cs – M/s MNA & Co.	14,67,000	7,29,000	By	Balance b/d	7,20,000	4,80,000
				By	Reserve (3:1)	1,12,500	37,500
				By	Profit on Realisation A/c (W.N.4)	6,34,500	2,11,500
		14,67,000	7,29,000			14,67,000	7,29,000

In the books of A & Co.

Partners' Capital Accounts

	Particulars	N ₹	A ₹		Particulars	N ₹	A ₹
To	Capital A/cs – M/s MNA & Co.	11,04,000	5,52,000	By	Balance b/d	6,00,000	3,00,000
				By	Reserve (2:1)	3,00,000	1,50,000
				By	Profit on Realisation (W.N.5)	2,04,000	1,02,000
		11,04,000	5,52,000			11,04,000	5,52,000

Working Notes:

1. Computation of purchase considerations

	M & Co. ₹	A& Co. ₹
Assets:		
Goodwill	3,60,000	1,80,000
Building	3,00,000	1,80,000
Plant & machinery	7,50,000	6,00,000
Office equipment	60,000	18,000
Stock-in-trade	4,32,000	5,04,000
Sundry debtors	4,80,000	6,00,000
Bank balance	90,000	2,70,000
Cash in hand	60,000	30,000

	Due from A & Co.		3,00,000	-
		(A)	28,32,000	23,82,000
Less:	*Liabilities:*			
	Creditors		3,60,000	3,48,000
	Provision for doubtful debts		36,000	78,000
	Due to M & Co.		-	3,00,000
	Bank overdraft		2,40,000	-
		(B)	6,36,000	7,26,000
Purchase consideration (A-B)			21,96,000	16,56,000

2. Computation of proportionate capital

	₹
M/s MNA& Co. (Purchase Consideration) (₹ 21,96,000+ ₹ 16,56,000)	38,52,000
Less: Goodwill adjustment	(5,40,000)
Total capital of new firm (Distributed in ratio 3:2:1)	33,12,000
M's proportionate capital	16,56,000
N's proportionate capital	11,04,000
A's proportionate capital	5,52,000

3. Computation of Capital Adjustments

	M	*N*	*A*	*Total*
	₹	₹	₹	₹
Balance transferred from M & Co.	14,67,000	7,29,000		21,96,000
Balance transferred from A & Co.		11,04,000	5,52,000	16,56,000
	14,67,000	18,33,000	5,52,000	38,52,000
Less: Goodwill written off in the ratio of 3:2:1	(2,70,000)	(1,80,000)	(90,000)	(5,40,000)
Existing capital	11,97,000	16,53,000	4,62,000	33,12,000
Proportionate capital	16,56,000	11,04,000	5,52,000	33,12,000
Amount to be brought in (paid off)	4,59,000	(5,49,000)	90,000	

4. In the books of M & Co.

Realisation Account

	₹		₹
To Building	1,50,000	By Creditors	3,60,000
To Plant & machinery	4,50,000	By Bank overdraft	2,40,000
To Office equipment	60,000	By M/s MNA & Co.	21,96,000

To Stock-in-trade	3,60,000	(purchase consideration)	
To Sundry debtors	4,80,000	(W.N.1)	
To Bank balance	90,000		
To Cash in hand	60,000		
To Due from A & Co.	3,00,000		
To Partners' capital A/cs			
M 6,34,500			
N 2,11,500	8,46,000		
	27,96,000		27,96,000

5. In the books of A & Co.

Realisation Account

	₹		₹
To Building	1,80,000	By Creditors	3,48,000
To Plant & machinery	4,80,000	By Due to M & Co.	3,00,000
To Office equipment	18,000	By M/s MNA & Co.	16,56,000
To Stock-in-trade	4,20,000	(purchase consideration)	
To Sundry debtors	6,00,000	(W.N.1)	
To Bank balance	2,70,000		
To Cash in hand	30,000		
To Partners' capital A/cs			
N 2,04,000			
A 1,02,000	3,06,000		
	23,04,000		23,04,000

16. Books of Amol and Vinod

Realisation Account

	₹	₹		₹
To Sundry debtors		1,20,000	By Sundry creditors	96,000
To Bills receivable		20,000	By Loan creditors	80,000
To Stock in trade		72,000	By Bank overdraft	32,000
To Patents		16,000	By Purchasing Company	4,20,000
To Plant and Machinery		32,000	(W.N. 2)	
To Land and Building		1,20,000		
To Capital A/c (Profit)				
Amol	1,24,000			
Vinod	1,24,000	2,48,000		
		6,28,000		6,28,000

Partners' Capital Accounts

	Amol	Vinod		Amol	Vinod
	₹	₹		₹	₹
To Shares in Purchasing Co.	2,10,000	2,10,000	By Balance b/d	80,000	80,000
			By Reserves	6,000	6,000
			By Realizations	1,24,000	1,24,000
	2,10,000	2,10,000		2,10,000	2,10,000

Working Notes

1. Goodwill = $\frac{60,000+72,000+84,000+12,000^*}{3} \times 2\text{years} = 1,52,000$

   * Profit transferred to reserve @ ₹ 4,000 for 3 years.

2. Purchase Consideration

	₹	₹
Assets taken over:		
Goodwill (W.N.1)		1,52,000
Land and Buildings		2,00,000
Machinery		48,000
Debtors		1,20,000
Bills Receivable		20,000
Stocks		72,000
Patents		16,000
		6,28,000
Less: Liabilities taken over:		
Creditors	96,000	
Loan Creditors	80,000	
Bank Overdraft	32,000	2,08,000
Purchase Consideration		4,20,000

17. (a) Events occurring after the Balance Sheet date that represent material changes and commitments affecting the financial position of the enterprise must be disclosed according to para 15 of AS 4 on Contingencies and Events occurring after the Balance Sheet date. Hence, fire accident and loss thereof must be disclosed.

Suit filed against the company being a contingent liability must be disclosed with the nature of contingency, an estimate of the financial effect and uncertainties which may affect the future outcome must be disclosed as per para 16 of AS 4.

There are events which, although take place after the balance sheet date, are sometimes reflected in the financial statements because of statutory requirements or because of their special nature. Such items include the amount of dividend proposed or declared by the enterprise after the balance sheet date in respect of the period covered by the financial statements. Thus, dividends which are proposed or declared by the enterprise after the balance sheet date but before approval of the financial statements, should be adjusted as per para 14 of AS 4.

(b) Para 29 of AS 5 (Revised), 'Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies", states that a change in an accounting policy should be 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 presentation of the financial statements of an enterprise. Therefore, the change in the method of stock valuation is justified in view of the fact that the change is in line with the recommendations of AS 2 (Revised) 'Valuation of Inventories' and would result in more appropriate preparation of the financial statements. As per AS 2, this accounting policy adopted for valuation of inventories including the cost formulae used should be disclosed in the financial statements.

Also, appropriate disclosure of the change and the amount by which any item in the financial statements is affected by such change is necessary as per AS 1, AS 2 and AS 5. Therefore, the under mentioned note should be given in the annual accounts.

"In compliance with the Accounting Standards issued by the ICAI, delayed cotton clearing charges which are in the nature of interest have been excluded from the valuation of closing stock unlike preceding years. Had the company continued the accounting practice followed earlier, the value of closing stock as well as profit before tax for the year would have been higher by ₹ 7.60 lakhs."

18. (a) (i) As per para 9 of AS 11 "Changes in Foreign Exchange Rates", a foreign currency transaction should be recorded, on initial recognition in the reporting currency, by applying to the foreign currency amount the exchange rate between the reporting currency and the foreign currency at the date of the transaction. Accordingly, on 31.12.2010, borrowings will be recorded at ₹ 2,20,00,000 (i.e $ 5,00,000 × ₹ 44.00)

As per para 11(a) of the standard, at each balance sheet date, foreign currency monetary items should be reported using the closing rate. Accordingly, on 31.12.2011, borrowings (monetary items) will be recorded at ₹ 2,22,50,000 (i.e $ 5,00,000 × ₹ 44.50).

In the books of Aman Ltd.

Journal Entries

	Date	Particulars		₹	₹
1.	31-12-2010	Bank A/c	Dr.	2,20,00,000	
		To Borrowings			2,20,00,000
2.	31.03.2011	P/L A/c (Difference in exchange) (W.N.1)	Dr.	2,50,000	
		To Borrowings			2,50,000
3.	30.06.2011	Borrowings A/c	Dr.	2,22,50,000	
		P/L A/c (Difference in exchange) (W.N.2)	Dr.	1,25,000	
		To Bank A/c			2,23,75,000

(ii) In case borrowings is repaid before balance sheet date, then the entry would be as follows:-

28-2-2011	Borrowings A/c	Dr.	2,20,00,000	
	P/L A/c (Difference in exchange) (W.N.3)	Dr.	1,00,000	
	To Bank A/c			2,21,00,000

Working Notes:

1. The exchange difference of ₹ 2,50,000 is arising because the transaction has been reported at different rate (₹ 44.50 =1 US $) from the rate initially recorded (i.e. ₹ 44 =1 US $).

2. The exchange difference of ₹ 1,25,000 is arising because the transaction has been settled at an exchange rate (₹ 44.75 =1 US $) different from the rate at which reported in the last financial statement (₹ 44.50= 1 US $).

3. The exchange difference of ₹ 1,00,000 is arising because the transaction has been settled at a different rate (i.e. ₹ 44.20 = 1 US $) than the rate at which initially recorded (1 US $ = ₹ 44.00).

(b) As per para 21 of AS-12, 'Accounting for Government Grants', "the amount refundable in respect of a grant related to specific fixed asset should be recorded by reducing the deferred income balance. To the extent the amount refundable exceeds any such deferred credit, the amount should be charged to profit and loss statement.

(i) In this case the grant refunded is ₹ 30 lakhs and balance in deferred income is ₹ 21 lakhs, ₹ 9 lakhs shall be charged to the profit and loss account for the year 2010-11. There will be no effect on the cost of the fixed asset and depreciation charged will be on the same basis as charged in the earlier years.

(ii) If the grant was deducted from the cost of the plant in the year 2007-08 then, para 21 of AS-12 states that the amount refundable in respect of grant which relates to specific fixed assets should be recorded by increasing the book value of the assets, by the amount refundable. Where the book value of the asset is increased, depreciation on the revised book value should be provided prospectively over the residual useful life of the asset. Therefore, in this case, the book value of the plant shall be increased by ₹ 30 lakhs. The increased cost of ₹ 30 lakhs of the plant should be amortized over 7 years (residual life). Depreciation charged during the year 2010-11 shall be (84 + 30)/7 years = ₹ 16.286 lakhs presuming the depreciation is charged on SLM.

(c) The Accounting Standard Board (ASB) has opinioned that investments other than investment properties are not qualifying assets as per AS-16 Borrowing Costs. Therefore, interest cost of holding such investments cannot be capitalized. Further, even interest in respect of investment properties can only be capitalized if such properties meet the definition of qualifying asset, namely, that it necessarily takes a substantial period of time to get ready for its intended use or sale. Also, where the investment properties meet the definition of 'qualifying asset', for the capitalization of borrowing costs, the other requirements of the standard such as that borrowing costs should be directly attributable to the acquisition or construction of the investment property and suspension of capitalization as per paragraphs 17 and 18 of AS-16 have to be complied with.

19. (a) As per para 50 of AS 19 "Leases", if a sale and leaseback transaction results in an 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.

Accordingly, following will be the treatment in the given cases:

(a) When sales price of ₹ 50 lakhs is equal to fair value, A Ltd. should immediately recognize the profit of ₹10 lakhs (i.e. 50 – 40) in its books.

(b) When fair value is ₹ 60 lakhs then also profit of ₹10 lakhs should be immediately recognized by A Ltd.

(c) When fair value of leased machinery is ₹ 45 lakhs & sales price is ₹ 38 lakhs, then loss of ₹ 2 lakhs (40 – 38) to be immediately recognized by A Ltd. in its books provided loss is not compensated by future lease payment.

(d) When fair value is ₹ 40 lakhs & sales price is ₹ 50 lakhs then, profit of ₹ 10 lakhs is to be deferred and amortized over the lease period.

(e) When fair value is ₹ 46 lakhs & sales price is ₹ 50 lakhs, profit of ₹ 6 lakhs (46 - 40) to be immediately recognized in its books and balance profit of ₹4 lakhs (50-46) is to be amortised/deferred over lease period.

(f) When fair value is ₹ 35 lakhs & sales price is ₹ 39 lakhs, then the loss of ₹5 lakhs (40-35) to be immediately recognized by A Ltd. in its books and profit of ₹ 4 lakhs (39-35) should be amortised/deferred over lease period.

(b) (i) As per para 16 of AS 20, "Earnings Per Share", the weighted average number of equity shares outstanding during the period reflects the fact that the amount of shareholders' capital may have varied during the period as a result of a larger or less number of shares outstanding at any time. For the purpose of calculating basic earnings per share, the number of equity shares should be the weighted average number of equity shares outstanding during the period.

Weighted average number of equity shares

7,20,000 X 5/12	= 3,00,000 shares
9,60,000 X 5/12	= 4,00,000 shares
8,40,000 X 2/12	= 1,40,000 shares
	= 8,40,000 shares

(ii) Equity per share

Basic EPS 2010-11 = ₹ 24,00,000/24,00,000 = ₹ 1

Adjusted EPS 2009-10 = ₹ 7,20,000/24,00,000 = ₹ 0.30

Since the bonus issue is an issue without consideration, the issue is treated as if it had occurred prior to the beginning of the year 2009-10, the earliest period reported.

20. (a) As per para 72 of AS 26 'Intangibles Assets', the amortization method used should reflect the pattern in which economic benefits are consumed by the enterprise. If pattern cannot be determined reliably, then straight-line method should be used.

In the instant case, the pattern of economic benefit in the form of net operating cash flow vis-à-vis production is determined reliably. Initially net operating cash flow per thousand bottles is ₹ 3 lakhs for first two years and ₹ 4 lakhs from fourth year onwards, the pattern is established. Therefore Hera Ltd. should amortize the license fee of ₹ 200 lakhs as under:

Year	Net operating Cash in flow	Ratio	Amortize amount (₹ in lakhs)
1	900	0.03	6
2	1,800	0.06	12
3	2,300	0.08	16
4	3,200	0.12	24
5	3,200	0.12	24
6	3,200	0.12	24
7	3,200	0.12	24
8	3,200	0.12	24
9	3,200	0.12	24
10	3,200	0.11 (bal.)	22
	27,400	1.00	200

(b) As per para 46 of AS-29, 'Provisions, Contingent Liabilities and Contingent Assets', where some or all of the expenditure required to settle a provision is expected to be reimbursed by another party, the reimbursement should be recognised when, and only when, it is virtually certain that reimbursement will be received if the enterprise settles the obligation. The reimbursement should be treated as a separate asset. The amount recognised for the reimbursement should not exceed the amount of the provision.

Accordingly, potential loss to an enterprise may be reduced or avoided because a contingent liability is matched by a related counter-claim or claim against a third party. In such cases, the amount of the provision is determined after taking into account the probable recovery under the claim if no significant uncertainty as to its measurability or collectability exists.

In this case, the provision of salary to employees of ₹ 680 lakhs will be ultimately collected from the client, as per the terms of the contract. Therefore, the liability of ₹ 680 lakhs is matched by the counter claim from the client. Hence, the provision for salary of employees should be made reducing the claim to be made from the client. It appears that the whole amount of ₹ 680 lakhs is recoverable from client and there is no significant uncertainty about the collection. Hence, the net charge to profit and loss account should be nil.

The opinion of the accountant regarding non-recognition of income of ₹ 680 lakhs is not as per AS-29 and AS-9. However, the concept of prudence will not be followed if ₹ 680 lakhs is simultaneously recognized as income. ₹ 680 lakhs is not the revenue at present but only reimbursement of claim. However the accountant is correct to the extent as that non- recognition of ₹ 680 lakhs as income will result in the under statement of profit.