# SUGGESTED ANSWERS

## INTERMEDIATE EXAMINATION

(SYLLABUS - 2008)

December 2010

# GROUP I



THE INSTITUTE OF
COST AND WORKS ACCOUNTANTS OF INDIA
12, SUDDER STREET, KOLKATA– 700 016

# SUGGESTED ANSWERS
# TO
# QUESTIONS

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**GUIDELINES TO STUDENTS**

1. **Students are advised to consult Study Notes and Text Books supplemented by the Suggested Answers.**
2. **Working Notes should be a part of Answers, particularly in Financial Accounting and Applied Direct Taxation.**
3. **Assumptions should be logical and clearly stated in the Answers.**



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## GROUP -I (DECEMBER 2010)



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# INTERMEDIATE EXAMINATION

## GROUP I

(SYLLABUS 2008)

# SUGGESTED ANSWERS TO QUESTIONS

## DECEMBER 2010

# Paper-5 : FINANCIAL ACCOUNTING

**Time Allowed :** 3 Hours **Full Marks :** 100

*The figures in the margin on the right side indicate full marks.*

*Answer* **Question No. 1**, *which is compulsory and* **any five** *questions from the rest.*

**Q. 1. (a) State whether the following statements are True (T) or False (F) :** 1×5=5

(i) Preference shares may be redeemed from the securities premium

(ii) Life membership fee may be capitalized and shown in Balance Sheet in liabilities side

(iii) R and S divided profit in the ratio of 3 : 2. T is admitted for 1/5the share in the business. The new profit sharing ratio will be 3 : 2 : 1.

(iv) As per AS-2 inventory is valued at the lower of net realizable value and current replacement cost.

(v) The Contract of insurance is a contract of guarantee.

**(b) Fill up the blanks :** 1×5=5

(i) Excess of hire purchase price over ________ is treated as hire purchase charges.

(ii) Excess of minimum rent over royalties is termed as ________ .

(iii) Balance of preliminary expenses account is shown in Company's Balance Sheet under the head of ________ on assets side.

(iv) The "Average Clause" is applicable when the actual loss is ________ than the sum assured.

(v) Turnover ratios are also known as ________ ratios.

**(c) Explain the following in single sentences** 1×5=5

(i) Stock Turnover ratio

(ii) Net Realisable value

(iii) Personal Accounts

(iv) Buy Back of shares

(v) Price Earning ratio

**(d)** State the method of preparing Cash Flow statement. 3

**(e)** What reconciliation entry will be required to be passed in the books of Head office when cash sent by the Branch to Head Office at the end of accounting year has not reached the Head Office? 2

**(f)** From the four alternatives given against each statement, choose the correct alternative : 1×5=5

(i) In the absence of an agreement amongst the partners, loan given by a partner to the firm will be at an interest at the rate of

(A) 5% (B) 6% (c) 8% (D) 10%

(ii) Depreciation accounting is a process of

(A) Apportionment

(B) Valuation

(C) Allocation

(D) Appropriation

(iii) Which of the following is a Capital Expenditure

(A) Freight and cartage on purchase of new machine

(B) Legal expenses in connection with defending a title to firm's propery

(C) Expenditure on painting of factory shed

(D) Wages paid to machine operatior

(iv) AS-6 is related to :

(A) Valuation of inventories

(B) Accounting for Construction Contracts

(C) Cash Flow Statements

(D) Depreciation accounting

(v) As per Section 17 of Banking Companies Act, an Indian Banking company prior to declaration of dividend must transfer to reserve fund the following percentage of profit

(A) 10% (B) 20% (C) 25% (D) 30%

**Answer 1. (a)**

(i) False

(ii) True

(iii) False

(iv) False

(v) False

**Answer 1. (b)**

(i) Cash Price

(ii) short working

(iii) Miscelleneous Expenditure

(iv) More

(v) velocity

**Answer 1. (c)**

(i) Ratio of cost of goods sold to average stock to measure acitivity and general efficiency of the firm.

(ii) Represents the estimated selling price in ordinary couses of business less estimated cost to bring the item in saleable condition.

(iii) Accounts dealing with transaction relating to persons or an organization.

(iv) A company repurchasing its own shares to increase earning per share.

(v) Ratio of market price per share to earning per share and used to ascertain true value of each equity share.

**Answer 1. (d)**

There are two methods of preparing Cash Flow statements — (1) Direct Method and (2) Indirect Method. Under the direct method, cash receipts (inflows) from operating revenues and cash payments (outflows) for operating expenses are calculated to arrive at cash flows from operating activities. The difference between the cash receipts & cash payment is to the net cash flow provided by operating activities.

Under indirect method, the net cash flow from operating activities is determined by adjusting net profit or loss for the effect of :-

(i) Non cash items such as depreciation, provisions etc.

(ii) Changes during the period in inventories & operating receivables and payables

(iii) All other items for which the cash effects are investing or financing cash flows.



**Answer 1. (e)**

In case of Debtor system :

Cash in Transit A/c Dr.
To Branch A/c

In case of Stock and Debtor System :

Cash in Transit A/c Dr.
To Branch Cash A/c

**Answer 1. (f)**

(i) (B) 6%

(ii) (C) Allocation

(iii) (A) Freight and cartage on purchase of new machine

(iv) (D) Depreciation accounting

(v) (B) 20%

**Q. 2. (a)** Ravi purchased a machine on hire purchase system from Moon & Sons. He paid Rs. 100000 at the time of agreement and the remaining amount including interest was payble in four annual instalments of Rs. 100000 each at the end of each year commencing from the date of agreement. Interest is charged @ 10% per annum.

You are required to prepare the Machinery Account and Moon & Sons account in the books of Ravi for four years if he provides depreciation on machinery @ 20 percent per annum on written down value basis. 10

**(b) Match the following :**

| | | |
|---|---|---|
| (i) AS-3 | (1) | Accounting for Research and Development |
| (ii) AS-7 | (2) | Revenue Recognition |
| (iii) AS-9 | (3) | Accounting for Construction Contracts |
| (iv) AS-8 | (4) | Cash Flow Statements |
| (v) AS-5 | (5) | Contingencies and Events Occuring after Balance Sheet date |

5

**Answer 2. (a)**

**Calculation of Interest and Cash Price**

| Instalment | Amount of instalment | Amount Payable at the time of instalment | Interest | Amount Payable after instalment |
|---|---|---|---|---|
| IV | 1,00,000 | 1,00,000 | $1{,}00{,}000 \times \frac{10}{110}$ = 9,091 | 90,909 |
| III | 1,00,000 | 1,00,000 + 90,909 = 1,90,909 | $1{,}90{,}909 \times \frac{10}{110}$ = 17,355 | 1,73,554 |
| II | 1,00,000 | 1,00,000 + 1,73,554 = 2,73,554 | $2{,}73{,}554 \times \frac{10}{110}$ = 24,869 | 2,48,685 |
| I | 1,00,000 | 1,00,000 + 2,48,685 = 3,48,685 | $3{,}48{,}685 \times \frac{10}{110}$ = 31,699 | 3,16,986 |

Total Interest = 9,091 + 17,355 + 24,869 + 31,699

= Rs. 83,014

Hire Purchase Price = 1,00,000 + (1,00,000 × 4) = Rs. 5,00,000

Cash Price = Rs. 5,00,000 – Rs. 83,104 = Rs. 4,16,986

**Ledger of Ravi**
**Machinery Account**

| Date | Particulars | Amount Rs. | Date | Particulars | Amount Rs. |
|---|---|---|---|---|---|
| I Year Beginning | To Moon & Sons | 4,16,986 | I Year End | By Depreciation | 83,397 |
| | | | " | By Balance c/d | 3,33,589 |
| | | 4,16,986 | | | 4,16,986 |
| II Year Beginning | To Balance b/d | 3,33,589 | II Year End | By Depreciation | 66,718 |
| | | | " | By Balance c/d | 2,66,871 |
| | | 3,33,589 | | | 3,33,589 |
| III Year Beginning | To Balance b/d | 2,66,871 | III Year End | By Depreciation | 53,374 |
| | | | " | By Balance c/d | 2,13,497 |
| | | 2,66,871 | | | 2,66,871 |
| IV Year Beginning | To Balance b/d | 2,13,497 | IV Year End | By Depreciation | 42,699 |
| | | | " | By Balance c/d | 1,70,798 |
| | | 2,13,497 | | | 2,13,497 |

**Moon & Sons Account**

| Date | Particulars | Amount Rs. | Date | Particulars | Amount Rs. |
|---|---|---|---|---|---|
| I Year Beginning | To Bank A/c | 1,00,000 | I Year Beginning | By Machinery A/c | 4,16,986 |
| End | To Bank A/c | 1,00,000 | End | By Interest A/c | 31,699 |
| " | To Balance c/d | 2,48,685 | | | |
| | | 4,48,685 | | | 4,48,685 |
| II Year End | To Bank A/c | 1,00,000 | II Year Beginning | By Balance b/d | 2,48,685 |
| " | To Balance c/d | 1,73,554 | End | By Interest A/c | 24,869 |
| | | 2,73,554 | | | 2,73,554 |
| III Year End | To Bank A/c | 1,00,000 | III Year Beginning | By Balance b/d | 1,73,554 |
| " | To Balance c/d | 90,909 | End | By Interest A/c | 17,355 |
| | | 1,90,909 | | | 1,90,909 |
| IV Year End | To Bank A/c | 1,00,000 | IV Year Beginning | By Balance c/d | 90,909 |
| | | | " | By Interest A/c | 9,091 |
| | | 1,00,000 | | | 1,00,000 |

**Answer 2. (b)**

(i) AS - 3 (4) Cash Flow Statements.

(ii) AS - 7 (3) Accounting for Construction Contracts

(iii) AS - 9 (2) Revenue Recognition

(iv) AS - 8 (1) Accounting for Research and Development

(v) AS - 5 AS-5 relates to Net Profit or Loss for the period, prior period items and changes in Accounting policies. Contingencies and events occuring after Balance Sheet date falls under AS-4 and not AS-5 as given in question paper.

**Q. 3. (a)** KC Limited has declared 15 percent dividend 'on equity-share capital of Rs. 2000000 (divided into shares of Rs. 100 each) for the year ending 31 st March, 2010 and despatched dividend warrants on 18th July, 2010 by opening a separate bank account on the day. A person holding 800 equity shares did not claim the amount of his share of dividend.

What journal entries will be passed in the books of the company for declaration and the despatch of dividend warrants and transferring the unclaimed amount to Unclaimed Dividend Account? What further journal entry will be passed in the books of the company when the unclaimed amount is not claimed by the claiment within stipulated time U/S 205(A)(5) of 7 years. Corporate dividend tax may be taken at 17 percent (gross) 8

**(b)** From the following information prepare a statement of Proprietor's Fund :

(i) Current ratio 2.5; (ii) Liquid ratio 1.5; (iii) Proprietory ratio (Fixed Assets/Proprietory Fund) 0.75; (iv) Working capital Rs. 90,000; (v) Reserves and Surplus Rs. 60,000 (vi) Bank Overdraft Rs. 20,000; (vii) There is no long term loan or fictitious assets. 7

**Answer 3. (a)**

**Journal of KC Limited**

| | | | | |
|---|---|---|---|---|
| 2010 July 18 | Proposed Equity Share Dividend A/c | Dr. | 3,00,000 | |
| | To Equity Share Dividend A/c | | | 3,00,000 |
| | (Being payment of dividend) | | | |
| " | Provision for Dividend Tax A/c | Dr. | 51,000 | |
| | To Dividend Tax A/c | | | 51,000 |
| | (Being provision for tax on dividend) | | | |
| " | Dividend Bank A/c | Dr. | 3,00,000 | |
| | To Bank A/c | | | 3,00,000 |
| | (Being transfer of dividend amount to Division Bank A/c) | | | |
| " | Equity Share Dividend A/c | Dr. | 3,00,000 | |
| | To Dividend Bank A/c | | | 3,00,000 |
| Date of Div. Tax paid | Dividend Tax A/c | Dr. | 51,000 | |
| | To Bank A/c | | | 51,000 |
| | (Being payment of Dividend tax) | | | |

| | | | | |
|---|---|---|---|---|
| Date of transfer upto 17.8.10 | Dividend Bank A/c<br>To Unclaimed Dividend A/c<br>(Being unclaimed amount of dividend transferred to Unclaimed Dividend Account) | Dr. | 12,000 | 12,000 |
| Date of opening of un-paid Div. Bank A/c | Unpaid Dividend Bank Account of KC Limited<br>To Dividend Bank A/c<br>(Being transfer unpaid Dividend to seperate Bank A/c) | Dr. | 12,000 | 12,000 |
| At the time of expiry u/s 205 (A)(5) i.e. on 17.8.10 | Unclaimed Dividend A/c<br>To Unpaid Dividend Bank Account of KC Limited<br>(Amount deposited IEPF as required by section 205(A)(5) of Companies Act, 1956) | Dr. | 12,000 | 12,000 |

**Answer 3. (b)**

(i) Current Ratio (CR) = $\frac{\text{Current Asset}}{\text{Current Liabilities}} = \frac{CA}{CL} = 2.5$

$CA = 2.5\ CL$

Working Capital $= CA - CL =$ Rs. 90,000

or, $2.5\ CL - CL =$ Rs. 90,000

or, $1.5\ CL =$ Rs. 90,000

or, $CL = 60,000$

or, $CA = 2.5 \times 60,000 = 1,50,000$

Quick Ratio (QR) = $\frac{\text{Quick Assets (QA)}}{CL} = 1.5$

$QA = 1.5\ CL$

$QA = 1.5 \times 60,000 =$ Rs. 90,000

Stock = CA – QA = 1,50,000 – 90,000 = Rs. 60,000

Proprietors Fund (PF)

PF + CL = Fixed Asset (FA) + CA

PF – FA = CA – CL

$\frac{FA}{PF} = .75$ or $FA = .75\ PF$

$PF - .75\ PF =$ Rs. 90,000

$.25\ PF = 90,000$

$PF = 3,60,000$

(vi) Share Capital :

Proprietor's fund – Reserves and surplus

Rs. 3,60,000 – Rs. 60,000 = Rs. 3,00,000.

(vii) Statement of Proprietor's Fund

| | |
|---|---|
| Share Capital – | Rs. 3,00,000 |
| Reserve and Surplus | 60,000 |
| | 3,60,000 |

**Q. 4. (a)** The following (i) Receipts and Payments Account for 2009-10; (ii) Balance Sheet as on 31st March, 2009 and other information are given by the Shiva City College :-

(i) Receipts and Payments Account for the year ended 31st March, 2010

| | Rs. | | Rs. |
|---|---|---|---|
| To Opening Balance | 6,00,000 | By Salary & Allowances | 21,15,000 |
| To Tuition fees | 18,00,000 | By Provident Fund Contribution | 1,66,200 |
| To Grant | 9,00,000 | By Printing & Stationery | 51,000 |
| To Interest on Bank FD. | 9,000 | By Books for Library | 78,000 |
| To Hall Rent | 30,000 | By Postage & Telegram | 15,000 |
| | | By Newspapers | 9,000 |
| | | By Laboratory Equipments | 29,400 |
| | | By Telephone Expenses | 25,000 |
| | | By Repairs for Building | 32,000 |
| | | By Misc. Charges | 18,000 |
| | | By Audit Fee | 10,000 |
| | | By Creditors for out standing | 21,000 |
| | | By Bank Fixed Deposit | 4,00,000 |
| | | By Closing Balances | 3,69,400 |
| | 33,39,000 | | 33,39,000 |

(ii) Balance Sheet as on 31st March, 2009.

| Liabilities | Rs. | Assets | Rs. |
|---|---|---|---|
| Outstanding Exp | 21,000 | Cash and Bank | 6,00,000 |
| Building Fund | 18,00,000 | Furniture | 10,50,000 |
| Scholarship Fund | 3,00,000 | Land and Building | 48,00,000 |
| General Reserves | 15,00,000 | Tuition Fee (Outstanding) | 66,000 |
| Capital Fund | 39,15,000 | Library Books | 7,20,000 |
| | | Fixed Deposit in Bank | 3,00,000 |
| | 75,36,000 | | 75,36,000 |

(iii) Other information:

(1) It was ascertained that Rs. 1,70,000 was outstanding by way of tuition fees on 31.03.2010

(2) The creditors outstanding for library books amounted to Rs. 30,000 at the end of the financial year 2009-10.

(3) Outstanding salaries were Rs. 90,000 as on 31.3.10

(4) Depreciation to be charged: Land and Building at 5%, Furniture at 10%, and Library Books at 20%. You are required to prepare for Shiva City College;

(a) Income and Expenditure Account for the year ended 31 st March, 2010

(b) Balance Sheet as on 31st March, 2010

(b) Describe how the classification of investments is done by a Banking Company 10

**(b)** Describe how the classification of investments is done by a Banking Company. 5

**Answer 4. (a)**

**Income and Expenditure Account of Shiva City College for the year ended 31st March, 2010**

| Expenditure | | Amount Rs. | Income | Amount Rs. |
|---|---|---|---|---|
| To Salary & Allowances (21,1,5000 + 90,000) | | 22,05,000 | By Tuition fee (18,00,000 – 66,000+1,70,000) | 19,04,000 |
| To P. F. Contribution | | 1,66,200 | By Grant | 9,00,000 |
| To Printing & Stationery | | 51,000 | By Interest on F.D. | 9,000 |
| To Postage & Telegram | | 15,000 | By Hall Rent | 30,000 |
| To Newspoapers | | 9,000 | By Excess of Expenditure over income | 1,98,800 |
| To Telephone Expenses | | 25,000 | | |
| To Repair for Building | | 32,000 | | |
| To Misc. Charges | | 18,000 | | |
| To Audit Fee | | 10,000 | | |
| To Depreciation : | | | | |
| Land & Building | 2,40,000 | | | |
| Furniture | 1,05,000 | | | |
| Library Books | 1,65,600 | 5,10,600 | | |
| | | 30,41,800 | | 30,41,800 |

**Balance Sheet of Shiva City College as on 31.3.2010**

| Liabilities | | Amount Rs. | Assets | Amount Rs. |
|---|---|---|---|---|
| Capital Fund : | 39,15,000 | | Land & Building | |
| *Less* : Excess of Exp. | | | (48,00,000-2,40,000) | 45,60,000 |
| over Income | 1,98,800 | 37,16,200 | Furniture (10,50,000–1,05,000) | 9,45,000 |
| Building Fund | | 18,00,000 | Library Books | 6,62,400 |
| Scholarship Fund | | 3,00,000 | (7,20,000+1,08,000–1,65,600) | |
| General Reserve | | 15,00,000 | Laboratory Equipments | 29,400 |
| Outstanding Salary | | 90,000 | Fixed Deposit in Bank | |
| Creditors for Library Books | | 30,000 | (3,00,000+4,00,000) | 7,00,000 |
| | | | Outstanding Tuition Fee | 1,70,000 |
| | | | Cash and Bank | 3,69,400 |
| | | 74,36,200 | | 74,36,200 |

**Working Note :**

1. Addition in Library Books during the year Rs. 78,000 (Paid) + Rs. 30,000 (Outstanding) = Rs. 1,08,000.
2. Laboratory Equipment is treated Capital in nature.

**Answer 4. (b)**

The investment portfolio of a Bank would normally consist of both approved securities (predominantly government securities) and other securities (shares, debentures, bonds etc.). Banks are required to classify their entire investment portfolio into three categories.

(i) Held-to-maturity : Securities acquired by bank with the intention to hold them up to maturity should be classified as 'held-to-maturity'.

(ii) Held-for-maturity : Securities required by bank with the intention to trade by taking advantage of short term price interest rate movements should be classified as held-for-maturity/trading.

(iii) Available -for-sale : Securities which do not fall within the above two catetgories should be classified as available-for-sale.

**Q. 5. (a)** Asha, Bipasa and Chitra are partners in a partnership firm sharing profits and losses as 8:7:5. From 1.4.09 the partners decided to change their profit sharing ratio as 5:4: 1 and for that purpose the following adjustments were agreed upon.

Balance Sheet of the firm As on 31.3.2009 was as under.

(Fig. in Rs.)

| Liabilities | | | Assets | | |
|---|---|---|---|---|---|
| Capital A/cs. | | | Plant & Machinery | | 80,000 |
| Asha | 50,000 | | Furniture | | 10,000 |
| Bipasha | 40,000 | | Stock | | 40,000 |
| Chitra | 30,000 | 1,20,000 | Trade Debtors | 52,000 | |
| Reserves | | 30,000 | Less Provision | (–) 2,000 | 50,000 |
| B's loan | | 20,000 | Bank | | 30,000 |
| Trade creditors | | 40,000 | | | |
| | | 2,10,000 | | | 2,10,000 |

(i) Furniture and Machinery were to be depreciated and appreciated by 5% and 10% respectively.

(ii) Provision for bad debts was to be increased by Rs. 3000.

(iii) P & L. A/c. of the firm for the year ended 31.3.10 showed a net profit of Rs. 68,700.

(iv) A contingent liability ofRs. 10,000 was to be treated as actual liability.

The partners decided not to alter the book values of the assets, liabilities and reserves but recorded the change by passing one single journal entry.

You are required—

(a) to show a single journal entry adjusting the capitals of the partners as on 1-4-09, and

(b) to show the P. & L. A./c. for the year ended 31.3.10 after considering the following adjusments :

(i) Interest on capital at 5%,

(ii) Interest on B's loan and

(iii) transfer 20% of the divisible profit to the reserves after charging such reserve. 10

**(b)** State the various accounting concepts. 5

**Answer 5. (a)**

**Memorandum Revaluation Account**

**(Fig. in Rs.)**

| | | | | | |
|---|---|---|---|---|---|
| To Provision for bad debts | | 3,000 | By Machinery | | 8,000 |
| To Furniture | | 500 | By Reserves | | 30,000 |
| To Contingent liability | | 10,000 | | | |
| Profits : | | | | | |
| Asha | 9,800 | | | | |
| Bipasa | 8,575 | | | | |
| Chitra | 6,115 | 24,500 | | | |
| | | 38,000 | | | 38,000 |
| To Reversal of itmes | | 8,000 | By Reversal of items | | 13,500 |
| Reserves | | 30,000 | By Profit written | | |
| | | | back | A - 5/10 | 12,250 |
| | | | | B - 4/10 | 9,800 |
| | | | | C - 1/10 | 2,450 |
| | | 38,000 | | | 38,000 |

Net adjustment :

| | Cr. | Dr. | Net |
|---|---|---|---|
| A - | 9,800 | 12,250 | – 2,450 |
| B - | 8,575 | 9,800 | – 1,225 |
| C - | 6,125 | 2,450 | + 3,675 |

| | | | |
|---|---|---|---|
| Asha | Dr. | 2,450 | |
| Bipasa | Dr. | 1,225 | |
| To Chitra | | | 3,675 |

**P & L Account for the year ended 31.3.10**

| Particulars | | Amount Rs. | Particulars | Amount Rs. |
|---|---|---|---|---|
| To Interest on capital – | | | By Balance b/d | 68,700 |
| A - 5% on (50,000 – 2,450) | | 2,378 | | |
| B - 5% on (40,000 – 1,225) | | 1,938 | | |
| C - 5% on (30,000 + 3,575) | | 1,684 | | |
| To Interest on B's loan @ 6% | | 1,200 | | |
| To Reserves 61500 × 20/120 | | 10,250 | | |
| Profit – | | | | |
| A 5/10 | 25,625 | | | |
| B 4/10 | 20,500 | | | |
| C 1/10 | 5,125 | 51,250 | | |
| | | 68,700 | | 68,700 |

**Answer 5. (b)**

Various accounting concepts are as follows :

1. Money measurement concept
2. Dual aspect concept.
3. Going concern concept.
4. Periodicity concept.
5. Accrual concept.
6. Matching concept.
7. Realisation concept.
8. Materiality concept.
9. Consistency concept.
10. Business entity concept.
11. Historical cost concept.

**Q. 6. (a)** Credential General Insurance Co. supplies you the following information. You are asked to show the amount of claim as it would appear in the Revenue Account for the year ended 31.3.2010.

| | | Direct business Rs. | Indirect business Rs. |
|---|---|---|---|
| Claims paid during the year : | | 90,10,000 | 12,40,000 |
| Claims payable - | 1.4.09 | 15,08,500 | 1,55,000 |
| | 31.3.10 | 17,25,000 | 65,500 |
| Claims received : | | – | 3,60,000 |
| Claims receivable- | 1.04.09 | – | 95,000 |
| | 31.3.10 | – | 1,90,500 |
| Expenses of the management - (included Rs. 61,500 as Surveyo's fees and Rs. 78,300 as legal expenses for settlement of claims) | | 4,10,000 | |

**(b)** A limited company finds that the stock sheets as on 31.3.2010 had included an item twice, the cost of which was Rs. 50,000

You are asked to suggest, how the error would be dealt with in the accounts for the year ended on 31.3.2010. 2

**(c)** While preparing the financial statements of X Co.Ltd, for the year ended 31.12.2009, you came across the following information. State with reasons, how you would deal with them in the financial statements;

There was a major theft of stores valued at Rs. 20 lakhs in the preceding year which was detected only during the current accounting year ended on 31.12.2009 3

**Answer 6. (a)**

**Credential General Insurance Co.**

(Abstract showing the amount of claims)

| | | |
|---|---|---|
| Claim less insurance : | | (fig in Rs.) |
| Paid during the year | 1,00,23,800 | |
| *Add* : Outstanding claims at the end of the year | 16,00,000 | |
| | 1,16,23,800 | |
| *Less* : Outstanding claims at the beginning of the year | 15,68,500 | 1,00,55,300 |

**Workings :**

| | | |
|---|---|---|
| 1. Claims paid during the year : | | |
| Direct business | 90,10,000 | |
| Re-Insurance | 12,40,000 | 1,02,50,000 |
| *Add* : Surveyor's fees | 61,500 | |
| Legal expenses | 72,300 | 1,33,800 |
| | | 1,03,83,800 |
| *Less* : Claims received from Re-insurance | | 3,60,000 |
| | | 1,00,23,800 |
| 2. Claims outstanding on 31.3.10 : | | |
| Direct business | 17,25,000 | |
| Re-insurance | 65,500 | 17,90,500 |
| *Less* : Claims receivable from Re-insurance | | 1,90,500 |
| | | 16,00,000 |
| 3. Claims outstanding on 1.4.09 : | | |
| Direct business | 15,08,500 | |
| Re-insurance | 1,55,000 | 16,63,500 |
| *Less* : Claims receivable from Re-insurance | | 95,000 |
| | | 15,68,500 |

**Answer 6. (b)**

According to AS-5, rectification of error in stock valuation is a Prior Period Item. It is necessary to deduct Rs. 50,000 from Opening Stock in the Profit and Loss Account for the year ended 30.3.10. However, it is also necessary to charge Rs. 50,000 as prior period adjustment in the Profit and Loss Account "below the line". AS-5 requires seperate disclosure of such Prior Period Items.

**Answer 6. (c)**

The major theft of stores in the preceding year 2008, detected only during the current financial year 2009, caused overstatement of closing stock of stores in the preceding year. This must have also resulted in the overstatement of profits of previous year, brought forward to the current year. The adjustments are required to be made in the current year as 'Prior Period Item' as per AS-5 (Revised), "Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies". As such the adjustments relating to both opening stock of the current year and profit brought forward from the previous year should be separately disclosed in the statement of profit and loss together with their nature and amount in a manner that their impact on the current profit and loss can be perceived.

Alternatively, it can be assumed that in the preceding year, the value of stock of stores was found out by physical verification of stocks and that was considered in the preparation of financial statements of the preceding year. In such a situation, only the disclosure as to the theft and the consequential loss is required in the notes to the accounts for the current year i.e. year ended 31.12.2009.

**Q. 7. (a)** Calcutta Head Office has its branch at Kanpur. Goods are invoiced to Branch at cost plus $33\frac{1}{3}$%. All expenses of the Branch are paid by the H.O. From the following particulars you are required to show Branch Stock A/c., Branch Adjustments A/c., Loss in Transit A/c., PilferageAlc. and Branch P. & L. A/c. in the books of H.O.

| | Rs. |
|---|---|
| Opening stock at branch at cost to branch | 60,000 |
| Goods sent to branch at invoice price | 1,30,000 |
| Loss in transit at invoice price | 20,000 |
| Goods pilfered at Branch - (at invoice price) | 6,000 |
| Normal loss at invoice price | 3,000 |
| Sales (Credit) | 2,20,000 |
| Expenses of branch | 35,000 |
| Recovered from Insurance Co. against loss in transit | 12,000 |
| Closing stock at Branch at invoice price | 80,500 |

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**(b)** Define Computer Software and explain what should be the period of amortisation of the computer software. 5

**Answer 7. (a)**

**In the Books of Calcutta Head Office** (fig in Rs.)

**Branch Stock Account**

*Dr.* *Cr.*

| Particulars | Amount Rs. | Particulars | Amount Rs. |
|---|---|---|---|
| To Balance b/d | 60,000 | By Sales | 2,20,000 |
| To Goods sent to Br. | 1,30,000 | By Loss in Transit | 20,000 |
| To Branch Adjustment A/c (Apparent G.P.) | 1,39,500 | By Pilferage | 6,000 |
| | | By Br. Adjustment A/c (normal loss) | 3,000 |
| | | By Balance c/f | 80,500 |
| | 3,29,500 | | 3,29,500 |

Dr. **Branch Adjustment Account** Cr.

| Particulars | Amount Rs. | Particulars | Amount Rs. |
|---|---|---|---|
| To Br. Stock (normal loss) | 3,000 | By Balance b/f (Branch Stock) (¼×60,000) | 15,000 |
| To Loss in transit (20000×¼) | 5,000 | By Goods sent to Branch (¼×130000) | 32,500 |
| To Pilferage (60000×¼) | 1,500 | By Br. Stock (App. G.P.) | 1,39,500 |
| To Gross profit (bal. fig.) | 1,57,375 | | |
| To Balance Stock (80500×¼) | 20,125 | | |
| | 1,87,000 | | 1,87,000 |

Dr. **Loss in Transit Account** Cr.

| Particulars | Amount Rs. | Particulars | Amount Rs. |
|---|---|---|---|
| To Branch Stock | 20,000 | By Br. Adjustment A/c | 5,000 |
| | | By Bank (Ins. claim) | 12,000 |
| | | By Branch P & L A/c | 3,000 |
| | 20,000 | | 20,000 |

Dr. **Pilferage Account** Cr.

| Particulars | Amount Rs. | Particulars | Amount Rs. |
|---|---|---|---|
| To Branch Stock | 6,000 | By Br. Adjustment A/c | 1,500 |
| | | By P & L A/c | 4,500 |
| | 6,000 | | 6,000 |

Dr. **Branch Profit & Loss Account** Cr.

| Particulars | Amount Rs. | Particulars | Amount Rs. |
|---|---|---|---|
| To Expenses | 35,000 | By Br. Adjustment A/c | 1,57,375 |
| To Loss in Transit | 3,000 | | |
| To Pilferage | 4,500 | | |
| To Gen. P & L A/c | 1,14,875 | | |
| | 1,57,375 | | 1,57,375 |

**Note :** Loading is $33\frac{1}{3}$% of cost i.e. 25% of Invoice Price.

**Answer 7. (b)**

Software is the general term describing programmes of instructions, languages and routines or procedures that make it possible for an individual to use the computer. It is any prepared set of instructions that controls the operations of the computer for computation and processing. Computer Software that are used internally may be (i) acquired, or (ii) internally generated.

The depreciable amount of a software should be allocated on a systematic basis over the best estimate of its useful life. The amortisation should commence when the software is available for use. As per AS-26, there is a presumption that the useful life of an intangible asset should not exceed ten years from the date when the asset is available for use. However, due to phenomenal changes in the technology, computer software is susceptible to technological obsolescence. Therefore, it is prudent to consider the useful life of the software much shorter than ten years, may be between 3 to 5 years.

**Q. 8. Write short notes on any three :** 3×5=15

(a) Non-Banking Assets

(b) Disclosures neccessary under AS-7

(c) Features of Financial Accounts and Balance Sheet of non-profit seeking organisations.

(d) Contingent liability.

**Answer 8. (a)**

**Non-banking assets :**

A Bank cannot acquire certain assets but it can always lend against the security of such assets. This means that sometimes, in case of failure on the part of the loanee to repay the loans, the bank may have to take possession of such assets. In that case, the assets will be shown in the balance sheet as "Non-banking Assets". These must be disposed of within seven years. Income from or profit/loss on sale such assets has to be separately shown in profit and loss account of the bank.

**Answer 8. (b)**

A. Under AS-7 relating to Accounting for Construction Contracts an enterprise should disclose :

(a) The amount of contract revenue recognised as revenue in the period.

(b) Methods used to determine the contract revenue recognised in the period.

(c) Method used to determine the state of completion of contract in progress.

B. An enterprise should disclose the following for contracts in progress at the reporting date.

(1) The aggregate amount of costs incurred and recognised profit less recognised losses upto reporting date.

(2) The amount of advance received and amount retained.

C. An enterprise should present :

(a) Gross amount due from customer is an asset.

(b) Gross amount due to customer is a liability.

(c) Contingencies as per AS-4 (warranty cost, penalties, guarantee issued by Banks against counter indemnity of contractor).

**Answer 8. (c)**

Certain concerns like Clubs, Charitable Institutions do not intend to earn profit. They render service to the society or to their members. Their members do not get any share of profit or dividend. These concerns are known as non-profit organisations. Their transactions are service based not profit based. Their annual accounts are prepared regularly to convey their financial affairs to their members or others like Government to obtain grants and financial aids. In smalll concerns the Accounts are kept in Single Entry System. In Big concerns complete double entry system is followed and Recepts & Payments Account, Income & Expenditure Account and Balance sheets are prepared.

**Answer 8. (d)**

Contingent Liability means "a obligation to an existing condition or situation which may arise in future depending the occurance or non-occurance of one or more uncertain events."

For example, there may be a pending litigation against the company. It becomes a liability if the decision goes against the company and the company is called upon to pay damages to the other party. On other hand if the judgement goes in the company's favour, the company neednot pay anything. Similarly a company may contest the assessments made by tax authorities relating to I.T., Sales Tax, Excise etc. In all such cases the amount involved in appeal are shown as contingent liabilities.

Schedule VI classifies contingent liabilities under the following heads :-

(1) Claims against company not acknowledged as debts.

(2) Uncalled liability on partly paid shares.

(3) Arrears of fixed cumulative dividend

(4) Estimated amounts of contracts remaining to be executed on Capital A/c not provided for;

(5) Other money for which the company is liable.

The contingent liabilities are shown as footnote to Balance sheet.