

PAPER – 1 : ACCOUNTING

Answer all questions.

Wherever appropriate, suitable assumptions should be made by the candidates.

Working notes should form part of the answer.

Question 1

Following incomplete information of X Ltd. are given below:

Trading and Profit & Loss Account for the year ended 31st March, 2008

	Rs.'000		Rs.'000
To Opening stock	700	By Sales	?
To Purchases	?	By Closing stock	?
To Direct expenses	175		
To Gross profit c/d	<u>?</u>		
	<u>?</u>		<u>?</u>
To Establishment expenses	740	By Gross profit b/d	?
To Interest on loan	60	By Commission	100
To Provision for taxation	?		
To Net profit c/d	<u>?</u>		
	<u>?</u>		<u>?</u>
To Proposed dividends	?	By Balance b/f	140
To Transfer to general reserve	?	By Net profit b/d	?
To Balance transferred to Balance sheet	<u>?</u>		
	<u>?</u>		<u>?</u>

Balance Sheet as at 31st March, 2008

Liabilities	Amount (Rs.'000)	Assets	Amount (Rs.'000)
Paid-up capital	1,000	Fixed assets:	
General reserve:		Plant & machinery	1,400
Balance at the beginning of the year	?	Other fixed assets	?
Proposed addition	?	Current assets:	
Profit and loss account	?	Stock	?
10% Loan account	?	Sundry debtors	?
Current liabilities	<u>?</u>	Cash at bank	<u>125</u>
	<u>?</u>		<u>?</u>

Other information:

- (i) Current ratio is 2:1.
- (ii) Closing stock is 25% of sales.
- (iii) Proposed dividends to paid-up capital ratio is 2:3.
- (iv) Gross profit ratio is 60% of turnover.
- (v) Loan is half of current liabilities.
- (vi) Transfer to general reserves to proposed dividends ratio is 1:1.
- (vii) Profit carried forward is 10% of proposed dividends.
- (viii) Provision for taxation is equal to the amount of net profit of the year.
- (ix) Balance to credit of general reserve at the beginning of the year is twice the amount transferred to that account from the current year's profits.

All working notes should be part of your answer. You are required to complete:

- (i) Trading and Profit and Loss account for the year ended 31st March, 2008 and
- (ii) The Balance Sheet as on that date. (20 Marks)

Answer

Trading and Profit & Loss A/c
for the year ended 31st March, 2008

	(Rs. in '000s)				(Rs. in '000s)
To Opening stock	700.00	By	Sales (W.N.10)		5366.66
To Purchases (Bal. Fig.)	2613.33	By	Closing stock (W.N.11)		1341.67
To Direct expenses	175.00				
To Gross profit c/d (W.N.9)	<u>3,220.00</u>				
	<u>6,708.33</u>				<u>6,708.33</u>
To Establishment expenses	740.00	By	Gross profit b/d (Bal. Fig.)		3,220.00
To Interest on loan	60.00	By	Commission		100.00
To Provision for tax (W.N.8)	1,260.00				
To Net profit c/d	<u>1,260.00</u>				
	<u>3,320.00</u>				<u>3,320.00</u>
To Proposed dividends (W.N.1)	666.67	By	Balance b/f		140.00
To Transfer to general reserve (W.N.2)	666.67	By	Net profit b/d (Bal. Fig.)		1,260.00

To	Balance transferred to Balance sheet (W.N.3)	<u>66.66</u>	
		<u>1,400.00</u>	<u>1,400.00</u>

Balance Sheet as at 31st March, 2008

Liabilities	(Rs. in '000s)	Assets	(Rs. in '000s)
Paid-up capital	1,000.00	Fixed assets:	
General reserve:		Plant & machinery	1,400.00
Balance at the beginning (W.N.14)	1333.34	Other fixed assets (Bal. Fig.)	1066.67
Proposed addition (W.N.2)	666.67	Current Assets:	
Profit and loss A/c	66.66	Stock (W.N.11)	1341.67
10% Loan A/c (W.N.4)	600.00	Sundry debtors (W.N.13)	933.33
Current liabilities (W.N.5)	<u>1,200.00</u>	Cash at bank	<u>125.00</u>
	<u>4,866.67</u>		<u>4,866.67</u>

Working Notes:

- Proposed dividend to paid up capital is 2:3.
i.e. Proposed dividend = $\frac{2}{3}$ of paid up capital
= Rs.1,000.00 thousand $\times \frac{2}{3}$ = Rs. 666.67 thousand
- Transfer to General Reserve is equal to proposed dividend i.e., 1:1.
Proposed dividend is Rs.666.67 thousand,
therefore general reserve is also Rs. 666.67 thousand.
- Profit carried forward to Balance Sheet = 10% of Proposed Dividend
i.e., Rs. 666.67 thousand \times 10% = Rs.66.66 thousand
- 10% Loan implies interest on loan being 10%
i.e. Rs.60.00 thousand $\times \frac{100}{10}$ = Rs.600.00 thousand
- Loan is half of current liabilities which means current liabilities are twice of loan
i.e., Rs.600.00 thousand \times 2 = Rs.1,200.00 thousand
- Current Ratio i.e., $\frac{\text{Current Assets}}{\text{Current Liabilities}} = 2:1$ or $\frac{2}{1}$
i.e. Current Assets = 2 x Current Liabilities
or 2 x Rs.1,200.00 thousand = Rs.2,400.00 thousand

4 **PROFESSIONAL EXAMINATION (COURSE – II) : MAY, 2008**

7. Current Net Profit	(Rs. in '000s)
Proposed dividend	666.67
Transfer to general reserve	666.67
Profit and loss balance transferred to balance sheet	<u>66.66</u>
	1,400.00
Less: Balance b/f	<u>140.00</u>
Net profit for the year	<u>1,260.00</u>

8. Provision for taxation is equal to current net profit i.e., = Rs.1,260.00 thousand
9. Gross profit being balancing figure of Profit and Loss A/c = Rs.3,220.00 thousand
10. Gross profit = 60% of sales i.e.
Rs.3,220.00 thousand = 60% of sales
- Or, sales = Rs.3,220 thousand $\times \frac{100}{60}$ = Rs. 5,366.67 thousand
11. Closing stock is 25% of sales i.e., 25% of Rs. 5,366.67 thousand = Rs.1,341.67 thousand
12. Purchases being balancing figure of Trading A/c = Rs.2,613.33 thousand
13. Debtors = Current Assets – Closing Stock – Cash at Bank
= Rs.2,400.00 thousand – Rs.1,341.67 thousand – Rs.125.00 thousand
= Rs.933.33 thousand
14. Balance of general reserve at the beginning of the year is twice of the amount transferred to general reserve during the year i.e. 2 x Rs.666.67 thousand = Rs.1,333.34 thousand
15. Other fixed assets = Total of balance sheet (liabilities side)- Current assets – Plant and machinery
i.e., Rs.4,866.67 thousand - Rs.2,400.00 thousand – Rs.1,400.00 thousand
= Rs.1,066.67 thousand

Question 2

The Balance Sheet of A Limited and B Limited as at 31st March, 2008 are as follows:

Liabilities	A Ltd.	B Ltd.	Assets	A Ltd.	B Ltd.
Equity share of Rs.10 each	20,00,000	12,00,000	Sundry assets	30,00,000	14,00,000
General reserve	4,00,000	2,20,000	40,000 Equity shares in A Ltd.	-	4,00,000
Creditors	<u>6,00,000</u>	<u>3,80,000</u>		<u>30,00,000</u>	<u>18,00,000</u>
	<u>30,00,000</u>	<u>18,00,000</u>			

A Ltd. absorbed B Ltd. on the basis of intrinsic value of the shares. The purchase consideration is to be discharged in fully paid-up equity shares. A sum of Rs.1,00,000 is owed by A Ltd. to B Ltd., also included in the stock of A Ltd. is Rs.1,20,000 goods supplied by B Ltd. at cost plus 20%.

Give Journal entries in the books of both the companies, if entries are made at intrinsic value. Also prepare Balance Sheet of A Ltd. after absorption. (16 Marks)

Answer

In the Books of B Ltd.

Journal Entries

		Dr. (Rs.)	Cr. (Rs.)
(i)	Realisation A/c	Dr. 14,00,000	
	To Sundry assets A/c		14,00,000
	(Being assets transferred to realization account on sale of business to A Ltd.)		
<hr/>			
(ii)	Creditors A/c	Dr. 3,80,000	
	To Realisation A/c		3,80,000
	(Being creditors transferred to realization account on sale of business to A Ltd.)		
<hr/>			
(iii)	Equity share capital A/c	Dr. 12,00,000	
	General reserve A/c	Dr. 2,20,000	
	To Equity shareholders A/c		14,20,000
	(Being transfer of share capital and general reserve to shareholders account)		
<hr/>			
(iv)	A Ltd.	Dr. 10,20,000	
	To Realisation A/c		10,20,000
	(Being purchase consideration due – W.N. 2)		
<hr/>			
(v)	Equity shares in A Ltd.	Dr. 10,20,000	
	To A Ltd.		10,20,000
	(Being purchase consideration received by A Ltd.)		
<hr/>			

6 PROFESSIONAL EXAMINATION (COURSE – II) : MAY, 2008

(vi)	Equity shares in A Ltd. A/c To Realisation A/c (Being appreciation in the value of shares of A Ltd. brought into books as entries are to be made at intrinsic value)	Dr. 80,000	80,000
<hr/>			
(vii)	Realisation A/c To Equity shareholders A/c (Being profit on realization transferred to shareholders account)	Dr. 80,000	80,000
<hr/>			
(viii)	Equity shareholders A/c To Equity shares in A Ltd. A/c (Being 85,000+ 40,000 = 1,25,000 shares distributed to equity shareholders of B Ltd.)	Dr. 15,00,000	15,00,000

In the Books of A Ltd.
Journal Entries

		Dr. (Rs.)	Cr. (Rs.)
(i)	Business purchase A/c To Liquidators of B Ltd. A/c (Being amount payable to B Ltd. – W.N. 2)	Dr. 10,20,000	10,20,000
<hr/>			
(ii)	Sundry assets A/c To Creditors A/c To Business purchase A/c (Being assets & liabilities taken over and purchase consideration due)	Dr. 14,00,000	3,80,000 10,20,000
<hr/>			
(iii)	Liquidators of B Ltd. A/c To Equity share capital A/c To Securities premium A/c (Being shares allotted in full payment of purchase consideration)	Dr. 10,20,000	8,50,000 1,70,000

(iv)	Creditors A/c	Dr.	1,00,000	
	To Debtors (of B Ltd.) A/c			1,00,000
	(Being cancellation of mutual liability of debtors & creditors of Rs.1,00,000)			
<hr/>				
(v)	General reserve A/c	Dr.	20,000*	
	To Stock A/c			20,000
	(Being elimination of unrealized profit on unsold stock of Rs.1,20,000, bought from B Ltd.)			
<hr/>				

*Unrealized profit = Rs.1,20,000 × 20/120 = Rs.20,000.

Balance Sheet of A Ltd.
as at 31st March, 2008

Liabilities	Rs.	Assets	Rs.
Share capital:		Sundry assets	42,80,000
2,85,000 Equity shares of Rs.10 each	28,50,000	(30,00,000 + 14,00,000 – 1,00,000 – 20,000)	
(of the above, 85,000 equity shares of Rs.10 each are issued for consideration other than cash)			
Securities premium	1,70,000		
General reserve	3,80,000		
Creditors	8,80,000		
(6,00,000 + 3,80,000- 1,00,000)			
	<u>42,80,000</u>		<u>42,80,000</u>

Working Notes:

1. Calculation of Intrinsic Value of shares of 'A' Ltd.

	Rs.
Sundry assets of A Ltd.	30,00,000
Less: Creditors	<u>6,00,000</u>
Net assets	<u>24,00,000</u>
Number of equity shares	2,00,000 shares
Intrinsic value per equity share = $\frac{\text{Rs.24,00,000}}{2,00,000 \text{ shares}}$	Rs. 12 per share

8 **PROFESSIONAL EXAMINATION (COURSE – II) : MAY, 2008**

2. Calculation of Purchase Consideration	Rs.
Sundry assets of B Ltd.	14,00,000
Add: Investments in shares of A Ltd. (40,000 shares × Rs.12)	<u>4,80,000</u>
	18,80,000
Less: Creditors	<u>3,80,000</u>
Net assets	<u>15,00,000</u>
	Shares
Total number of equity shares to be issued by A Ltd. @Rs.12 per share (Rs.15,00,000 / Rs.12)	1,25,000
Less: Number of equity shares of A Ltd. which are already with B Ltd.	<u>40,000</u>
Number of shares to be issued to outsiders	<u>85,000</u>
	Rs.
Equity share capital (85,000 shares × Rs.10)	8,50,000
Securities premium (85,000 shares × Rs.2)	<u>1,70,000</u>
Purchase consideration	<u>10,20,000</u>

Question 3

S and T were carrying on business as equal partners. Their Balance Sheet as on 31st March, 2007 stood as follows:

Liabilities	Rs.	Assets	Rs.
Capital accounts:		Stock	2,70,000
S	6,40,000	Debtors	3,65,000
T	<u>6,60,000</u>	Furniture	75,000
Creditors	3,27,500	Joint life policy	47,500
Bank overdraft	1,50,000	Plant	1,72,500
Bills payable	<u>62,500</u>	Building	<u>9,10,000</u>
	<u>18,40,000</u>		<u>18,40,000</u>

The operations of the business was carried on till 30th September, 2007. S and T both withdrew in equal amounts, half the amount of profits made during the current period of 6 months after 10% p.a. had been written off on building and plant and 5% p.a. written off on furniture. During the current period of 6 months, creditors were reduced by Rs.50,000, Bills payables by Rs.11,500 and bank overdraft by Rs.75,000. The Joint life policy was surrendered for Rs.47,500 on 30th September, 2007. Stock was valued at Rs.3,17,000 and

Working Notes:

(1) Ascertainment of total capital:

Balance Sheet			
as at 30 th September, 2007			
Liabilities	Rs.	Assets	Rs.
Sundry creditors	2,77,500	Building	9,10,000
Bills payable	51,000	Less: Depreciation	<u>45,500</u>
Bank overdraft	75,000	Plant	1,72,500
Total capital (bal. fig.)	13,40,000	Less: Depreciation	<u>8,625</u>
		Furniture	75,000
		Less: Depreciation	<u>1,875</u>
		Stock	3,17,000
		Debtors	<u>3,25,000</u>
	<u>17,43,500</u>		<u>17,43,500</u>

(2) Profit earned during six months to 30 September, 2007	Rs.
Total capital (of S and T) on 30 th September, 2007 (W.N.1)	13,40,000
Capital on 1 st April, 2007	
S	6,40,000
T	<u>6,60,000</u>
	<u>13,00,000</u>
Net increase (after drawings)	<u>40,000</u>

Since drawings are half of profits therefore, actual profit earned is Rs.40,000 x 2 = Rs.80,000 (shared equally by partners S and T).

Half of the profits, has been withdrawn by both the partners equally i.e. drawings Rs. 40,000 (Rs.80,000 x ½) withdrawn by S and T in 1:1 (i.e. Rs.20,000 each).

(3) Purchase consideration:	Rs.
Total assets (W.N.1)	17,43,500
Add: Goodwill	<u>5,40,000</u>
	22,83,500
Less: Liabilities (2,77,500 + 51,000 + 75,000)	<u>4,03,500</u>
Purchase consideration	<u>18,80,000</u>

Note: The above solution is given on the basis that reduction in bank overdraft is after surrender of Joint life policy.

Question 4

The Washington branch of XYZ Limited, Mumbai sent the following trial balance as on 31st December, 2007:

	\$	\$
Head office A/c	–	22,800
Sales	–	84,000
Debtors and creditors	4,800	3,400
Machinery	24,000	–
Cash at bank	1,200	–
Stock, 1 January, 2007	11,200	–
Goods from H.O.	64,000	–
Expenses	<u>5,000</u>	<u>–</u>
	<u>1,10,200</u>	<u>1,10,200</u>

In the books of head office, the Branch A/c stood as follows:

Washington Branch A/c			
	Rs.		Rs.
To Balance b/d	8,10,000	By Cash	28,76,000
To Goods sent to branch	<u>29,26,000</u>	By Balance c/d	<u>8,60,000</u>
	<u>37,36,000</u>		<u>37,36,000</u>

Goods are sent to the branch at cost plus 10% and the branch sells goods at invoice price plus 25%. Machinery was acquired on 31st January, 2002, when \$ 1.00 = Rs.40.

Rates of exchange were:

1 st January, 2007	\$ 1.00	=	Rs.46
31 st December, 2007	\$ 1.00	=	Rs.48
Average	\$ 1.00	=	Rs.47

Machinery is depreciated @ 10% and the branch manager is entitled to a commission of 5% on the profits of the branch.

You are required to:

- (i) Prepare the Branch Trading & Profit & Loss A/c in dollars.
- (ii) Convert the Trial Balance of branch into Indian currency and prepare Branch Trading & Profit and Loss A/c and the Branch A/c in the books of head office. (16 Marks)

Answer

(i)

In the Books of Head Office
Branch Trading and Profit & Loss A/c (in Dollars)
for the year ended 31st December, 2007

	Particulars	\$		Particulars	\$
To	Opening stock	11,200	By	Sales	84,000
To	Goods from H.O.	64,000	By	Closing stock (W.N.2)	8,000
To	Gross profit c/d	<u>16,800</u>			
		<u>92,000</u>			<u>92,000</u>
To	Expenses	5,000	By	Gross profit b/d	16,800
To	Depreciation	2,400			
To	Manager's commission (W.N.1)	470			
To	Net profit c/d	<u>8,930</u>			
		<u>16,800</u>			<u>16,800</u>

(ii) (a) Converted Branch Trial Balance (into Indian Currency)

Particulars	Rate per \$	Dr. (Rs.)	Cr. (Rs.)
Machinery	40	9,60,000	–
Stock January 1, 2007	46	5,15,200	–
Goods from head office	Actual	29,26,000	–
Sales	47	–	39,48,000
Expenses	47	2,35,000	–
Debtors & creditors	48	2,30,400	1,63,200
Cash at bank	48	57,600	–
Head office A/c	Actual	–	8,60,000
Difference in exchange rate		<u>47,000</u>	–
		<u>49,71,200</u>	<u>49,71,200</u>
Closing stock \$ 8,000 (W.N. 2)	48		Rs.3,84,000

(b) Branch Trading and Profit & Loss A/c
for the year ended 31st December, 2007

	Rs.		Rs.
To Opening stock	5,15,200	By Sales	39,48,000
To Goods from head office	29,26,000	By Closing stock (W.N.2)	3,84,000
To Gross profit c/d	<u>8,90,800</u>		
	<u>43,32,000</u>		<u>43,32,000</u>
To Expenses	2,35,000	By Gross profit b/d	8,90,800
To Depreciation @ 10% on Rs.9,60,000	96,000		
To Exchange difference	47,000		
To Manager's commission (W.N.1)	22,560		
To Net Profit c/d	<u>4,90,240</u>		
	<u>8,90,800</u>		<u>8,90,800</u>

(c) Branch Account

	Rs.		Rs.
To Balance b/d	8,60,000	By Machinery	9,60,000
To Net profit	4,90,240	Less: Depreciation	96,000
To Creditors	1,63,200	By Closing stock	3,84,000
To Outstanding commission	22,560	By Debtors	2,30,400
	<u>15,36,000</u>	By Cash at bank	57,600
			<u>15,36,000</u>

Working Note:

1. Calculation of manager's commission @ 5% on profit

i.e. 5% of \$[16,800 – (5,000 + 2,400)]

Or 5% × \$9,400 = \$ 470

Manager's commission in Rupees = \$ 470 × Rs.48 = Rs. 22,560

2. Calculation of closing stock	\$
Opening stock	11,200
Add: Goods from head office	<u>64,000</u>
	75,200
Less: Cost of goods sold (at invoice price)	
i.e. $\frac{100}{125} \times 84,000$	<u>67,200</u>
Closing stock	<u>8,000</u>
Closing stock in Rupees = \$8,000 x Rs.48 = Rs.3,84,000.	

Question 5

- (a) The following are the figures extracted from the books of New Generation Bank Limited as on 31.3.2008:

	Rs.
Interest and discount received	37,05,738
Interest paid on deposits	20,37,452
Issued and subscribed capital	10,00,000
Salaries and allowances	2,00,000
Directors fee and allowances	30,000
Rent and taxes paid	90,000
Postage and telegrams	60,286
Statutory reserve fund	8,00,000
Commission, exchange and brokerage	1,90,000
Rent received	65,000
Profit on sale of investments	2,00,000
Depreciation on bank's properties	30,000
Statutory expenses	40,000
Preliminary expenses	25,000
Auditor's fee	5,000

The following further information is given:

- (i) A customer to whom a sum of Rs.10 lakhs has been advanced has become insolvent and it is expected only 50% can be recovered from his estate.
- (ii) There were also other debts for which a provision of Rs.1,50,000 was found necessary by the auditors.

- (iii) Rebate on bills discounted on 31.3.2007 was Rs.12,000 and on 31.3.2008 was Rs.16,000.
- (iv) Provide Rs.6,50,000 for Income-tax.
- (v) The directors desire to declare 10% dividend.

Prepare the Profit and Loss account of New Generation Bank Limited for the year ended 31.3.2008 and also show, how the Profit and Loss account will appear in the Balance Sheet, if the Profit and Loss account opening balance was Nil as on 31.3.2007.

- (b) Prepare the Fire Insurance Revenue A/c as per IRDA regulations for the year ended 31st March, 2008 from the following details:

	Rs.
Claims paid	4,90,000
Legal expenses regarding claims	10,000
Premiums received	13,00,000
Re-insurance premium paid	1,00,000
Commission	3,00,000
Expenses of management	2,00,000
Provision against unexpired risk on 1 st April, 2007	5,50,000
Claims unpaid on 1 st April, 2007	50,000
Claims unpaid on 31 st March, 2008	80,000

(10+6 = 16 Marks)

Answer

- (a) New Generation Bank Limited
Profit and Loss Account for the year ended 31st March, 2008

	Schedule	Year ended 31.03.2008 (Rs. in '000s)
I. Income:		
Interest earned	13	3,701.74
Other income	14	<u>455.00</u>
Total		<u>4,156.74</u>
II. Expenditure		
Interest expended	15	2,037.45
Operating expenses	16	480.29

	Provisions and contingencies (500 + 150 + 650)	<u>1,300.00</u>
	Total	<u>3,817.74</u>
III.	Profits/Losses	
	Net profit for the year	339.00
	Profit brought forward	<u>Nil</u>
		<u>339.00</u>
IV.	Appropriations	
	Transfer to statutory reserve (25%)	84.75
	Proposed dividend	100.00
	Balance carried over to balance sheet	<u>154.25</u>
		<u>339.00</u>

The Profit & Loss Account balance of Rs.154.25 thousand will appear in the Balance Sheet under the head 'Reserves and Surplus' in Schedule 2.

Year ended
31.3.2008
(Rs. in '000s)

Schedule 13 – Interest Earned

I.	Interest/discount on advances/bills (Refer W.N.)	<u>3,701.74</u>
		<u>3,701.74</u>

Schedule 14 – Other Income

I.	Commission, exchange and brokerage	190.00
II.	Profit on sale of investments	200.00
III.	Rent received	<u>65.00</u>
		<u>455.00</u>

Schedule 15 – Interest Expended

I.	Interests paid on deposits	<u>2,037.45</u>
		<u>2,037.45</u>

Schedule 16 – Operating Expenses

I.	Payment to and provisions for employees	200.00
II.	Rent, taxes and lighting	90.00

III.	Depreciation on bank's properties	30.00
IV.	Director's fee, allowances and expenses	30.00
V.	Auditors' fee	5.00
VI.	Law (statutory) charges	40.00
VII.	Postage and telegrams	60.29
VIII.	Preliminary expenses	<u>25.00*</u>
		<u>480.29</u>

*It is assumed that preliminary expenses have been fully written off during the year.

Working Note:

Interest/discount (net of rebate on bills discounted)	3,705.74
Add: Rebate on bills discounted on 31.3.2007	12.00
Less: Rebate on bills discounted on 31.3.2008	<u>(16.00)</u>
	<u>3701.74</u>

(b)

FORM B - RA

Name of the Insurer:

Registration No. and Date of Registration with the IRDA:

Fire Insurance Revenue Account
for the year ended 31st March, 2008

	Particulars	Schedule	Amount (Rs.)
(1)	Premium earned	1	11,50,000
(2)	Other income		-
(3)	Interest, dividend and rent		<u>-</u>
	Total (A)		<u>11,50,000</u>
(4)	Claims incurred	2	5,30,000
(5)	Commission	3	3,00,000
(6)	Operating expenses related to Insurance business	4	<u>2,00,000</u>
	Total (B)		<u>10,30,000</u>
	Operating Profit (A)- (B)		<u>1,20,000</u>

Schedule 1 : Premium earned (net)	Rs.
Premium received	13,00,000
Less: Re-insurance premium	<u>1,00,000</u>
Net premium	12,00,000
Adjustment for change in reserve for unexpired risks (Refer W.N.)	<u>50,000</u>
	<u>11,50,000</u>

Schedule 2 : Claims Incurred	Rs.
Claims paid including legal expenses (4,90,000 + 10,000)	5,00,000
Add : Claims outstanding at the end of the year	80,000
Less : Claims outstanding at the beginning of the year	<u>(50,000)</u>
Total claims incurred	<u>5,30,000</u>

Schedule 3 : Commission	Rs.
Commission paid	<u>3,00,000</u>
	<u>3,00,000</u>

Schedule 4: Operating expenses	Rs.
Expenses of management	<u>2,00,000</u>
	<u>2,00,000</u>

Working Note:

Change in the provision for unexpired risk	Rs.
Unexpired risk reserve on 31 st March, 2008 =50% of net premium i.e. 50% of Rs.12,00,000 (See Schedule 1)	6,00,000
Less : Unexpired risk reserve as on 1 st April 2007	<u>5,50,000</u>
Change in the provision for unexpired risk	<u>50,000</u>

Question 6

Answer any four of the following:

- (i) (a) X Ltd. purchased debentures of Rs.10 lacs of Y Ltd., which are traded in stock exchange. How will you show this item as per AS 3 while preparing cash flow statement for the year ended on 31st March, 2008?
- (b) Mr. Raj a relative of key management personnel received remuneration of Rs.2,50,000 for his services in the company for the period from 1.4.2007 to

30.6.2007. On 1.7.2007, he left the service.

Should the relative be identified as a related party at the closing date i.e., on 31.3.2008 for the purpose of AS 18?

- (ii) A manufacturing company purchased shares of another company from stock exchange on 1st May, 2007 at a cost of Rs.5,00,000. It also purchased Gold of Rs.2,00,000 and Silver of Rs.1,50,000 on 1st April, 2005. How will you treat these investments as per the applicable AS in the books of the company for the year ended on 31st March, 2008, if the values of these investments are as follows:

	Rs.
Shares	2,00,000
Gold	4,00,000
Silver	2,50,000

- (iii) (a) Wye Ltd. received Rs.50 lacs from the Central Government as subsidy for setting up an industry in backward area. How will you treat it in accounts?
 (b) How Government grant relating to Specific Fixed Assets is treated in the books as per AS 12?
- (iv) A Ltd. had 6,00,000 equity shares on April 1, 2007. The company earned a profit of Rs.15,00,000 during the year 2007-08. The average fair value per share during 2007-08 was Rs.25. The company has given share option to its employees of 1,00,000 equity shares at option price of Rs.15. Calculate basic EPS and diluted EPS.
- (v) Give names of books required to be maintained in agriculture farm accounting.
- (vi) (a) How the Government expenditure in India is classified?
 (b) In a production process, normal waste is 5% of input. 5,000 MT of input were put in process resulting in wastage of 300 MT. Cost per MT of input is Rs.1,000. The entire quantity of waste is on stock at the year end. State with reference to Accounting Standard, how will you value the inventories in this case?

(4 x 4= 16 Marks)

Answer

- (i) (a) As per AS 3 on 'Cash flow Statement', cash and cash equivalents consists of cash in hand, balance with banks and short-term, highly liquid investments¹. If investment, of Rs.10 lacs, made in debentures is for short-term period then it is an item of 'cash equivalents'.

However, if investment of Rs.10 lacs made in debentures is for long-term period then as per AS 3, it should be shown as cash flow from investing activities.

¹ As per para 6 of AS 3, an investment normally qualifies as a cash equivalent only when it has a short maturity of, say three months or less from the date of acquisition.

- (b) According to para 10 of AS 18 on 'Related Party Disclosures', parties are considered to be related if at any time during the reporting period one party has the ability to control the other party or exercise significant influence over the other party in making financial and/or operating decisions.

Here, Mr. Raj, who received remuneration of Rs.2,50,000 from the company, is the relative of the key management personnel of that company. And as per para 3 clause (d) of the Standard, 'key management personnel and relatives of such personnel' are said to be in related party relationships. Hence, Mr. Raj, a relative of key management personnel, should be identified as related party at the closing date i.e. on 31.3.2008.

- (ii) As per para 32 of AS 13 on 'Accounting for Investments', any investment of long term period is shown at cost. Hence, the investment in Gold and Silver (purchased on 1st April 2005) shall continue to be shown at cost i.e., Rs.2,00,000 and Rs.1,50,000 respectively as their value have increased.

Also as per AS 13, for investment in shares - if the investment is for short-term period then the loss of Rs.3,00,000 is to be charged to profit & loss account for the year ended 31st March, 2008. If investment is of long term period then it will continue to be shown at cost in the Balance Sheet of the company. However, provision for diminution shall be made to recognize a decline, other than temporary, in the value of the investments, such reduction being determined and made for each investment individually.

- (iii) (a) As per para 10 of AS 12 on 'Accounting for Government Grants', subsidy of Rs.50 lacs from the Central government, for setting up an industry in backward area is a government grant in the nature of promoter's contribution. Such grants are treated as capital reserve which can be neither distributed as dividend nor considered as deferred income.
- (b) According to para 8 of AS 12 on 'Accounting for Government Grants', two methods of presentation, in financial statements, of grants related to specific fixed assets are regarded as acceptable alternatives.
- ◆ Under one method, the grant is shown as a deduction from the gross value of the asset concerned in arriving at its book value.
 - ◆ Under the other method, grant related to depreciable asset is treated as deferred income which is recognized in the profit and loss statement on a systematic and rational basis over the useful life of the assets. Grants related to non-depreciable assets are credited to capital reserve under this method, as there is usually no charge to income in respect of such assets. However, if a grant related to a non-depreciable asset requires the fulfillment of certain obligations, the grant is credited to income over the same period over which the cost of meeting such obligations is charged to income. The deferred income is suitably disclosed in the balance sheet pending its apportionment to profit and loss account.

(iv) Computation of earnings per share			
	Earnings	Shares	Earnings per share
Net profit for the year 2007-08	Rs.15,00,000		
Weighted average number of shares outstanding during year 2007-08		6,00,000	
Basic earnings per share			Rs. 2.50
Number of shares under option		1,00,000	
Number of shares that would have been issued at fair value: (100,000 x 15.00)/25.00	<u> *</u>	<u>(60,000)</u>	
Diluted earnings per share	<u>Rs. 15,00,000</u>	<u>6,40,000</u>	Rs. 2.34 (approx.)

*The earnings have not been increased as the total number of shares has been increased only by the number of shares (40,000) deemed for the purpose of the computation to have been issued for no consideration.

(v) The following seven books/registers are required in agriculture farm accounting:

- i. Cash book
- ii. Fixed assets register
- iii. Loan register
- iv. Stock register
- v. Debtors and creditors register
- vi. Register for notional transactions
- vii. Cost analysis register

(vi) (a) Government expenditure in India is classified into a five tier system:

- (i) Sectors
- (ii) Major Heads
- (iii) Minor Heads
- (iv) Sub-Heads
- (v) Detailed Heads of Accounts

(b) As per para 13 of AS 2 (Revised), abnormal amounts of wasted materials, labour and other production costs are excluded from cost of inventories and such costs are recognized as expenses in the period in which they are incurred.

In this case, normal waste is 250 MT and abnormal waste is 50 MT.

The cost of 250 MT will be included in determining the cost of inventories (finished goods) at the year end. The cost of abnormal waste amounting to Rs.50,000 (50 MT × Rs.1,000) will be charged to the profit and loss statement.