PAPER – 1 : ACCOUNTING

*Question No. **1** is compulsory.*

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

Wherever necessary, suitable assumptions may be made and indicated in answer by the candidates.

Working Notes should form part of the answer.

Question 1

(a) (i) PP Ltd. an Indian Company acquired long term finance from WW (P) Ltd. a U.S. company, amounting to ₹ 40,88,952. The transaction was recorded at US $1 = ₹ 72.00, taking exchange rate prevailing at the date of transaction. The exchange rate on balance sheet date (31.03.2021) is US $1 = ₹ 73.60.

(ii) Trade receivables of PP Ltd. include amount receivable from Preksha Ltd., ₹ 20,00,150 recorded at the prevailing exchange rate on the date of sales, transaction recorded at US $1 = ₹ 73.40. The exchange rate on balance sheet date (31.03.2021) is US $1 = ₹ 73.60. Exchange rate on 1st April, 2020 is US $1 = ₹ 74.00.

You are required to calculate the amount of exchange difference and also explain the accounting treatment needed in the above two cases as per AS 11 in the books of PP Ltd.

(b) Following are the extracts from the Balance Sheet of ABC Ltd.

Liabilities	31.3.2020 (₹)	31.3.2021 (₹)
Equity Share Capital	25,00,0000	35,60,000
10% Preference Share Capital	7,00,000	6,00,000
Securities Premium Account	5,00,000	5,50,000
Profit & Loss A/c	20,00,000	28,00,000

Equity Share Capital for the year ended 31st March, 2021 includes ₹ 60,000 of equity shares issued to Grey Ltd. at par for supply of Machinery of ₹ 60,000.

Profit & Loss account on 31st March, 2021 includes ₹ 50,000 of dividend received on Equity shares invested in X Ltd.

Show how the related items will appear in the Cash Flow Statement of ABC Ltd. as per AS-3 (Revised) *(c) Mr. Mohan has invested some money in various Mutual funds. Following information in this regard is given:*

Mutual Funds	*Date of purchase*	*Purchase cost (₹)*	*Brokerage Cost (₹)*	*Stamp duty (₹)*	*Market value as on 31.03.2021 (₹)*
A	*01.05.2017*	*50,000*	*200*	*20*	*48,225*
B	*05.08.2020*	*25,000*	*150*	*25*	*24,220*
C	*01.01.2021*	*75,000*	*300*	*75*	*78,190*
D	*07.05.2020*	*70,000*	*275*	*50*	*65,880*

You are required to:

1. *Classify his investment in accordance with AS-13 (revised).*
2. *Value of Investment in mutual fund as on 31.03.2021*

(d) (i) ABC Ltd. was previously making provision for non-moving stocks based on stocks not issued for the last 12 months up to 31.03.2020. Now, the company wants to make provisions based on technical evaluation during the year ending 31.03.2021.

Total value of stock ₹ 133.75 lakhs

Provision required based on technical evaluation ₹ 4.00 lakhs

Provision required based on 12 months not issued ₹ 5.00 lakhs.

(ii) In the Books of Kay Ltd., Closing stock as on 31st March, 2021 amounts to ₹ 1,24,000 (on the basis of FIFO method)

The company decides to change from FIFO method to weighted average method for ascertaining the cost of inventory from the year 2020-2021. On the basis of weighted average method, closing stock as on 31st March, 2021 amounts to ₹ 1,15,000. Realisable value of the inventory as on 31st March, 2021 amounts to ₹ 1,54,000.

Discuss Disclosure Requirements of change in accounting policy in above cases as per AS 1. ***(4 Parts x 5 Marks = 20 Marks)***

Answer

(a) (i) Long term Finance

	Foreign Currency Rate	₹
Initial recognition US $ 56,791 (40,88,952/72)	1 US $ = ₹ 72	40,88,952
Rate on Balance sheet date	1 US $ = ₹ 73.60	
Exchange Difference Loss [US $ 56,791 x (73.60 – 72)]		90,866 (rounded off)

As per AS 11 "The Effects of Changes in Foreign Exchange Rates", exchange differences arising on the settlement of monetary items or on reporting an enterprise's monetary items at rates different from those at which they were initially recorded during the period, or reported in previous financial statements, should be recognized as income or as expenses in the period in which they arise.

However, at the option of an entity, exchange differences arising on reporting of long-term foreign currency monetary items at rates different from those at which they were initially recorded during the period, or reported in previous financial statements, in so far as they relate to the acquisition of a non-depreciable capital asset can be accumulated in a "Foreign Currency Monetary Item Translation Difference Account" in the enterprise's financial statements and amortized over the balance period of such long-term asset/ liability, by recognition as income or expense in each of such periods.

Treatment needed in this case: PP Ltd. can either Debit Foreign Currency Monetary Item Translation Difference (FCMITD) A/c or Debit Profit and Loss A/c by ₹ 90,866 and Credit Loan A/c

(ii) Trade Receivables

	Foreign Currency Rate	₹
Initial recognition US $ 27,250 (20,00,150/ 73.40)	1 US $ = ₹ 73.40	20,00,150
Rate on Balance sheet date	1 US $ = ₹ 73.60	
Exchange Difference Gain [US $ 27,250 X (73.60-73.40)]		5,450

As per AS 11 "The Effects of Changes in Foreign Exchange Rates", exchange differences on trade receivables amounting ₹ 5,450 is required to be transferred to Profit and Loss A/c.

Treatment needed in this case: Credit Profit and loss account by ₹ 5,450.

(b) The related items given in the question will appear in the Cash Flow Statement of ABC Limited for the year ended 31st March, 2021 as follows:

	₹	₹
Cash flows from operating activities		
Closing Balance as per Profit and Loss Account	28,00,000	
Less: Opening Balance as per Profit and Loss Account	(20,00,000)	
	8,00,000	
Less: Dividend received	50,000	
		7,50,000

Cash flows from investing activities		
Dividend received		50,000
Cash flows from financing activities		
Proceeds from issuance of share capital		
Equity shares issued for cash ₹ 10,00,000		
Proceeds from securities premium		
(₹ 5,50,000 – 5,00,000) ₹ 50,000		
	10,50,000	
Less: Redemption of Preference shares		
(₹ 7,00,000 – ₹ 6,00,000)	(1,00,000)	9,50,000

Note:

1. Machinery acquired by issue of shares does not amount to cash outflow, hence also not considered in the cash flow statement.
2. ABC Ltd. has been considered as a non-financial company in the given answer.

(c) As per AS 13 "Accounting for Investments", a current investment is an investment that is by its nature readily realizable and is intended to be held for not more than one year from the date on which such investment is made. The carrying amount for current investments is the lower of cost and fair value.

A long-term investment is an investment other than a current investment. Long term investments are usually carried at cost. If there is a decline, other than temporary, in the value of a long-term investment; the carrying amount is reduced to recognize the decline.

Mutual Funds	Classification	Cost (₹)	Market value (₹)	Carrying value (₹)
A	Long-term Investment	50,220	48,225*	50,220
B	Current Investment	25,175	24,220	24,220
C	Current Investment	75,375	78,190	75,375
D	Current Investment	70,325	65,880	65,880
Total				2,15,695

Note: *The reduction in value of Mutual fund A is considered to be temporary. If reduction in Market value is assumed as other than temporary in nature, then the carrying value of ₹48,225 will be considered.

(d) (i) The decision of making provision for non-moving inventories on the basis of technical evaluation does not amount to change in accounting policy. Accounting policy of a company may require that provision for non-moving inventories should be made. The method of estimating the amount of provision may be changed in case a more prudent estimate can be made.

In the given case, considering the total value of inventory, the change in the amount of required provision of non-moving inventory from ₹ 5 lakhs to ₹ 4 lakhs is also not material. The disclosure can be made for such change in the following lines by way of notes to the accounts in the annual accounts of ABC Ltd. for the year 2020-21:

"The company has provided for non-moving inventories on the basis of technical evaluation unlike preceding years. Had the same method been followed as in the previous year, the profit for the year and the corresponding effect on the year end net assets would have been lower by ₹ 1 lakh."

(ii) As per AS 1 "Disclosure of Accounting Policies", any change in an accounting policy which has a material effect should be disclosed in the financial statements. The amount by which any item in the financial statements is affected by such change should also be disclosed to the extent ascertainable. Where such amount is not ascertainable, wholly or in part, the fact should be indicated. Thus company should disclose the change in valuation method of inventory and its effect on financial statements. The company may disclose the change in accounting policy in the following manner:

"The company values its inventory at lower of cost and net realizable value. Since net realizable value of all items of inventory in the current year was greater than respective costs, the company valued its inventory at cost. In the present year i.e. 2020-21, the company has changed to weighted average method, which better reflects the consumption pattern of inventory, for ascertaining inventory costs from the earlier practice of using FIFO for the purpose. The change in policy has reduced current profit and value of inventory by ₹ 9,000."

Question 2

(a) The Godown of X Ltd. caught fire on 01.06.2021, records saved from fire shows the following particulars:

	₹
Stock at cost on 01.01.2020	*50,000*
Stock at cost on 31.12.2020	*80,000*
Purchases for the year 2020	*4,75,000*
Purchase returns for the year 2020	*5,000*
Carriage inward for the year 2020	*20,000*
Sales for the year 2020	*5,60,000*
Sales returns for the year 2020	*10,000*

Following information is given for the period of 1st January 2021 to 1st June, 2021:

Credit sales of ₹ 2,50,000, which constituted 25% of total sales.

Sales return ₹ 9,500, Goods used for personal purpose costing ₹ 5,000,

Good distributed as free sample costing ₹ 2,700, Wages ₹ 25,000.

Sales include goods sold on approval basis amounting to ₹ 81,000, no confirmation had been received in respect of 50% of such goods sold on approval basis.

Stock on 31 December, 2020 was calculated at 20% less than cost.

Purchases for the period 1st January, 2021 to 1st June, 2021 is ₹ 6,75,000, purchase returns ₹ 10,000.

Selling price was increased by 20% with effect from 01.01.2021.

Company had taken an insurance policy of ₹ 70,000 which was subject to an average clause. The value of salvaged goods was ₹ 21,967. You are required to compute the amount of the claim.

(b) During the year ended 31st March, 2021, Purple Ltd. entered into the following transactions:

1st April, 2020	*Purchased ₹ 4,00,000, 10% Govt. loan [1](interest payable on 30th April and 31st October) at ₹ 70 cum interest.*
1st April, 2020	*Purchased 6,000 Equity shares of ₹ 5 each in XY Ltd. for ₹ 1,26,000.*
1st October, 2020	*Sold ₹ 80,000, 10% Govt. loan at ₹75 ex-interest.*
15th January, 2021	*XY Ltd. made a bonus issued of four equity shares for every three shares held. Purple Ltd. sold all of the bonus shares for ₹ 10 each.*
1st March, 2021	*Received dividend @ 22% on shares in XY Ltd. for the year ended 31st December, 2020.*

Prepare Investment accounts in the books of Purple Ltd. ***(10 + 10 = 20 Marks)***

Answer

(a) X Ltd.

Trading Account for the year ending 31st December, 2020

(To determine the rate of gross profit)

		₹			₹	₹
To	Opening Stock	50,000	By	Sales A/c (5,60,000 – 10,000)		5,50,000

[1] Face value of Govt. loan to be read as ₹ 100.

To	Purchases (4,75,000 – 5,000)	4,70,000	By	Closing Stock: (80,000/80x100)		1,00,000
To	Carriage inward	20,000				
To	Gross Profit (b.f.)	1,10,000				
		6,50,000				6,50,000

The (normal) rate of gross profit to sales is = ₹ 1,10,000/ 5,50,000 x100= 20%

Memorandum Trading Account for the period

1st January, 2021 to 1st June, 2021

		₹		₹
To Opening Stock		1,00,000	By Sales (W.N. 2)	9,50,000
To Purchases	6,75,000		By Goods with customers (for approval) (W.N.1)*	27,000
Less: Returns	(10,000)			
Samples	(2,700)		By Closing stock (Bal. fig.)	1,21,967
Drawings	(5,000)	6,57,300		
To Wages		25,000		
To Gross Profit [1/3of Sales - Refer W.N. 3]		3,16,667		
		10,98,967		10,98,967

* *For financial statement purposes, this would form part of closing stock (since there is no sale). However, this has been shown separately for computation of claim for loss of stock since the goods were physically not with the concern and, hence, there was no loss of such stock as a result of fire.*

Statement of claim for loss of stock on 18.06.2021

Book value of stock	₹ 1,21,967
Less: Salvaged value of stock	₹ 21,967
Loss of stock	1,00,000

$$\text{Amount of claim} = \frac{\text{Insured Value}}{\text{Total cost of stock on the date of fire}} \text{ x Loss of stock} \qquad 57,393 \text{ (rounded off)}$$

$$\left(\frac{70,000}{1,21,967} \times 1,00,000\right)$$

A claim of ₹ 57,393 (rounded off) should be lodged to the insurance company.

Working Notes:

1. **Calculation of goods with customers**

   Since no approval for sale has been received for the goods of ₹ 40,500 (i.e. 1/2 of ₹ 81,000) hence, these should be valued at cost i.e. ₹ 27,000 (40,500/120 x 80)

2. **Calculation of actual sales**

   Total sales – Returns - Sale of goods on approval (1/2)

   = ₹ 10,00,000 – ₹ 9,500 – ₹ 40,500 (81,000/2) = ₹ 9,50,000

3. **Calculation of Gross Profit Ratio**

   For year 2020 : Cost of goods sold was 80, Gross profit rate 20% and sales 100

   For year 2021 : Cost of goods sold was 80, Gross profit rate 33.33% (1/3 of sales) and sales 120

Note: It is given in the question, that selling price was increased by 20% with effect from 01.01.2021. While solving the question in the given answer, new gross profit ratio has been computed and applied to arrive at the value of closing stock. Alternatively, instead of computing new gross profit ratio, sales can be reduced to the levels before increase and old gross profit ratio can be applied to arrive at the value of closing stock.

(b) **In the books of Purple Ltd.**

10% Govt. Loan
[Interest Payable: 30th April & 31st October]

Date	Particulars	Nominal Value(₹)	Interest (₹)	Cost (₹)	Date	Particulars	Nominal Value (₹)	Interest (₹)	Cost (₹)
1.4.20	To Bank A/c (W.N.1)	4,00,000	16,667	2,63,333	30.4.20	By Bank A/c (4,00,000 x 10% x 6/12)	-	20,000	-
1.10.20	To Profit & Loss A/c (W.N 5)			7,333	1.10.20	By Bank A/c (W.N.2)	80,000	3,333	60,000
					31.10.20	By Bank A/c	-	16,000	-
31.3.21	To Profit & Loss A/c		35,999		31.3.21	By Balance c/d (W.N.3)	3,20,000	13,333	2,10,666
		4,00,000	52,666	2,70,666			4,00,000	52,666	2,70,666

Investment in Equity Shares of XY Ltd. Account (of ₹ 5 each)

Date	Particulars	No.	Dividend (₹)	Cost (₹)	Date	Particulars	No.	Dividend (₹)	Cost (₹)
1.4.20	To Bank A/c	6,000		1,26,000	15.1.21	By Bank A/c	8,000		80,000
15.1.21	To Bonus Issue	8,000			1.3.21	By Bank A/c (W.N.6)		4,950	1,650
15.1.21	To Profit & Loss A/c.			8,000					

	(W.N.4)								
31.3.21	To Profit & Loss A/c		4,950		31.3.21	By Balance c/d	6,000		52,350
		14,000	4,950	1,34,000			14,000	4,950	1,34,000

Working Notes:

1. Cost of investment purchased on 1st April, 2020

4,000, 10% Govt. loan were purchased @ ₹ 70 cum-interest. Total amount paid 4,000 bonds x ₹ 70 = 2,80,000 which includes accrued interest for 5 months, i.e., 1st November, 2020 to 31st March, 2021. Accrued interest will be ₹ 4,00,000 x 10% x 5/12 = ₹ 16,667. Therefore, cost of investment purchased = ₹ 2,80,000 – ₹ 16,667 = ₹ 2,63,333.

2. Sale of 10% Govt. loan on 1st October, 2020

800, 10% Govt. loan were sold@ ₹ 75 ex-interest, i.e., Total amount received = 800 x 75 + accrued interest for 5 months = ₹ 60,000 + ₹ 3333

3. Cost of 10% Govt. loan on 31.3.2021

Cost of 10% Govt. loan on 31.3.2021 will be ₹ 2,63,333 x 3,20,000/4,00,000 = ₹ 2,10,666.

Interest accrued on 10% Government Loan on 31.3.2021 = ₹ 3,20,000 x 10% x 5/12 = ₹ 13,333

4. Profit on sale of bonus shares

Cost per share after bonus = ₹ 1,26,000/ 14,000 = ₹ 9 (average cost method being followed)

Profit per share sold (₹ 10 – ₹ 9) = ₹ 1.

Therefore, total profit on sale of 8,000 shares = 8,000 x ₹ 1 = ₹ 8,000.

5. Profit on sale of 10% Govt. loan

		₹
Sale value	=	60,000
Cost of ₹ 80,000 10% Government Loan = 2,63,333 x 80,000/ 4,00,000	=	52,667
Profit	=	7,333

6. Dividend on equity shares = 6,000 x 5 x 22% = ₹ 6,600 out of which ₹ 1,650 will be treated as capital receipt as it has been received for the period of 3 months during which shares were not held.

Note: It has been considered that dividend received relates for the period of 12 months ended 31st Dec., 2020, strictly based on the information, given in the question. Hence, dividend received for the period of 3 months (1st January, 20 to 31st March, 20) has been treated as pre-acquisition.

Question 3

(a) *Delta Ltd. has a branch at Kanpur. Goods are invoiced from head office to Branch at cost plus 50%. Branch remits all cash received to head office and all expenses are met by head office.*

Prepare necessary Ledger accounts in the books of Delta Ltd. under Stock and Debtors system to show profit earned at the branch for the year ending 31st March, 2021.

Following information related to Branch is given:

Stock on 1st April, 2020 (Invoice price)	31,200	Goods returned by Debtors	3,000
Debtors on 1st April, 2020	17,400	Surplus in stock (Invoice price)	600
Goods invoiced at cost	72,000	Expenses at Branch	13,400
Sales at Branch: Cash sales	20,000	Discount allowed to Debtors	700
Credit sales	68,200	Debtors on 31st March, 2021	14,300

(b) *M/s Wee has two Departments X and Y. From the following particulars, Prepare Departmental Trading Account and Consolidated Trading Account for the year ending 31st March, 2021.*

Particulars	Department X ₹	Department Y ₹
Opening stock (at Cost)	1,40,000	1,08,000
Purchases	4,28,000	3,32,000
Carriage inwards	12,000	12,000
Carriage outwards	5,000	4,000
Wages	42,000	48,900
Sales	5,70,000	4,74,000
Purchased goods transferred by Dept. Y to Dept. X	60,000	-
Purchased goods transferred by Dept. X to Dept. Y	-	48,000
Finished goods transferred by Dept. Y to Dept. X	1,60,000	-
Finished goods transferred by Dept. X to Dept. Y	-	2,00,000
Closing Stock of Purchased Goods	24,000	30,000
Closing Stock of Finished Goods	1,54,000	1,20,000

Purchased goods have been transferred mutually at their respective departmental purchase cost and finished goods at departmental market price and that 15% of the finished stock (closing) at each department represented finished goods received from the other department. **(10 + 10 = 20 Marks)**

Answer

(a) **Books of Delta Ltd.**

Kanpur Branch Stock Account

	₹		₹
To Balance b/d – Opening Stock	31,200	By Bank A/c – Cash Sales	20,000
To Branch Debtors A/c – Sales Return	3,000	By Branch Debtors A/c - Credit Sales	68,200
To Goods sent to Branch A/c (72,000 +50% of 72,000)	1,08,000	By Balance c/d - Closing stock	54,600
To Surplus in stock	600		
	1,42,800		1,42,800

Kanpur Branch Stock Adjustment Account

	₹		₹
To Branch Profit and Loss Account	28,400	By Balance b/d (1/3 of ₹ 31,200)	10,400
To Balance c/d (1/3 of 54,600)	18,200	By Goods sent to Branch A/c (1/3 of ₹ 1,08,000)	36,000
		By Surplus in stock	200
	46,600		46,600

Goods Sent to Branch Account

	₹		₹
To Kanpur Branch Stock Adjustment A/c	36,000	By Kanpur Branch Stock A/c	1,08,000
To Purchases A/c	72,000		
	1,08,000		1,08,000

Branch Debtors Account

	₹		₹
To Balance b/d	17,400	By Bank (Bal fig.)	67,600
To Branch Stock A/c	68,200	By Branch Expenses A/c (Discount allowed)	700
		By Branch Stock - Sales Returns	3,000

		By Balance c/d	14,300
	85,600		85,600

Branch Expenses Account

	₹		₹
To Bank A/c (expenses)	13,400	By Branch Profit & Loss A/c (Transfer)	14,100
To Branch Debtors A/c (Discount allowed)*	700		
	14,100		14,100

Branch Profit & Loss Account for the year ending 31st March 2021

	₹		₹
To Branch Expenses A/c	14,100	By Branch Adjustment A/c	28,400
To Net Profit	14,700	By surplus in stock (Cost)	400
	28,800		28,800

Note: * Discount allowed to debtors may be shown in Branch Profit and Loss account directly instead of transferring it through Branch Expenses account.

(b) **M/s Wee**

Departmental Trading A/c for the year ending 31st March, 2021

	Deptt. X. ₹	Deptt. Y ₹		Deptt. X. ₹	Deptt. Y ₹
To Stock	1,40,000	1,08,000	By Sales	5,70,000	4,74,000
To Purchases	4,28,000	3,32,000	By Purchased Goods transferred	48,000	60,000
To Wages	42,000	48,900	By Finished goods transferred	2,00,000	1,60,000
To Carriage inward	12,000	12,000	By Closing Stock:		
To Purchased Goods			Purchased Goods	24,000	30,000
transferred	60,000	48,000	Finished Goods	1,54,000	1,20,000
To Finished Goods transferred	1,60,000	2,00,000			
To Gross profit c/d (b.f.)	1,54,000	95,100			
	9,96,000	8,44,000		9,96,000	8,44,000

Consolidated Trading Account for the year ending 31st March 2021

	₹		₹
To Opening Stock	2,48,000	By Sales	10,44,000
To Purchases	7,60,000	By Closing Stock:	
To Wages	90,900	Purchased Goods	54,000
To Carriage inward	24,000	Finished Goods	2,74,000
To Stock Reserve*	7,065		
To Gross Profit c/d	2,42,035		
	13,72,000		13,72,000

Working Note:

	Deptt. X	Deptt. Y
Sale	5,70,000	4,74,000
Add: Transfer	2,00,000	1,60,000
Net Sales plus Transfer	7,70,000	6,34,000
Rate of Gross profit	1,54,000/7,70,000 x 100 = 20%	95,100/6,34,000 x 100 = 15%
Closing Stock out of transfer (15% of closing stock)	1,54,000 x 15% = 23,100	1,20,000 x 15% = 18,000
Unrealized Profit	23,100 × 15% = 3,465	18,000 × 20% = 3,600

Note: *Stock reserve has been shown separately in the above solution and the closing stock has been given at the full value without reducing stock reserve from it. Alternatively, stock reserve may not be shown and the closing stock can be shown at the net amount (after deducting amount of stock reserve).

Question 4

The following is the summarized Balance Sheet of R Limited as at 31st March, 2021:

	₹
Liabilities	
Authorized Capital	
1,50,000 Equity shares of ₹ 10 each	*15,00,000*
30,000 10% Redeemable Preference shares of ₹ 100 each	*30,00,000*
	45,00,000
Issued, subscribed and paid up	
90,000 Equity shares of ₹ 10 each	*9,00,000*
15,000 10% Redeemable Preference shares of ₹ 100 each	*15,00,000*

Reserves & Surplus	
Securities Premium	*18,00,000*
General Reserve	*16,50,000*
Profit & Loss A/c	*1,20,000*
7500, 9% Debentures of ₹ 100 each	*7,50,000*
Trade Payables	*2,12,500*
	69,32,500
Assets	
Non-Current Assets	
Property Plant & Equipment	*31,60,000*
Investments (Market Value, ₹ 17,40,000)	*14,70,000*
Trade Receivables	*17,60,000*
Cash & Bank Balance	*5,42,500*
	69,32,500

In Annual General Meeting held on 15th May, 2021 the company passed the following resolutions:

(i) To redeem 10% preference shares at a premium of 5%.

(ii) To redeem 9% Debentures by making offer to Debenture holders to convert their holding into equity shares at ₹ 40 per share or accept cash on redemption.

(iii) To issue fully paid bonus shares in the ratio of one equity share for every three shares held on 31st March, 2021.

(iv) Redemption of preference shares and debentures will be paid through company's cash & bank balance subject to leaving a minimum cash & bank balance of ₹ 2,00,000.

(v) To issue sufficient number of equity shares @ ₹ 40 per share if required to finance redemption of Preference Shareholders and debenture holders.

On 5th June, 2021 investments were sold for ₹ 16,80,000 and preference shares were redeemed.

30% of Debenture holders exercised their option to accept cash and their claims were settled on 1st August, 2021. The bonus issue was concluded by 10th August, 2021.

You are requested to journalize the above transactions including cash transactions and prepare Balance Sheet as at 30th September, 2021. All working notes should form part of your answer. ***(20 Marks)***

Answer

Journal Entries in the Books of R Limited

		₹	₹
June 5	Cash & Bank A/c Dr.	16,80,000	
	To Investment A/c		14,70,000
	To Profit & Loss A/c		2,10,000
	(Being investment sold out and profit on sale credited to Profit & Loss A/c)		
June 5	10% Redeemable preference share capital A/c	15,00,000	
	Premium on redemption of pref. share A/c Dr.	75,000	
	To Preference shareholders A/c		15,75,000
	(Being amount payable to preference shareholders on redemption)		
June 5	Preference shareholders A/c Dr.	15,75,000	
	To Cash & bank A/c		15,75,000
	(Being amount paid to preference shareholders)		
June 5	General reserve* A/c Dr.	15,00,000	
	To Capital redemption reserve A/c		15,00,000
	(Being amount equal to nominal value of preference shares transferred to Capital Redemption Reserve A/c on its redemption as per the law)		
Aug. 1	9% Debentures A/c Dr.	7,50,000	
	Interest on debentures A/c (₹ 7,50,000 x 9% x 4/12)	22,500	
	To Debenture holders A/c		7,72,500
	(Being amount payable to debenture holders along with interest payable)		
Aug. 1	Debenture holders A/c Dr.	7,72,500	
	To Cash & bank A/c (2,25,000 + 22,500)		2,47,500
	To Equity share capital A/c (13,125 X₹ 10)		1,31,250
	To Securities premium A/c (13,125 x ₹ 30)		3,93,750
	(Being claims of debenture holders satisfied) (refer W.N.1)		
Aug. 10	Capital Redemption Reserve A/c Dr.	3,00,000	

	To Bonus to shareholders A/c		3,00,000
	(Being balance in capital redemption reserve capitalized to issue bonus shares)		
Aug. 10	Bonus to shareholders A/c Dr.	3,00,000	
	To Equity share capital A/c		3,00,000
	(Being 30,000 fully paid equity shares of ₹ 10 each issued as bonus in ratio of 1 share for every 3 shares held)		
Sept.30	General Reserve* A/c Dr.	75,000	
	To Premium on redemption of preference shares A/c		75,000
	(Being premium on preference shares adjusted from general reserve)		
Sept.30	Profit & Loss A/c Dr.	22,500	
	To Interest on debentures A/c		22,500
	(Being interest on debentures transferred to Profit and Loss Account)		

Balance Sheet as at 30th September, 2021

		Particulars	Notes	₹
		Equity and Liabilities		
1		Shareholders' funds		
	a	Share capital	1	13,31,250
	b	Reserves and Surplus	2	37,76,250
2		Current liabilities		
	a	Trade Payables		2,12,500
		Total		53,20,000
		Assets		
1		Non-current assets		
	a	Property, Plant and Equipment		31,60,000
2		Current assets		
	a	Trade receivables		17,60,000
	b	Cash and bank balances (W.N.2)		4,00,000
		Total		53,20,000

* Alternatively, Profit & Loss A/c may also be used for the amount available.

Notes to accounts:

		₹	₹
1	**Share Capital**		
	Authorized share capital		
	1,50,000 Equity shares of ₹ 10 each	15,00,000	
	30,000 Redeemable Preference shares of ₹ 100 each	30,00,000	
	Issued, subscribed and paid up		
	1,33,125 Equity shares of ₹ 10 each [90,000+13,125+30,000] (Out of which 1,33,125 shares were issued for the consideration other than cash)		13,31,250
2	**Reserves and Surplus**		
	Securities Premium		
	Balance as per balance sheet	18,00,000	
	Add: Premium on equity shares issued on conversion of debentures (13,125 x 30)	3,93,750	
	Balance		21,93,750
	Capital Redemption Reserve (15,00,000 - 3,00,000)		12,00,000
	General Reserve		
	Opening Balance 16,50,000		
	Less Transfer to Capital Redemption Reserve (15,00,000)		
	1,50,000		
	Less: Premium on redemption of preference shares (75,000)		75,000
	Profit & Loss A/c	1,20,000	
	Add: Profit on sale of investment	2,10,000	
	Less: Interest on debentures	(22,500)	3,07,500
	Total		37,76,250

Working Notes:

		₹
1.	**Redemption of Debentures**	
	7,500 Debentures of ₹ 100 each	7,50,000
	Less: Cash option exercised by 30% holders	(2,25,000)
	Conversion option exercised by remaining 70%	5,25,000
	Equity shares issued on conversion = 5,25,000/40 = 13,125 shares	

2.	**Cash and Bank Balance**	
	Balance as per balance sheet	5,42,500
	Add: Realization on sale of investment	16,80,000
		22,22,500
	Less: Paid to preference share holders	(15,75,000)
	Paid to Debenture holders (2,25,000 + 22,500)	(2,47,500)
	Balance	4,00,000

Note:

1. There is no need to issue fresh equity shares as the company is having sufficient cash balance.
2. Securities premium has not been utilized for the purpose of premium payable on redemption of preference shares assuming that the company referred in the question is governed by Section 133 of the Companies Act, 2013 and comply with the Accounting Standards prescribed for them. Alternative considering otherwise also possible by utilizing securities premium.

Question 5

(a) Peek Ltd. was incorporated on 01.07.2020 to take over the existing business of Rich & Co. with effect from 01.04.2020. Date of closing books of accounts is 31.03.2021.

Total sales were ₹ 75,00,000, Rate of Gross profit is 10% on sales.

The expenses charged to profit and loss statement include:

Salesmen's Commission	*₹ 30,000*
Discount Allowed	*₹ 15,000*
Carriage outward	*₹ 45,000*
Free Sample	*₹ 60,000*
After sales service charge	*₹ 90,000*
Directors' fees	*₹ 1,50,000*
Audit fees (Statutory audit of company)	*₹ 70,000*
Tax audit fees to Chartered Accountant	*₹ 15,000*
Salary to general staff	*₹ 16,000*
Formation Expenses	*₹ 30,000*
Rent (Office Building)	*₹ 27,000*
General Expenses	*₹ 48,000*
Donation to political party	*₹ 51,000*
General travelling Expenses	*₹ 60,000*

The sales per month in the first half year were half of what they were in the later half year.

Rent of office building was paid @ ₹ 2,000 p.m. upto 30th September, 2020 and thereafter it was increase by ₹ 500 p.m.

Prepare a statement showing pre incorporation & post incorporation profit for the year ended 31.03.2021 and also compute the amount to be transferred to capital reserve account.

(b) ABC Ltd. acquired a Machine on hire purchase from P Ltd. with term of payment in four equal annual installments. The annual installment is commencing from the date of agreement signed by both the parties.

The payment of annual installment is ₹ 25,000 at the end of each year. The interest is charged @ 25% and is included in the annual installment. ABC Ltd. could not pay third annual installment and declared "Purchaser Defaulted" whereupon P Ltd. acted to repossess the Machinery.

ABC Ltd. is providing depreciation on Machinery at the rate of 20% per annum on the diminishing balance method.

You are required to prepare Machinery Account and P Ltd. account in the books of ABC Ltd. Working notes will form part of the answer. ***(12 + 8 = 20 Marks)***

Answer

(a) (i) Statement showing calculation of profits for pre and post incorporation periods for the year ended 31.3.2021

Particulars	Basis of allocation	*Pre-incorporation period* ₹	*Post-incorporation period* ₹
Gross profit	Sales	1,25,000	6,25,000
Less: Salesmen commission	Sales	5,000	25,000
Discount allowed	Sales	2,500	12,500
Carriage outwards	Sales	7,500	37,500
Free samples	Sales	10,000	50,000
After sale service charges	Sales	15,000	75,000
Director's fee (post-incorporation)	Post	--	1,50,000
Company Audit fee	Post	--	70,000
Tax audit fee	Sales	2,500	12,500
Salaries	Time	4,000	12,000
Formation Expenses	Post	--	30,000

Rent (office building)	W.N. 3	6,000	21,000
General expenses	Time	12,000	36,000
Donation to political party (assumed to be paid by company)	Post	--	51,000
General Travelling expenses	Sales	10,000	50,000
Net profit/loss (Bal. Fig.)		50,500	(7,500)

(ii) **Transfer to capital reserve** = Pre incorporation profit is treated as capital profit, hence amount transfer to capital reserve is ₹ 50,500.

Working Notes:

1. Time Ratio

Pre incorporation period = 1st April, 2020 to 30th June, 2020 i.e. 3 months

Post incorporation period is 9 months

Time ratio is 1: 3.

2. Sales ratio

Let the monthly sales for first 6 months (i.e from 1.4.2020 to 30.09.2020) be x

Monthly sales for next 6 months (i.e. from 1.10.20 to 31.3.2021) = 2x

Sales in the pre incorporation period =3x

Total sales for post-incorporation period =3x+12x=15x

Sales Ratio = 1 : 5

3. Rent

		₹
Rent for pre-incorporation period (₹ 2,000 x 3)		6,000 (pre)
Rent for post incorporation period		
July, August& September, 2020 (₹ 2,000 x 3)	6,000	
October,2020 to March,2021 (₹ 2,500 x 6)	15,000	21,000 (post)

Note:

1. General Travelling expenses have been divided on the basis of turnover ratio. Alternatively, it may be divided on time basis (1:3).
2. In the above solution, it has been assumed as donation is paid by the company. Alternatively, it can be divided in time ratio also.

(b) **In the books of ABC Ltd.**

Machinery Account

		₹			₹
I Yr.	To Hire Vendor A/c (W.N.)	73,800	I Yr.	By Depreciation A/c	14,760
				By Balance c/d	59,040
		73,800			73,800
II Yr.	To Balance b/d	59,040	II Yr.	By Depreciation A/c	11,808
				By Balance c/d	47,232
		59,040			59,040
III Yr.	To Balance b/d	47,232	III Yr.	By Depreciation A/c	9,446
				By Hire Vendor	25,000
				By Profit and Loss A/c (Loss on surrender) (Balancing figure)	12,786
		47,232			47,232

P Ltd. Account

		₹			₹
I Yr.	To Bank A/c (1st Installment)	25,000	I Yr.	By Machinery A/c	73,800
End of year	To Bank A/C (2nd Installment)	25,000			
	To Balance c/d	36,000		By Interest A/c	12,200
		86,000			86,000
II Yr.	To Bank A/c (3rd Installment)	25,000	II Yr.	By Balance b/d	36,000
	To Balance c/d	20,000		By Interest A/c	9,000
		45,000			45,000
III Yr.	To Machinery A/c (transfer)	25,000	III Yr.	By Balance b/d	20,000
				By Interest A/c	5,000
		25,000			25,000

Working Note:

		Installment Amount	*Interest*	*Principal*
4th Installment		25,000	₹	₹
Interest	25,000 x 25/125	5,000	5,000	20,000
		20,000		
Add: 3rd Installment		25,000		
		45,000		
Interest	45,000 x 25/125	9,000	9,000	16,000
		36,000		
Add: 2nd Installment		25,000		
		61,000		
Interest	61,000 x 25/125	12,200	12,200	12,800
		48,800		
Add: 1st Installment (Down Payment)		25,000		25,000
		73,800	26,200	73,800

Note: In the question, it is given that “the annual instalment is commencing from the date of agreement signed by both the parties. The payment of annual instalment ₹ 25,000 at the end of each year”. It has been assumed in the above answer that first instalment is paid on the date of agreement and rest instalments are paid at the end of each year. Alternative answer assuming that the first instalment is paid at the end of first year is also possible. The solution under this assumption will get changed and will be given as follows:

Machinery Account

		₹			₹
I Yr.	To Hire Vendor A/c (W.N.)	59,040	I Yr.	By Depreciation A/c	11,808
				By Balance c/d	47,232
		59,040			59,040
II Yr.	To Balance b/d	47,232	II Yr.	By Depreciation A/c	9,446
				By Balance c/d	37,786
		47,232			47,232
III Yr.	To Balance b/d	37,786	III Yr.	By Depreciation A/c	7,557
	To Profit and Loss A/c (profit on surrender) (Balancing figure)	14,771		By Hire Vendor	45,000
		52,557			52,557

P Ltd. Account

		₹			₹
I Yr.	To Bank A/c	25,000	I Yr.	By Machinery A/c	59,040
	To Balance c/d	48,800		By Interest A/c	14,760
		73,800			73,800
II Yr.	To Bank A/c	25,000	II Yr.	By Balance b/d	48,800
	To Balance c/d	36,000		By Interest A/c	12,200
		61,000			61,000
III Yr.	To Machinery A/c (transfer)	45,000	III Yr.	By Balance b/d	36,000
				By Interest A/c	9,000
		45,000			45,000

Working Note:

		Instalment Amount	*Interest*	*Principal*
4th Instalment		25,000	₹	₹
Interest	25,000 x 25/125	5,000	5,000	20,000
		20,000		
Add: 3rd Instalment		25,000		
		45,000		
Interest	45,000 x 25/125	9,000	9,000	16,000
		36,000		
Add: 2nd Instalment		25,000		
		61,000		
Interest	61,000 x 25/125	12,200	12,200	12,800
		48,800		
Add: 1st Instalment		25,000		
		73,800		
Interest	73,800 x 25/125	14,760	14,760	10,240
		59,040	40,960	59,040

Question 6

Answer any ***four*** *of the following:*

(a) *Mrs. A is showing the consolidated aggregate opening balance of equity, liabilities and assets of ₹ 6 lakh, 4 lakh and 10 lakh respectively. During the current year Mrs. A has the following transactions:*

1. *Received 20% dividend on 10,000 equity shares of ₹ 10 each held as investment.*

2. *The amount of ₹ 70,000 is paid to creditors for settlement of ₹ 90,000.*
3. *Salary is pending by ₹ 20,000.*
4. *Mrs. A's drawing ₹ 20,000 for her personal use.*

You are required to prepare the statement of the effect of aforesaid each transaction on closing balance sheet in the form of Assets – Liabilities = Equity after each transaction.

(b) *X Ltd. a non investment company has been incurring losses for the past few years. The company provides the following information for the current year:*

	₹ in lakhs
Paid up equity share capital	*90*
Paid up preference share capital	*10*
Reserves (including revaluation reserve ₹ 5 lakhs)	*75*
Securities premium	*30*
Long term loans	*20*
Deposit repayable after one year	*10*
Application money pending allotment	*360*
Accumulated losses not written off	*40*
Investment	*90*

X Ltd. has only one whole time director, Mr. Y. You are required to calculate the amount of maximum remuneration that can be paid to him if no special resolution is passed at the general meeting of the company in respect of payment of remuneration for a period not exceeding three years.

(c) *What is meant by 'Measurement'? What are the bases of measurement of Elements of Financial Statements? Explain the brief.*

(d) *A Company had issued 25,000, 12% Debentures of ₹ 100 each on 1st April, 2018. The Debentures were due for redemption on 1st July, 2020. The terms of issue of Debentures provided that they will be redeemable at a premium of 5% and also conferred option to convert 20% of their holding into equity Shares (Nominal value ₹ 10 each) at a price of ₹ 20 per share.*

Debenture holders holding 5,000 Debentures did not exercise the option. Calculate the number of Equity shares to be allotted to the debenture holders exercising the option to the maximum.

(e) *A company sold 20% of the Goods on Cash Basis and the balance on Credit basis. Debtors are allowed 1.5 month's credit and their balance as on 31st March, 2021 is ₹ 1,50,000. Assume that sale is evenly spread throughout the year.*

Purchases during the year ₹ 9,50,000

Closing stock is ₹ 10,000 less than the Opening Stock. Average stock maintained during the year ₹ 60,000

Direct Expenses amounted to ₹ 35,000

Calculate Credit sales, Total sales and Gross profit for the year ended 31st March, 2021.

(4 Parts x 5 Marks = 20 Marks)

Answer

(a) Effect of each transaction on Balance sheet of Mrs. A is shown below:

Transactions	*Assets ₹ lakh*	–	*Liabilities ₹ lakh*	=	*Equity ₹ lakh*
Opening	10.00	–	4.00	=	6.00
(1) Dividend earned	10.20 [10.00+0.20]	–	4.00	=	6.20 [6.00+0.20]
(2) Settlement of Creditors	9.50 [10.20-0.70]	-	3.10 [4.00-0.90]	=	6.40 [6.20+0.20]
(3) Salary Outstanding	9.50	–	3.30 [3.10+0.20]	=	6.20 [6.40-0.20]
(4) Drawings	9.30 [9.50-0.20]	–	3.30	=	6.00 [6.20-0.20]

(b) Calculation of effective capital and maximum amount of managerial remuneration

	(₹ In lakhs)
Paid up equity share capital	90
Paid up Preference share capital	10
Reserve excluding Revaluation reserve (75 – 5)	70
Securities premium	30
Long term loans	20
Deposits repayable after one year	10
	230
Less: Accumulated losses not written off	(40)
Investments	(90)
Effective capital for the purpose of managerial remuneration	100

Since X Ltd. is incurring losses and no special resolution has been passed by the company for payment of remuneration, managerial remuneration will be calculated on the basis of effective capital of the company as the effective capital is less than 5 crores. Therefore, maximum remuneration payable to the Managing Director should be @ ₹ 60,00,000 per annum.

Note: Revaluation reserve, and application money pending allotment are not included while computing effective capital of Kumar Ltd.

(c) Measurement is the process of determining money value at which an element can be recognized in the balance sheet or statement of profit and loss. The Framework for Preparation and Presentation of Financial statements recognizes four alternative measurement bases for the purpose of determining the value at which an element can be recognized in the balance sheet or statement of profit and loss.

These bases are: (i) Historical Cost; (ii) Current cost (iii) Realizable (Settlement) Value and (iv) Present Value.

A brief explanation of each measurement basis is as follows:

1. **Historical Cost**: Historical cost means acquisition price. According to this, assets are recorded at an amount of cash or cash equivalent paid or the fair value of the asset at the time of acquisition. Liabilities are generally recorded at the amount of proceeds received in exchange for the obligation.
2. **Current Cost:** Current cost gives an alternative measurement basis. Assets are carried out at the amount of cash or cash equivalent that would have to be paid if the same or an equivalent asset was acquired currently. Liabilities are carried at the undiscounted amount of cash or cash equivalents that would be required to settle the obligation currently.
3. **Realizable (Settlement) Value:** As per realizable value, assets are carried at the amount of cash or cash equivalents that could currently be obtained by selling the assets in an orderly disposal. Liabilities are carried at their settlement values, i.e. the undiscounted amount of cash or cash equivalents paid to satisfy the liabilities in the normal course of business.
4. **Present Value**: Under present value convention, assets are carried at present value of future net cash flows generated by the concerned assets in the normal course of business. Liabilities under this convention are carried at present value of future net cash flows that are expected to be required to settle the liability in the normal course of business.

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

	Number of debentures
Total number of debentures	25,000
Less: Debenture holders not opted for conversion	(5,000)
Debenture holders opted for conversion	20,000
Option for conversion	20%
Number of debentures to be converted (20% of 20,000)	4,000

Redemption value of 4,000 debentures at a premium of 5% [4,000 x (100+5)]	₹ 4,20,000
Equity shares of ₹ 10 each issued on conversion [₹ 4,20,000/ ₹ 20]	21,000 shares

(e) Calculation of Credit Sales, Total Sales and Gross Profit

Credit Sales for the year ended 31st March, 2021 = Debtors x $\frac{12\text{ months}}{1.5\text{ months}}$

= ₹ 1,50,000 x $\frac{12\text{ months}}{1.5\text{ months}}$

= ₹ 12,00,000

Total sales for the year ended 2020 -21 = Credit sales x $\frac{100\%}{80\%}$

= ₹ 12,00,000 x $\frac{100\%}{80\%}$

= ₹ 15,00,000

Trading Account for the year ended 31st March, 2021

	₹		₹
To Opening stock	65,000	By Sales	15,00,000
To Direct expenses	35,000	By Closing Stock	55,000
To Purchases	9,50,000		
To Gross profit	5,05,000		
	15,55,000		15,55,000

Working Note:

Calculation of opening stock and closing stock

If closing stock is x then opening stock is x+10,000

Average stock ₹ 60,000

Average stock = Opening stock + Closing stock /2

Thus Opening stock is ₹ 65,000 and closing stock is ₹ 55,000.