

MOCK TEST PAPER - 1
INTERMEDIATE (IPC): GROUP – II
PAPER – 5 : ADVANCED ACCOUNTING
ANSWERS

1. (a) As per para 14 of AS 29 'Provisions, Contingent Liabilities and Contingent Assets', a provision should be recognised when:
- (i) An enterprise has a present obligation as a result of past event;
 - (ii) It is probable that an outflow of resources embodying economic benefits will be required to settle the obligation; and
 - (iii) A reliable estimate can be made of the amount of the obligation.

If these conditions are not met, no provision should be recognised.

A contingent liability is disclosed, unless the possibility of an outflow of resources embodying economic benefits is remote. The possibility of an outflow of resources embodying economic benefits seems to be remote in the given situation, since the directors of Mohan Ltd. are of the opinion that the claim can be successfully resisted by the company. Therefore, the company shall not disclose the same as contingent liability. However, following note in this regard may be given in annual accounts of the company:

“Litigation is in process against the company relating to a dispute with a competitor who alleges that the company has infringed patents and is seeking damages of Rs. 900 lakhs. However, the directors are of the opinion that the claim can be successfully resisted by the company”.

- (b) 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	= <u>1,40,000 shares</u>
	= <u>8,40,000 shares</u>

- (c) (i) Interest for the period 2016-17
 = US \$ 10 lakhs x 4% x Rs. 62 per US\$ = Rs. 24.80 lakhs
- (ii) Increase in the liability towards the principal amount
 = US \$ 10 lakhs x Rs. (62 - 56) = Rs. 60 lakhs
- (iii) Interest that would have resulted if the loan was taken in Indian currency
 = US \$ 10 lakhs x Rs. 56 x 10.5% = Rs. 58.80 lakhs
- (iv) Difference between interest on local currency borrowing and foreign currency borrowing = Rs. 58.80 lakhs - Rs. 24.80 lakhs = Rs. 34 lakhs.

Therefore, out of Rs. 60 lakhs increase in the liability towards principal amount, only Rs. 34 lakhs will be considered as the borrowing cost. Thus, total borrowing cost would be Rs. 58.80 lakhs being the aggregate of interest of Rs. 24.80 lakhs on foreign currency borrowings plus the

exchange difference to the extent of difference between interest on local currency borrowing and interest on foreign currency borrowing of Rs. 34 lakhs.

Hence, Rs. 58.80 lakhs would be considered as the borrowing cost to be accounted for as per AS 16 and the remaining Rs. 26 lakhs (60 - 34) would be considered as the exchange difference to be accounted for as per AS 11

(d) Following will be the treatment in the given cases:

- (i) When sales price of Rs. 50 lakhs is equal to fair value, A Ltd. should immediately recognise the profit of Rs. 10 lakhs (i.e. 50 – 40) in its books.
- (ii) When fair value of leased machinery is Rs. 45 lakhs & sales price is Rs. 38 lakhs, then loss of Rs. 2 lakhs (40 – 38) to be immediately recognised by A Ltd. in its books provided loss is not compensated by future lease payment.
- (iii) When fair value is Rs. 40 lakhs & sales price is Rs. 50 lakhs then, profit of Rs. 10 lakhs is to be deferred and amortised over the lease period.
- (iv) When fair value is Rs. 46 lakhs & sales price is Rs. 50 lakhs, profit of Rs. 6 lakhs (46-40) to be immediately recognised in its books and balance profit of Rs. 4 lakhs (50-46) is to be amortised/deferred over lease period.
- (v) When fair value is Rs. 35 lakhs & sales price is Rs. 39 lakhs, then the loss of Rs. 5 lakhs (40-35) to be immediately recognised by A Ltd. in its books and profit of Rs. 4 lakhs (39-35) should be amortised/deferred over lease period.

2. (i) Journal Entries in the books of Omega Ltd. (Rs. in lakhs)

Particulars				
1	Bank A/c To Investments A/c To Profit and Loss A/c (Being investment sold on profit for the purpose of buy-back)	Dr.	3,150	3,000 150
2	10% Redeemable Preference Share Capital A/c Premium on Redemption of Preference Shares A/c To Preference Shareholders A/c (Being redemption of preference share capital at premium of 10%)	Dr. Dr.	2,500 250	2,750
3	Securities Premium A/c To Premium on Redemption of Preference Shares A/c (Being premium on redemption of preference shares adjusted through securities premium)	Dr.	250	250
4	Equity Share Capital A/c Premium on buyback To Equity buy-back A/c (Being Equity Share bought back, Share Capital cancelled, and Premium on Buyback accounted for)	Dr. Dr.	1,200 1,200	2,400
5	Securities Premium A/c (800-250) General Reserve A/c To Premium on Buyback A/c (Being premium on buyback provided first out of securities premium and the balance out of general reserves.)	Dr. Dr.	550 650	1,200

6	Bank A/c To Bank Loan A/c (Being loan taken from bank to finance buyback and redemption of shares)	Dr.	400	400
7	Preference Shareholders A/c Equity buy-back A/c To Bank A/c (Being payment made to preference shareholders and equity shareholders)	Dr. Dr.	2,750 2,400	5,150
8	General Reserve Account To Capital Redemption Reserve Account (Being amount transferred to capital redemption reserve account towards face value of preference shares redeemed and equity shares bought back)	Dr.	3,700	3,700

(ii) **Balance Sheet of Omega Ltd. (after Redemption and Buyback)** **(Rs. Lakhs)**

	<i>Particulars</i>	<i>Note No</i>	<i>Amount</i>
	EQUITY AND LIABILITIES		<i>Rs.</i>
(I)	Shareholders' Funds:		
	(a) Share Capital	1	6,800
	(b) Reserves and Surplus	2	6,800
(2)	Non-Current Liabilities:		
	(a) Long Term Borrowings	3	5,400
(3)	Current Liabilities:		
	(a) Trade payables		2,300
	(b) Short Term Provisions		<u>1,000</u>
	Total		<u>22,300</u>
(II)	ASSETS		
(1)	Non-Current Assets		
	Property, Plant & Equipment		14,000
	Current Assets:		
	(a) Cash and Cash equivalents (W N)		50
	(b) Other Current Assets		<u>8,250</u>
	Total		<u>22,300</u>

Notes to Accounts

		<i>Rs. in Lakhs</i>	
1.	Share Capital		
	680 lakh Equity Shares of Rs. 10 each Fully Paid up (120 lakh Equity Shares bought back)		6,800
2.	Reserves and Surplus		
	General Reserve	6,000	
	Less: Adjustment for premium paid on buy back	(650)	
	Less: Transfer to CRR	<u>(3,700)</u>	1,650

	Capital Redemption Reserve	1,000		
	Add: Transfer due to buy-back of shares from Gen. res.	<u>3,700</u>	4,700	
	Securities premium	800		
	Less: Adjustment for premium paid on redemption of preference shares	(250)		
	Less: Adjustment for premium paid on buy back	<u>(550)</u>	-	
	Profit & Loss A/c	300		
	Add: Profit on sale of investment	<u>150</u>	<u>450</u>	6,800
3.	Long-term borrowings			
	Secured			
	9 % Debentures		5,000	
	Term Loans – From Banks		<u>400</u>	5,400

Working Note

Bank Account

Receipts	Amount	Payments	Amount
	(Rs. Lakhs)		(Rs. Lakhs)
To balance b/d	1,650	By Preference Shareholders A/c	2,750
To Investment A/c (sale Proceeds)	3,150	By Equity Shareholders A/c	2,400
To Bank Loan A/c (Loan received)	400	By Balance c/d (Balancing figure)	
	<u>5,200</u>		<u>50</u>
			<u>5,200</u>

Income tax on the above will not be included in Revenue A/c of an insurance company.

3.

Realization Account

	Rs.	Rs.		Rs.
To Land & Building		2,00,000	By Trade Payables	1,20,000
To Plant		2,00,000	By Preet Limited (W.N.1)	6,69,500
To Inventories		1,50,000		
To Trade Receivable		1,00,000		
To Cash		1,00,000		
To Profit transferred to Capital A/c:				
L	19,750			
M	11,850			
N	<u>7,900</u>	39,500		
		<u>7,89,500</u>		<u>7,89,500</u>

Cash Account

	Rs.		Rs.
To N's Capital A/c	46,000	By L's Capital A/c	23,000
		By M's Capital A/c	23,000
	<u>46,000</u>		<u>46,000</u>

Partners' Current Accounts

	L Rs.	M Rs.	N Rs.		L Rs.	M Rs.	N Rs.
To Balance b/d	-		50,000	By Balance b/d	50,000	30,000	-
To L's Capital A/c	69,750			By Realisation A/c	19,750	11,850	7,900
To M's Capital A/c		41,850		By N's Capital A/c			42,100
	69,750	41,850	50,000		69,750	41,850	50,000

Partners' Capital Accounts

	L Rs.	M Rs.	N Rs.		L Rs.	M Rs.	N Rs.
To N's Current A/c	-	-	42,100	By Balance b/d	3,00,000	2,00,000	1,00,000
To Preference Shares in Preet Ltd. A/c	1,12,500	67,500	45,000	By L's Current A/c	69,750		
To Debentures A/c	1,47,250	88,350	58,900	By M'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:

- Calculation of Purchase consideration

Net Payment Method

	Rs.
Equity Shares = 10,000 @ Rs. 15	1,50,000
Preference Shares = 15,000 @ Rs. 15	2,25,000
Debentures = 20,000 @ Rs. 14.725	<u>2,94,500</u>
	<u>6,69,500</u>

- As whole business of the firm was sold to Preet Limited, cash balance of the firm Rs. 1,00,000 is also transferred to realization account. Cash brought in by N equal to Dr. balance appearing in his account, after distribution of preference shares and debentures in profit sharing ratio would be shared by L and M equally. The balance amount payable to L and M would be settled by transfer of equity shares in Preet Company.

- (a) **In the books of Head Office – XYZ**
Kolkata Branch Account (at invoice)

	Rs.		Rs.
To Balance b/d		By Stock reserve (opening)	6,000
Stock	30,000	By Remittances:	
Debtors	18,000	Cash Sales	1,00,000
Cash in hand	800	Cash from Debtors	<u>60,000</u>
Furniture	3,000	By Goods sent to branch (loading)	32,000

To Goods sent to branch	1,60,000	By Goods returned by branch (Return to H.O.)	2,000
To Goods returned by branch (loading)	400	By Balance c/d	
To Bank (expenses paid by H.O.)		Stock	28,000
Rent	1,800	Debtors	16,880
Salary	3,200	Cash (800-600)	200
Stationary & printing	800	Furniture (3,000-300)	2,700
	5,800		
To Stock reserve (closing)	5,600		
To Profit transferred to General Profit & Loss A/c	24,180		
	2,47,780		2,47,780

Working Note:

Debtors Account

	Rs.		Rs.
To Balance b/d	18,000	By Cash account	60,000
To Sales account (credit)	60,000	By Sales return account	960
		By Discount allowed account	160
		By Balance c/d	16,880
	78,000		78,000

Note: It is assumed that goods returned by branch are at invoice price.

(b)

**In the books of Ganesh Ltd.
New York Branch Trial Balance in (Rs.)
as on 31st March, 2018**

	Conversion rate per US \$ (Rs.)	Dr. Rs.	Cr. Rs.
Stock on 1.4.15	40	12,000	
Purchases and sales	41	32,800	61,500
Sundry debtors and creditors	42	16,800	12,600
Bills of exchange	42	5,040	10,080
Sundry expenses	41	44,280	
Bank balance	42	17,640	
Delhi office A/c	-		44,380
		1,28,560	1,28,560

(c)

Journal Entries in the books of company

Date	Particulars	Dr. Rs.	Cr. Rs.
1-3-X2 to	Bank A/c	Dr. 2,40,000	
31-3-X2	Employees compensation expenses A/c	Dr. 4,32,000	
	To Equity Share Capital A/c		48,000

31-3-X2	To Securities Premium A/c (Being allotment to employees 4,800 shares of Rs. 10 each at a premium of Rs. 130 at an exercise price of Rs. 50 each)		6,24,000
	Profit and Loss account	Dr.	4,32,000
	To Employees compensation expenses A/c (Being transfer of employees compensation expenses)		4,32,000

Working Note:

- Employee Compensation Expenses = Discount between Market Price and option price = Rs. 140 – Rs. 50 = Rs. 90 per share = Rs. 90 x 4,800 = Rs. 4,32,000/- in total.
- The Employees Compensation Expense is transferred to Securities Premium Account.
- Securities Premium Account = Rs. 50 – Rs. 10 = Rs. 40 per share + Rs. 90 per share on account of discount of option price over market price = Rs. 130 per share = Rs. 130 x 4,800 = Rs. 6,24,000/- in total.

5. (a) (i) Calculation of Rebate on bills discounted (not due) on 31.3.2017

S. No.	Amount (Rs.)	Due date 2017	Unexpired portion	Rate of discount	Rebate on bill discounted (Rs.)
(i)	7,50,000	April 8	8 days	12%	1,972
(ii)	3,00,000	May 5	35 days	14%	4,028
(iii)	4,40,000	June 12	73 days	14%	12,320
(iv)	9,60,000	July 15	106 days	15%	4,1820
					<u>60,140</u>

(ii) Amount of discount to be credited to the Profit and Loss Account

	Rs.
Transfer from Rebate on bills discount as on 31 st March, 2016	66,400
Add: Discount received during the year ended 31 st March, 2017	<u>3,00,000</u>
	3,66,400
Less: Rebate on bills discounted as on 31 st March, 2017	<u>60,140</u>
Discount credited to the Profit and Loss Account	<u>3,06,260</u>

(b) Modern Insurance Company (Abstract showing the Amount of claims)

Net Claims incurred

	Rs.
Claims paid on direct business (7,06,000 + 7,600 + 8,400)	7,22,000
Add: Re-insurance	1,64,000
Add: Outstanding as on 31.3.2017	17,400
Less: Outstanding as on 1.4.2016	<u>(11,600)</u>
	8,91,800
Less: Claims received from re-insurance	64,000
Add: Outstanding as on 31.3.2017	28,400
Less: Outstanding as on 1.4.2016	<u>(17,000)</u>
	<u>(75,400)</u>
	8,16,400

Add: Outstanding direct claims at the end of the year	1,75,000
	9,91,400
Less: Outstanding claims at the beginning of the year	(1,64,600)
Net claims incurred	8,26,800

- (c) The event is a non-adjusting event with reference to the provisions of AS 4 "Contingencies and Events Occurring After the Balance Sheet Date" since it occurred after the year-end and does not relate to the conditions existing at the year-end. However, the event would appear to be of such significance as to require a disclosure in the report of the approving authority to enable users of the financial statements to make proper evaluation and decision, hence, such disclosure is recommended.

6. Journal Entries in the books of Lion Ltd.

	<i>Particulars</i>	<i>Debit (Rs. in lakhs)</i>	<i>Credit (Rs. in lakhs)</i>
(i)	8% Preference share capital A/c (Rs. 100 each) Dr. To 8% Preference share capital A/c (Rs. 80 each) To Capital Reduction A/c (Being the preference shares of Rs. 100 each reduced to Rs. 80 each as per the approved scheme)	400	320 80
(ii)	Equity share capital A/c (Rs. 10 each) Dr. To Equityshare capital A/c (Rs. 2 each) To Capital Reduction A/c (Being the equity shares of Rs. 10 each reduced to Rs. 2 each)	1,000	200 800
(iii)	Capital Reduction A/c Dr. To Equity share capital A/c (Rs. 2 each) (Being 1/3 rd arrears of preference share dividend of 3 years to be satisfied by issue of 8 lakhs equity shares of Rs. 2 each)	32	32
(iv)	6% Debentures A/c Dr. To Freehold property A/c (Being claim of Debenture holders settled in part by transfer of freehold property)	300	300
(v)	Accrued debenture interest A/c Dr. To Bank A/c (Being accrued debenture interest paid)	24	24
(vi)	Freehold property A/c Dr. To Capital Reduction A/c (Being appreciation in the value of freehold property)	150	150
(vii)	Bank A/c Dr. To Investments A/c To Capital Reduction A/c (Being investment sold at profit)	250	200 50

(vii)	Director's loan A/c To Equity share capital A/c (Rs. 2 each) To Capital Reduction A/c (Being director's loan waived by 70% and balance being discharged by issue of 45 lakhs equity shares of Rs. 2 each)	Dr.	300	
				90
				210
(ix)	Capital Reduction A/c To Profit and loss A/c To Trade receivables A/c (450x 40%) To Inventories-in-trade A/c (300x 80%) To Bank A/c (600 x 5%) (Being certain value of various assets, penalty on cancellation of contract, profit and loss account debit balance written off through Capital Reduction Account)	Dr.	972	
				522
				180
				240
				30
(x)	Capital Reduction A/c To Capital reserve A/c (Being balance transferred to capital reserve account as per the scheme)		286	
				286

Capital Reduction Account

		(Rs. in lakhs)			(Rs. in lakhs)
To	Equity Share Capital	32	By	Preference Share Capital	80
To	Trade receivables	180	By	Equity Share Capital	800
To	Finished Goods	240	By	Freehold Property	150
To	Profit & Loss A/c	522	By	Bank	50
To	Bank A/c	30	By	Director's Loan	210
To	Capital Reserve	<u>286</u>			
		<u>1,290</u>			<u>1,290</u>

Notes to Balance Sheet

		(Rs. in lakhs)	(Rs. in lakhs)
1.	<u>Share Capital</u>		
	<u>Authorized:</u>		
	200 lakhs Equity shares of Rs. 2 each		<u>400</u>
	8 lakhs 8% Preference shares of Rs. 80 each		<u>640</u>
			<u>1,040</u>
	<u>Issued:</u>		
	161 lakhs equity shares of Rs. 2 each		322
	4 lakhs Preference Shares of Rs. 80 each		<u>320</u>
			<u>642</u>
2.	<u>Tangible Assets</u>		
	Freehold Property	550	
	Less: Utilized to pay Debenture holders	<u>(300)</u>	
		250	

Add: Appreciation	150	400
Plant and Machinery		<u>200</u>
		<u>600</u>

7. (a) A liability is recognized when outflow of economic resources in settlement of a present obligation can be anticipated and the value of outflow can be reliably measured. In the given case, ABC Ltd. should recognize a liability of Rs.4, 00,000 payable to XYZ Ltd.

When flow of economic benefit to the enterprise beyond the current accounting period is considered improbable, the expenditure incurred is recognized as an expense rather than as an asset. In the present case, flow of future economic benefit from the machine to the enterprise is improbable. The entire amount of purchase price of the machine should be recognized as an expense.

Hence ABC Ltd. should charge the amount of Rs. 4,00,000 (being loss due to change in production method) to Profit and loss statement and record the corresponding liability (amount payable to XYZ Ltd.) for the same amount in the books for the year ended 31st March, 2016.

(b) Calculation of Total Remuneration payable to Liquidator

		<i>Amount in Rs.</i>
2% on Assets realised	(45,00,000 x 2%)	90,000
3% on payment made to Preferential creditors	1,25,000 x 3%	3,750
3% on payment made to Unsecured creditors (Refer W.N)		<u>79,551</u>
Total Remuneration payable to Liquidator		<u>1,73,301</u>

Working Note:

Liquidator's remuneration on payment to unsecured creditors =

Cash available for unsecured creditors after all payments including liquidation expenses, payment to secured creditors, preferential creditors & liquidator's remuneration

= Rs. 45,00,000 – Rs. 50,000 – Rs. 15,00,000 – Rs. 1,25,000 – Rs. 90,000 – Rs. 3,750

= Rs. 27,31,250

Liquidator's remuneration on payment to unsecured creditors = $\frac{3}{103} \times \text{Rs. } 27,31,250 = \text{Rs. } 79,551$.

- (c) **Nature of Limited Liability Partnership:** A limited liability partnership is a body corporate formed and incorporated under the LLP Act, 2008 and is a legal entity separate from that of its partners. A limited liability partnership shall have perpetual succession and any change in the partners of a limited liability partnership shall not affect the existence, rights or liabilities of the limited liability partnership.

Designated partners: Every limited liability partnership shall have at least two designated partners who are individuals and at least one of them shall be a resident in India.

In case of a limited liability partnership in which all the partners are bodies corporate or in which one or more partners are individuals and bodies corporate, at least two individuals who are partners of such limited liability partnership or nominees of such bodies corporate shall act as designated partners

(d) **Calculation of number of equity shares to be allotted**

	<i>Number of debentures</i>
Total number of debentures	30,000
Less: Debenture holders who have not opted for conversion	<u>(2,500)</u>
Debenture holders who opted for conversion	<u>27,500</u>
Option for conversion	20%
Number of debentures to be converted (20% of 27,500)	5,500
Redemption value of 5,500 debentures at a premium of 5% [$5,500 \times (100+5)$]	Rs. 5,77,500
Equity shares of Rs. 10 each issued on conversion [Rs. 5,77,500/ Rs. 15]	38,500 shares

- (e) As per provisions of AS 26 "Intangible Assets", expenditure on research should be recognized as an expense when it is incurred. An intangible asset arising from development (or from the development phase of an internal project) should be recognized if, and only if, an enterprise can demonstrate all of the conditions specified in para 44 of the standard. An intangible asset (arising from development) should be derecognized when no future economic benefits are expected from its use according to para 87 of the standard. Thus, the manager cannot defer the expenditure write off to future years in the given case. Hence, the expenses amounting Rs. 40 lakhs incurred on the research and development project has to be written off in the current year ending 31st March, 2018.