

ANSWER OF MODEL TEST PAPER 6
INTERMEDIATE COURSE: GROUP – I
PAPER – 1 : ADVANCED ACCOUNTING
ANSWERS

1. (a) (iii)
 (b) (i)
 (c) (ii)
 (d) (iii)
2. (a) (ii)
 (b) (iii)
 (c) (iii)
 (d) (i)
3. (a) (iii)
 (b) (iii)
 (c) (ii)
 (d) (iv)
4. (ii)
5. (i)
6. (iv)

PART II – Descriptive Questions (70 Marks)

1. (a) Provision to be made for warranty under AS 29 'Provisions, Contingent Liabilities and Contingent Assets'

$$\begin{aligned} \text{As at 31}^{\text{st}} \text{ March, 2023} &= ₹ 60,000 \times .02 + ₹ 40,000 \times .03 \\ &= ₹ 1,200 + ₹ 1,200 = ₹ 2,400 \end{aligned}$$

$$\begin{aligned} \text{As at 31}^{\text{st}} \text{ March, 2024} &= ₹ 40,000 \times .02 + ₹ 1,35,000 \times .03 \\ &= ₹ 800 + ₹ 4,050 = ₹ 4,850 \end{aligned}$$

Amount debited to Profit and Loss Account for year ended 31st March, 2024

	₹
Balance of provision required as on 31.03.2024	4,850
Less: Opening Balance as on 1.4.2023	<u>(2,400)</u>
Amount debited to profit and loss account	<u>2,450</u>

Note: No provision will be made on 31st March, 2024 in respect of sales amounting ₹ 60,000 made on 11th February, 2022 as the warranty period of 2 years has already expired.

- (b) As per AS 26 “Intangible Assets”, subsequent expenditure on an intangible asset after its purchase or its completion should be recognized as an expense when it is incurred unless (a) it is probable that the expenditure will enable the asset to generate future economic benefits in excess of its originally assessed standard of performance; and (b) expenditure can be measured and attributed to the asset reliably. If these conditions are met, the subsequent expenditure should be added to the cost of the intangible asset.
- (i) In the given case, the legal expenses to defend the patent of a product amounting ₹ 23,00,000 should not be capitalized and be charged to Profit and Loss Statement.
 - (ii) The company is required to expense the entire amount of ₹ 7,00,000 in the Profit and Loss account for the year ended 31st March, 2024 because no benefit will arise in the future.
 - (iii) As per AS 26, expenditure on an intangible item that was initially recognized as an expense by a reporting enterprise in previous annual financial statements should not be recognized as part of the cost of an intangible asset at a later date. Thus, the company cannot capitalize the amount of ₹ 25,00,000 and it should be recognized as expense
 - (iv) Expenditure of ₹ 50,00,000 on advertising and promotional activities should always be charged to Profit and Loss Statement. Hence, the company has done the correct treatment by debiting the sum of 50 lakhs to Profit and Loss Account.
- (c) (1) Trade discounts and volume rebates received are not encompassed within the definition of revenue, since they represent a reduction of cost. Trade discounts and volume rebates given should be deducted in determining revenue.
- (2) When goods are sold to distributor or others, revenue from such sales can generally be recognized if significant risks of ownership have passed; however, in some situations the buyer may in substance be an agent and in such cases the sale should be treated as a consignment sale.
- (3) For transactions, where seller concurrently agrees to repurchase the same goods at a later date that are in substance a financing agreement, the resulting cash inflow is not revenue as defined and should not be recognized as revenue.
- (4) Insurance agency commissions should be recognized on the effective commencement or renewal dates of the related policies.

- (5) On 11.03.2024, if X mart takes title and accepts billing for the goods then it is implied that the sale is complete and all risk and reward on ownership has been transferred to the buyers.

Revenue should be recognized for year ended 31st March, 2024 notwithstanding that physical delivery has not been completed so long as there is every expectation that delivery will be made and items were ready for delivery to the buyer at the time.

2.

MN Limited

Balance Sheet as at 31st March, 2024

Particulars		Note No.	(₹ in 000)
Equity and Liabilities			
1.	Shareholders' funds		
	A Share capital	1	300
	B Reserves and Surplus	2	530
2.	Non-Current liabilities		
	A Long term borrowings	3	200
3.	Current liabilities		
	A Trade Payables		<u>52</u>
	Total		<u>1082</u>
Assets			
1.	Non-current assets		
	A PPE (Property, Plant & Equipment)	4	880
2.	Current assets		
	A Inventories		86
	B Trade receivables		96
	C Cash and bank balances		<u>20</u>
	Total		<u>1082</u>

MN Limited

Statement of Profit and Loss for the year ended 31st March, 2024

	Particulars	Notes	(₹ in 000)
I.	Revenue from operations		700
II.	Other Income	5	<u>2</u>
III.	Total Income		<u>702</u>
IV.	Expenses:		
	Purchases		320
	Finance costs	6	20

	Depreciation (10% of 760*)		76
	Other expenses	7	<u>120</u>
	Total Expenses		<u>536</u>
V.	Profit (Loss) for the period (III – IV)		166

Notes to accounts

			(₹ in 000)
1.	Share Capital		
	Equity share capital		
	Authorised		
	40,000 shares of ₹ 10 each		<u>400</u>
	Issued & subscribed & called up		
	30,000 shares of ₹ 10 each		300
2.	Reserves and Surplus		
	Securities Premium Account		40
	Revaluation reserve (360 – 220)		140
	General reserve		130
	Profit & loss Balance		
	Opening balance	72	
	Profit for the period	<u>166</u>	238
	Less: Appropriations		
	Interim Dividend	(18)	<u>220</u>
			<u>530</u>
3.	Long term borrowing		
	10% Debentures		200
4.	PPE		
	Land		
	Opening balance	220	
	Add: Revaluation adjustment	<u>140</u>	
	Closing balance		360
	Plant and Machinery		
	Opening balance	770	
	Less: Disposed off	(10)	
		760	
	Less: Depreciation (172-8+76)	(240)	
	Closing balance		520

* 770 (Plant and machinery at cost) – 10 (Cost of plant and machinery sold)

	Total		880
5. Other Income			
Profit on sale of machinery:			
Sale value of machinery		4	
Less: Book value of machinery (10-8)		(2)	2
6. Finance costs			
Debenture interest			20
7. Other expenses:			
Factory expenses		60	
Selling expenses		30	
Administrative expenses		<u>30</u>	120

Note: The final dividend will not be recognized as a liability at the balance sheet date (even if it is declared after reporting date but before approval of the financial statements) as per Accounting Standards. Hence, it has not been recognized in the financial statements for the year ended 31 March, 2024. Such dividends will be disclosed in notes only.

3. (a)
$$\frac{\text{Fair value of shares immediately prior to exercise of rights} + \text{Total amount received from exercise}}{\text{Number of shares outstanding prior to exercise} + \text{Number of shares issued in the exercise}}$$

$$\frac{102 \times 2,50,000 \text{ Shares} + ₹ 98 \times 1,00,000 \text{ shares}}{3,50,000 \text{ shares}}$$

Theoretical ex-rights fair value per share = ₹ 100.86

Computation of adjustment factor:

$$\frac{\text{Fair value per share prior to exercise of rights}}{\text{Theoretical ex - rights value per share}} = 102/100.86 = 1.01$$

Computation of earnings per share:

EPS for the year 2022-23 as originally reported: ₹ 50,00,000/2,50,000 shares = ₹ 20

EPS for the year 2022-23 restated for rights issue: = ₹ 50,00,000/(2,50,000 shares x 1.01)

$$= ₹ 19.80$$

EPS for the year 2023-24 including effects of rights issue:

$$\text{EPS} = 75,00,000/3,25,625^* = ₹ 23.03$$

$$* [(2,50,000 \times 1.01 \times 3/12) + (3,50,000 \times 9/12)] = 63,125 + 2,62,500 = 3,25,625 \text{ shares}$$

Note: Financial year (ended 31st March) is considered as accounting year while giving the above answer.

(b)

In the books of Fortunate Ltd.

Journal Entries

	Particulars		Debit (₹)	Credit (₹)
1.	Equity share capital A/c (₹ 50) Dr. To Equity share capital A/c (₹ 5) To Capital reduction A/c* (Being equity capital reduced to nominal value of ₹ 5 each)		9,37,500	93,750 8,43,750
2.	Bank A/c Dr. To Equity share capital (Being 3 right shares against each share was issued and subscribed)		2,81,250	2,81,250
3.	8% Preference share capital A/c (₹ 50) Dr. Capital reduction A/c Dr. To 6% Preference share capital (₹ 10) To equity share capital (Being 8% preference shares of ₹ 50 each converted to 6% preference shares of ₹ 10 each and also given to them 3 equity shares for every share held)		7,50,000 75,000	6,00,000 2,25,000
4.	Loan A/c Dr. To 6% Preference share capital A/c (15,000 x ₹ 10) To Equity share capital A/c (7,500 x ₹ 5) (Being loan to the extent of ₹ 1,50,000 converted into share capital)		1,87,500	1,50,000 37,500
5.	Bank A/c (25,000 x ₹ 5) Dr. To Equity share application A/c (Being shares subscribed by the directors)		1,25,000	1,25,000
6.	Equity share application A/c Dr. To Equity share capital A/c (Being application money transferred to capital A/c)		1,25,000	1,25,000

7.	Loan A/c To Bank A/c (Being loan repaid)	Dr.	2,50,000	2,50,000
8.	Capital reduction A/c To Profit and loss A/c To Plant A/c To Trademarks and Goodwill A/c (Bal. fig.) (Being losses and assets written off to the extent required)	Dr.	7,68,750	5,63,750 43,750 1,61,250

**Balance sheet of Fortunate Ltd. (and reduced)
as on 31.3.2024**

		Particulars	Notes	₹
1		Equity and Liabilities		
		Shareholders' funds		
	a	Share capital	1	15,12,500
2		Non-current liabilities		
	a	Long-term borrowings (7,16,250 – 1,87,500 – 2,50,000)		2,78,750
3		Current liabilities		
	a	Trade Payables		2,58,750
	b	Other current liabilities		<u>43,750</u>
		Total		<u>20,93,750</u>
		Assets		
1		Non-current assets		
	a	Property, Plant and Equipment	2	7,91,250
	b	Intangible assets	3	2,36,250
2		Current assets		
	a	Inventories		5,00,000
	b	Trade receivables		4,10,000
	c	Cash and cash equivalents	4	<u>1,56,250</u>
		Total		<u>20,93,750</u>

Notes to accounts:

			₹
1	Share Capital		
	Authorized capital:		
	81,250 Preference shares of ₹ 10 each	8,12,500	

	1,87,500 Equity shares of ₹ 5 each Issued, subscribed and paid up:	<u>9,37,500</u>	<u>17,50,000</u>
	1,52,500 equity shares of ₹ 5 each (out of the above 52,500 shares issued for consideration other than cash)	7,62,500	
	75,000, 6% Preference shares of ₹ 10 each	<u>7,50,000</u>	15,12,500
2	Property, Plant and Equipment		
	Building at cost less depreciation	5,00,000	
	Plant at cost less depreciation	<u>2,91,250</u>	7,91,250
3.	Intangible assets		
	Trademarks and goodwill		2,36,250
4	Cash and cash equivalents		
	Bank (2,81,250+1,25,000-2,50,000)		1,56,250

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In the Books of Y Ltd. Realisation Account

		₹			₹
To Sundry Assets:			By Retirement Gratuity Fund		60,000
Goodwill	75,000		By Trade payables		2,40,000
Land & Building	3,00,000		By X Ltd. (Purchase Consideration)		15,90,000
Plant & Machinery	4,50,000				
Inventory	5,25,000				
Trade receivables	3,00,000				
Bank	<u>60,000</u>	17,10,000			
To Preference Shareholders (Premium on Redemption)		30,000			
To Equity Shareholders (Profit on Realisation)		<u>1,50,000</u>			
		<u>18,90,000</u>			<u>18,90,000</u>

Balance Sheet of X Ltd. (after absorption) as at 31st March, 2024

Particulars		Notes	₹
1	Equity and Liabilities		
	Shareholders' funds		
A	Share capital	1	48,30,000
B	Reserves and Surplus	2	2,70,000

2	Non-current liabilities		
A	Long-term provisions	3	2,10,000
3	Current liabilities		
A	Trade Payables	4	6,10,000
B	Short term provision	5	7,500
	Total		59,27,500
	Assets		
1	Non-current assets		
A	Fixed assets		
	Tangible assets	6	33,00,000
	Intangible assets	7	3,00,000
2	Current assets		
A	Inventories	8	12,22,500
B	Trade receivables	9	8,80,000
C	Other current Assets	10	15,000
D	Cash and cash equivalents	11	<u>2,10,000</u>
	Total		59,27,500

Notes to accounts

		₹
1	Share Capital	
	Equity share capital	
	4,20,000 Equity Shares of ₹ 10 each fully paid (Out of above 1,20,000 Equity Shares were issued in consideration other than for cash)	42,00,000
	Preference share capital	
	6,300 9% Preference Shares of ₹ 100 each (Out of above 3,300 Preference Shares were issued in consideration other than for cash)	6,30,000
	Total	48,30,000
2	Reserves and Surplus	
	Securities Premium	60,000
	General Reserve	2,10,000
	Total	2,70,000
3	Long-term provisions	
	Retirement Gratuity fund	2,10,000
4	Trade payables (3,90,000 + 2,40,000 - 20,000*)	
	* <i>Mutual Owings eliminated.</i>	6,10,000

5	Short term Provisions	
	Provision for Doubtful Debts	7,500
6	Tangible assets	
	Land & Buildings	14,00,000
	Plant & Machinery	19,00,000
	Total	33,00,000
7	Intangible assets	
	Goodwill (1,50,000 +1,50,000)	3,00,000
8	Inventories (7,50,000 + 4,72,500)	12,22,500
9	Trade receivables (6,00,000 + 3,00,000 - 20,000)	8,80,000
10	Other current Assets	15,000
11	Cash and cash equivalents (1,50,000 +60,000)	2,10,000

Working Notes:

1. Computation of goodwill

₹

Profit of 2022-23	90,000
Profit of 2021-22 adjusted ₹ 78,000 + 10,000)	88,000
Profit of 2020-21 adjusted (₹ 72,000 – 25,000)	<u>47,000</u>
	<u>2,25,000</u>
Average profit	75,000

Goodwill to be valued at 2 times of average profits = ₹ 75,000 x 2
= ₹ 1,50,000

2.

Purchase Consideration:		₹
Goodwill		1,50,000
Land & Building		5,00,000
Plant & Machinery		4,00,000
Inventory		4,72,500
Trade receivables		3,00,000
Unrecorded assets		15,000
Cash at Bank		<u>60,000</u>
		18,97,500
Less: Liabilities:		
Retirement Gratuity	60,000	
Trade payables	2,40,000	
Provision for doubtful debts	<u>7,500</u>	<u>(3,07,500)</u>
Net Assets/ Purchase Consideration		15,90,000
To be satisfied as under:		

10% Preference Shareholders of Y Ltd.	3,00,000
Add: 10% Premium	<u>30,000</u>
9% Preference Shares of X Ltd.	3,30,000
Equity Shareholders of Y Ltd. to be satisfied by issue of 1,20,000 equity Shares of X Ltd. at 5% Premium	<u>12,60,000</u>
Total	<u>15,90,000</u>

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Restated Balance Sheet of MNT Ltd.
as at 31st December, 2024

Particulars	Note No.	(₹)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital		7,50,000
(b) Reserves and Surplus	1	7,18,500
(2) Current Liabilities		
(a) Short term borrowings	2	1,70,000
(b) Trade Payables		2,46,000
(c) Short-term provision	3	4,30,000
Total		<u>23,14,500</u>
II. Assets		
(1) Non-current assets		
(a) Property, Plant & Equipment	4	6,37,500
(b) Non-current Investment		5,30,000
(2) Current assets		
(a) Inventories (6,90,000 +12,000)	5	7,02,000
(b) Trade Receivables $\left(\frac{3,43,000}{98} \times 100\right)$		3,50,000
(c) Cash & Cash Equivalents		42,500
(d) Other current assets	6	52,500
Total		<u>23,14,500</u>

Notes to Accounts

			₹
1.	Reserves and Surplus		
	Revenue Reserve (refer W.N.)	5,11,500	
	Securities Premium	<u>2,07,000</u>	7,18,500
2.	Short term borrowings		

	Bank overdraft		1,70,000
3.	Short-term provision		
	Provision for taxation		4,30,000
4.	Property, Plant and Equipment		
	Cost	9,20,000	
	Less: Depreciation to date	<u>(2,82,500)</u>	6,37,500
5.	Inventories	6,90,000	
	Increase in value as per FIFO	<u>12,000</u>	7,02,000
6.	Other current assets		
	Prepaid expenses (After adjusting sales promotion expenses to be written off each year) (65,000 -12,500)		52,500

Working Note:

Adjusted revenue reserves of MNT Ltd.:

	₹	₹
Revenue reserves as given		5,05,000
Add: Provision for doubtful debts [3,43,000 X 2/98)	7,000	
Add: Increase in value of inventory	<u>12,000</u>	<u>19,000</u>
		5,24,000
Less: Sales Promotion expenditure to be written off		<u>(12,500)</u>
Adjusted revenue reserve		<u>5,11,500</u>

6. (a) Elements of Financial Statements

Asset	Resource controlled by the enterprise as a result of past events from which future economic benefits are expected to flow to the enterprise
Liability	Present obligation of the enterprise arising from past events, the settlement of which is expected to result in an outflow of a resource embodying economic benefits.
Equity	Residual interest in the assets of an enterprise after deducting all its liabilities
Income/gain	Increase in economic benefits during the accounting period in the form of inflows or enhancement of assets or decreases in liabilities that result in increase in equity other than those relating to contributions from equity participants
Expense/loss	Decrease in economic benefits during the accounting period in the form of outflows or depletions of assets or incurrance of liabilities that result in decrease in

	equity other than those relating to distributions to equity participants
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Or

Schedule III has come into force for the Balance Sheet and Profit and Loss Account prepared for the financial year commencing on or after 1st April, 2023. As per Part I of the Schedule III, a company should, inter alia, disclose in notes to accounts for the period of 5 years immediately preceding the balance sheet date (31st March, 2024 in the instant case) the aggregate number and class of shares allotted as fully paid-up bonus shares. Schedule III does not require a company to disclose the source from which bonus shares have been issued. Therefore, non-disclosure of source from which bonus shares have been issued does not violate the Schedule III to the Companies Act.

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

- (i) When sale price of ₹ 24 lakhs is equal to fair value, A Ltd. should immediately recognise the profit of ₹ 4 lakhs (i.e. 24 – 20) in its books.
- (ii) When fair value is ₹ 20 lakhs & sale price is ₹ 24 lakhs then profit of ₹ 4 lakhs is to be deferred and amortised over the lease period.
- (iii) When fair value is ₹ 22 lakhs & sale price is ₹ 25 lakhs, profit of ₹ 2 lakhs (22 - 20) to be immediately recognised in its books and balance profit of ₹ 3 lakhs (25-22) is to be amortised/deferred over lease period.
- (iv) When fair value of leased machinery is ₹ 25 lakhs & sale price is ₹ 18 lakhs, then loss of ₹ 2 lakhs (20 – 18) to be immediately recognised by A Ltd. in its books provided loss is not compensated by future lease payment.
- (v) When fair value is ₹ 18 lakhs & sale price is ₹ 19 lakhs, then the loss of ₹ 2 lakhs (20-18) to be immediately recognised by A Ltd. in its books and profit of ₹ 1 lakhs (19-18) should be amortised/deferred over lease period.

(c) Books of Branch A

Journal Entries

	Particulars		Dr. Amount ₹	Cr. Amount ₹
(i)	Expenses account Dr. To Head office account (Being the allocated expenditure by the head office recorded in branch books)		3,500	3,500
(ii)	Depreciation account Dr. To Head office account		1,500	1,500

	(Being the depreciation provided)			
(iii)	Head office account	Dr.	2,000	
	To Salaries account			2,000
	(Being the rectification of salary paid on behalf of H.O.)			
(iv)	Head office account	Dr.	10,000	
	To Debtors account			10,000
	(Being the adjustment of collection from branch debtors)			
(v)	No entry in branch books			
(vi)	Head Office account	Dr.	3,000	
	To Cash account			3,000
	(Being the expenditure on account of Branch B, recorded in books)			

Note: Entry (vi) Inter branch transactions are routed through Head Office.