MOCK TEST PAPER - 1

INTERMEDIATE (IPC) : GROUP – I

PAPER – 1: ACCOUNTING

SUGGESTED ANSWERS/HINTS

1. (a) As per AS 9 "Revenue Recognition", in a transaction involving the sale of goods, performance should be regarded as being achieved when the following conditions are fulfilled:

(i) the seller of goods has transferred to the buyer the property in the goods for a price or all significant risks and rewards of ownership have been transferred to the buyer and the seller retains no effective control of the goods transferred to a degree usually associated with ownership; and

(ii) no significant uncertainty exists regarding the amount of the consideration that will be derived from the sale of the goods.

Case (i): 25% goods lying unsold with consignee should be treated as closing inventory and sales should be recognized for Rs. 3,00,000 (75% of Rs. 4,00,000) for the year ended on 31.3.17. In case of consignment sale revenue should not be recognized until the goods are sold to a third party.

Case (ii): The sale is complete but delivery has been postponed at buyer's request. Fashion Ltd. should recognize the entire sale of Rs.1,95,000 for the year ended 31st March, 2017.

Case (iii): In case of goods sold on approval basis, revenue should not be recognized until the goods have been formally accepted by the buyer or the buyer has done an act adopting the transaction or the time period for rejection has elapsed or where no time has been fixed, a reasonable time has elapsed. Therefore, revenue should be recognized for the total sales amounting Rs. 2,50,000 as the time period for rejecting the goods had expired.

Thus total revenue amounting Rs. 7,45,000 (3,00,000+1,95,000+2,50,000) will be recognized for the year ended 31st March, 2017 in the books of Fashion Ltd.

(b) As per AS 7 on 'Construction Contracts', when a contract covers a number of assets, the construction of each asset should be treated as a separate construction contract when:

(a) separate proposals have been submitted for each asset;

(b) each asset has been subject to separate negotiation and the contractor and customer have been able to accept or reject that part of the contract relating to each asset; and

(c) the costs and revenues of each asset can be identified.

In the given case, each outlet is submitted as a separate proposal to different Zonal Office, which can be separately negotiated, and costs and revenues thereof can be separately identified. Hence, each asset will be treated as a "single contract" even if there is one document of contract.

Therefore, four separate contract accounts have to be recorded and maintained in the books of X Ltd. For each contract, principles of revenue and cost recognition have to be applied separately and net income will be determined for each asset as per AS 7.

(c) (i) As per AS 13, "Accounting for Investments" Investments classified as long term investments should be carried in the financial statements at cost. However, provision for diminution shall be made to recognise a decline, other than temporary, in the value of the investments, such reduction being determined and made for each investment individually. The standard also states that indicators of the value of an investment are obtained by reference to its market value, the investee's assets and results and the expected cash flows from the investment.

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On this basis, the facts of the case given in the question clearly suggest that the provision for diminution should be made to reduce the carrying amount of shares to Rs. 45,000 in the financial statements for the year ended 31st March, 2018 and charge the difference of loss of Rs. 2,55,000 to profit and loss account.

(ii) As per AS 13 'Accounting for Investments', where investments are reclassified from current to long-term, transfers are made at the lower of cost or fair value at the date of transfer. In the given case, the market value of the investment (X Ltd. shares) is Rs. 2.50 lakhs, which is lower than its cost i.e. Rs. 5 lakhs. Therefore, the transfer to long term investments should be made at cost of Rs. 2.50 lakhs. The loss of Rs. 2.50 lakhs should be charged to profit and loss account.

(d) According to AS 10 (Revised), the following costs can be capitalized:

Cost of the plant	Rs. 25,00,000
Initial delivery and handling costs	Rs. 2,00,000
Cost of site preparation	Rs. 6,00,000
Consultants' fees	Rs. 7,00,000
Estimated dismantling costs to be incurred after 7 years	Rs. 3,00,000
	Rs. 43,00,000

Note: Interest charges paid on "Deferred credit terms" to the supplier of the plant (not a qualifying asset) of Rs. 2,00,000 and operating losses before commercial production amounting to Rs. 4,00,000 are not regarded as directly attributable costs and thus cannot be capitalised. They should be written off to the Statement of Profit and Loss in the period they are incurred.

2. Journal Entries

		Rs.	*Rs.*
Bank A/c	Dr.	10,00,000	
To Equity share capital A/c			10,00,000
(Being money on final call received)			
Equity share capital (Rs. 50) A/c	Dr.	75,00,000	
To Equity share capital (Rs. 40) A/c			60,00,000
To Capital Reduction A/c			15,00,000
(Being conversion of equity share capital of Rs. 50 each into Rs. 40 each as per reconstruction scheme)			
Bank A/c	Dr.	12,50,000	
To Equity Share Capital A/c			12,50,000
(Being new shares allotted at Rs. 40 each)			
Trade payables A/c	Dr.	12,40,000	
To Equity share capital A/c			7,50,000
To Bank A/c (4,90,000 x 70%)			3,43,000
To Capital Reduction A/c			1,47,000
(Being payment made to creditors in shares or cash to the extent of 70% as per reconstruction scheme)			
8% Debentures A/c	Dr.	3,00,000	
12% Debentures A/c	Dr.	4,00,000	
To A A/c			7,00,000
(Being cancellation of 8% and 12% debentures of A)			
A A/c	Dr.	7,00,000	

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To 15% Debentures A/c			5,00,000
To Capital Reduction A/c			2,00,000
(Being issuance of new 15% debentures and balance transferred to capital reduction account as per reconstruction scheme)			
Bank A/c	Dr.	1,00,000	
To 15% Debentures A/c			1,00,000
(Being new debentures subscribed by A)			
8% Debentures A/c	Dr.	1,00,000	
12% Debentures A/c	Dr.	2,00,000	
To B A/c			3,00,000
(Being cancellation of 8% and 12% debentures of B)			
B A/c	Dr.	3,00,000	
To 15% Debentures A/c			2,50,000
To Capital Reduction A/c			50,000
(Being issuance of new 15% debentures and balance transferred to capital reduction account as per reconstruction scheme)			
Land and Building (51,84,000 – 42,70,000)	Dr.	9,14,000	
Inventories	Dr.	30,000	
To Capital Reduction A/c			9,44,000
(Being value of assets appreciated)			
Outstanding expenses A/c	Dr.	10,60,000	
To Bank A/c			10,60,000
(Being outstanding expenses paid in cash)			
Capital Reduction A/c	Dr.	33,41,000	
To Machinery A/c			1,30,000
To Computers A/c			1,20,000
To Trade receivables A/c			1,09,000
To Profit and Loss A/c			29,82,000
(Being amount of Capital Reduction utilized in writing off P & L A/c (Dr.) balance and downfall in value of other assets)			
Capital Reserve A/c	Dr.	5,00,000	
To Capital Reduction A/c			5,00,000
(Being debit balance of capital reduction account adjusted against capital reserve)			

Balance Sheet of Xylem Ltd. (as reduced) as on 31.3.2017

Particulars			*Notes*	*Rs.*
	Equity and Liabilities			
1	**Shareholders' funds**			
a		Share capital	1	80,00,000
2	**Non-current liabilities**			
a		Long-term borrowings	2	8,50,000
		Total		**88,50,000**
	Assets			
1	**Non-current assets**			
a		Fixed assets		

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		Tangible assets	3	63,04,000
2		**Current assets**		
	a	Inventories		3,50,000
	b	Trade receivables		9,81,000
	c	Cash and cash equivalents		12,15,000
		Total		**88,50,000**

Notes to accounts

			Rs.
1.	**Share Capital**		
	2,00,000 Equity shares of Rs. 40		80,00,000
2.	**Long-term borrowings**		
	Secured		
	15% Debentures (assumed to be secured)		8,50,000
3.	**Tangible assets**		
	Land & Building	51,84,000	
	Machinery	7,20,000	
	Computers	4,00,000	63,04,000

Working Notes:

1. **Cash at Bank Account**

Particulars		*Rs.*	*Particulars*		*Rs.*
To	Balance b/d	2,68,000	By	Trade Creditors A/c	3,43,000
To	Equity Share capital A/c	10,00,000	By	Outstanding expenses A/c	10,60,000
To	Equity Share Capital A/c	12,50,000	By	Balance c/d (bal. fig.)	12,15,000
To	15% Debentures A/c	1,00,000			
		26,18,000			26,18,000

2. **Capital Reduction Account**

Particulars		*Rs.*	*Particulars*		*Rs.*
To	Machinery A/c	1,30,000	By	Equity Share Capital A/c	15,00,000
To	Computers A/c	1,20,000	By	Trade payables A/c	1,47,000
To	Trade receivables A/c	1,09,000	By	A A/c	2,00,000
To	Profit and Loss A/c	29,82,000	By	B A/c	50,000
			By	Land & Building	9,14,000
			By	Inventories	30,000
			By	Capital Reserve A/c	5,00,000
		33,41,000			33,41,000

3. Megha Ltd.

Balance Sheet as on 31st March, 20X1

		Particulars	*Notes*	*Rs.*
		Equity and Liabilities		
1		**Shareholders' funds**		
	a	Share capital	1	49,95,000
	b	Reserves and Surplus	2	14,83,500

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2		**Non-current liabilities**		
		Long-term borrowings	3	13,17,500
3		**Current liabilities**		
	a	Trade Payables		8,00,000
	b	Other current liabilities	4	37,500
	c	Short-term provisions	5	6,40,000
	d	Short-term borrowings		2,00,000
		Total		**94,73,500**
		Assets		
1		**Non-current assets**		
		Fixed assets		
		Tangible assets	6	56,25,000
2		**Current assets**		
	a	Inventories	7	12,50,000
	b	Trade receivables	8	10,00,000
	c	Cash and bank balances	9	13,85,000
	d	Short-term loans and advances		2,13,500
		Total		**94,73,500**

Notes to accounts

			Rs.
1	**Share Capital**		
	Equity share capital		
	Issued & subscribed & called up		
	50,000 Equity Shares of Rs. 100 each		
	(of the above 10,000 shares have been issued for consideration other than cash)	50,00,000	
	Less: Calls in arrears	(5,000)	49,95,000
	Total		49,95,000
2	**Reserves and Surplus**		
	General Reserve	10,50,000	
	Add: current year transfer	20,000	10,70,000
	Profit & Loss balance		
	Profit for the year	4,33,500	
	Less: Appropriations:		
	Transfer to General reserve	(20,000)	4,13,500
	Total		14,83,500
3	**Long-term borrowings**		
	Secured Term Loan		
	State Financial Corporation Loan (7,50,000-37,500)		
	(Secured by hypothecation of Plant and Machinery)		7,12,500
	Unsecured Loan		6,05,000
	Total		13,17,500

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4	**Other current liabilities**			
	Interest accrued but not due on loans (SFC)			37,500
5	**Short-term provisions**			
	Provision for taxation			6,40,000
6	**Tangible assets**			
	Land and Building		30,00,000	
	Less: Depreciation		(2,50,000) (b.f.)	27,50,000
	Plant & Machinery		35,00,000	
	Less: Depreciation		(8,75,000) (b.f.)	26,25,000
	Furniture & Fittings		3,12,500	
	Less: Depreciation		(62,500)(b.f.)	2,50,000
		Total		56,25,000
7	**Inventories**			
	Raw Materials			2,50,000
	Finished goods			10,00,000
		Total		12,50,000
8	**Trade receivables**			
	Outstanding for a period exceeding six months			2,60,000
	Other Amounts			7,40,000
		Total		10,00,000
9	**Cash and bank balances**			
	Cash at bank			
	with Scheduled Banks		12,25,000	
	with others (Omega Bank Ltd.)		10,000	12,35,000
	Cash in hand			1,50,000
	Other bank balances			Nil
		Total		13,85,000

4. **Memorandum Revaluation Account**

		Rs.			*Rs.*
To	Stock	80,000	By	Building	3,60,000
To	Plant & machinery	2,40,000	By	Investments	40,000
To	Provision for doubtful debts	30,000			
To	Unrecorded liability	20,000			
To	Profit transferred to Partners' Capital A/cs (in old ratio)				
	Kamal = 20,000				
	Rani = 10,000	30,000			
		4,00,000			4,00,000
To	Building	3,60,000	By	Stock	80,000
To	Investments	40,000	By	Plant & machinery	2,40,000

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		By Provision for doubtful debts	30,000
		By Unrecorded liability	20,000
		By Loss transferred to Partners' Capital A/cs (in new ratio)	
		Kamal = 15,000	
		Rani = 7,500	
		Nisha = 7,500	30,000
	4,00,000		4,00,000

Partners' Capital Accounts

	Kamal	Rani	Nisha		Kamal	Rani	Nisha
To Memorandum Revaluation	15,000	7,500	7,500	By Balance b/d	20,00,000	10,00,000	-
To Reserve Fund	9,00,000	4,50,000	4,50,000	By Reserve	12,00,000	6,00,000	-
To Kamal (W.N.3)	-	-	35,000	By Nisha (W.N.3)	35,000	17,500	-
To Rani (W.N.3)	-	-	17,500	By Memorandum Revaluation A/c	20,000	10,000	
To Balance c/d (Refer W.N.2)	23,40,000	11,70,000	11,70,000	By Cash (Bal. Fig.)			16,80,000
	32,55,000	16,27,500	16,80,000		32,55,000	16,27,500	16,80,000

Balance Sheet of newly reconstituted firm as on 31.12.2017

Liabilities	*Rs.*	*Assets*	*Rs.*
Capital Accounts		Plant & Machinery	24,00,000
Kamal	23,40,000	Building	18,00,000
Rani	11,70,000	Sundry Debtors	6,00,000
Nisha	11,70,000	Stock	8,00,000
Reserve Fund	18,00,000	Cash (2,00,000 + 16,80,000)	18,80,000
Sundry Creditors	8,00,000		
Bills Payable	2,00,000		
	74,80,000		74,80,000

Working Notes:

1. **Calculation of new profit and loss sharing ratio**

   Nisha will get 1/4th share in the new profit sharing ratio.

   Therefore, remaining share will be 1-1/4 =3/4

   Share of Kamal will be 3/4 x 2/3 = 2/4 i.e. 1/2

   Share of Rani will be 3/4 x 1/3 = 1/4

   New ratio will be

   Kamal : Rani : Nisha

   1/2 : 1/4 : 1/4

   2 : 1: 1

2. **Calculation of closing capital of Nisha**

   Closing capitals of Kamal & Rani after all adjustments are:

   Kamal = Rs. 23,40,000

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Rani = Rs. 11,70,000

Since Rani's capital is less than Kamal's capital, therefore Rani's capital is taken as base.

Hence, Nisha's closing capital should be Rs. 11,70,000 (46,80,000 x ¼) i.e. at par with Rani (as per new profit and loss sharing ratio)

3. Adjustment entry for goodwill

Partners	*Goodwill as per old ratio*	*Goodwill as per new ratio*	*Effect*	
Kamal	1,40,000	1,05,000	+ 35,000	-
Rani	70,000	52,500	+ 17,500	-
Nisha	-	52,500	-	52,500
	2,10,000	2,10,000	52,500	52,500

Adjustment entry will be:

Nisha's Capital A/c	Dr.	52,500	
To Kamal's Capital A/c			35,000
To Rani's Capital A/c			17,500

5. (a) Income and Expenditure Account

for the year ended 31st March, 2018

		Rs.		*Rs.*
To Medicines consumed			By Prescription fees	3,30,000
Purchases	1,22,500		By Visiting fees	1,25,000
Less: Closing Stock	(47,500)	75,000	By Fees from lectures	12,000
To Motor car expense (60,000 x 2/3)		40,000		
To Salaries (Rs. 52,500 – Rs. 15,000)		37,500		
To Rent for clinic		30,000		
To General charges		24,500		
To Interest on loan		18,000		
To Excess of income over expenditure		2,42,000		
		4,67,000		4,67,000

Capital Account

for the year ended 31st March, 2018

	Rs.		*Rs.*
To Drawings:		By Cash/bank	1,00,000
Motor car expenses	20,000	By Cash/bank (pension)	1,50,000
Household expenses	90,000	By Net income from practice	2,42,000
Marriage expenses	1,07,500	(derived from income	
To Salary of domestic servants	15,000	and expenditure A/c)	
To Household furniture	12,500		
To Balance c/d	2,47,000		
	4,92,000		4,92,000

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Balance Sheet as on 31st March, 2018

Liabilities	*Rs.*	*Assets*	*Rs.*
Capital	2,47,000	Motor car	1,60,000
Loan	1,50,000	Surgical equipment	1,25,000
		Stock of medicines	47,500
		Cash at bank	55,000
		Cash in hand	9,500
	3,97,000		3,97,000

(b) Calculation of net profit u/s 198 of the Companies Act, 2013

	Rs.	*Rs.*
Balance from Trading A/c		40,25,365
Add: Subsidies received from Government		2,73,925
		42,99,290
Less: Administrative, selling and distribution expenses	8,22,542	
Director's fees	1,34,780	
Interest on debentures	31,240	
Depreciation on fixed assets as per Schedule II	5,75,345	(15,63,907)
Profit u/s 198		27,35,383

Maximum Managerial remuneration under Companies Act, 2013= 11% of Rs.27,35,383 = Rs.3,00,892

6. (a) Statement of Affairs of Ms. Shreya as on 31.03.2017 and 31.03.2018

Liabilities	*31.03.2017* *Rs.*	*31.03.2018* *Rs.*	*Assets*	*31.03.2017* *Rs.*	*31.03.2018* *Rs.*
Capital (Balancing Figure)	1,22,150	2,27,125	Machinery & Tools	25,000	27,125
Loan	50,000	46,000	Furniture & Fixtures	50,000	54,750
Creditors	20,000	35,000	Stock	60,000	1,35,000
			Debtors	20,000	45,000
			Cash at Bank	35,000	42,500
			Cash in Hand	2,150	3,750
	1,92,150	3,08,125		1,92,150	3,08,125

Determination of Profit:	**Rs.**
Capital Balance as on 31.03.2018	2,27,125
Less: Prize won, retained in business	20,000
	2,07,125
Add: Withdrawals (Rs. 1,000 x 12)	12,000
	2,19,125
Less: Capital Balance as on 31.03.2017	1,22,150
Profit for the year ended 31st March, 2018	96,975

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Working Notes:

1.	**Written Down Value of Machinery and Tools**	**Rs.**
	W.D.V. as on 01.04.2017	25,000
	Less: Depreciation on W.D.V. @ 10% p.a.	2,500
		22,500
	Add: Addition during the year on 01.07.2017	5,000
		27,500
	Less: Depreciation on Addition @ 10% p.a. (5,000 x 10/100x9/12)	375
	W.D.V. of Machinery & tools as on 31.03.2018	27,125

2.	**Written Down Value of Furniture and Fixtures**	**Rs.**
	W.D.V. as on 01.04.2017	50,000
	Less: Depreciation on W.D.V. @ 10% p.a.	5,000
		45,000
	Add: Addition during the year on 01.01.2018	10,000
		55,000
	Less: Depreciation on Addition @ 10% p.a. (10,000 x 10/100x3/12)	250
	W.D.V. of Furniture & Fixtures as on 31.03.2018	54,750

(b) **Mr. S in Account Current with Mr. R as on 31st October, 2018**

		Rs.	*Days*	*Product (Rs.)*			*Rs.*	*Days*	*Product (Rs.)*
01.07.18	To Bal. b/d	750	123	92,250	20.08.18	By Sales Returns	200	72	14,400
15.8.18	To Sales	1,250	77	96,250	22.09.18	By Bank	800	39	31,200
31.10.18	To Interest	18.48			15.10.18	By Cash	500	16	8,000
						By Balance of Products			1,34,900
					31.10.18	By Bal. c/d	518.48		
		2018.48		1,88,500			2018.48		1,88,500

Interest = Rs. 1,34,900 x $\frac{5}{100} \times \frac{1}{365}$ = Rs. 18.48

7. **(a)** As per AS 1, any change in the accounting policies which has a material effect in the current period or which is reasonably expected to have a material effect in later periods should be disclosed. In the case of a change in accounting policies which has a material effect in the current period, 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. Accordingly, the notes on accounts should properly disclose the change and its effect.

Notes on Accounts:

So far, the company has been providing 2% of sales for meeting "after sales expenses during the warranty period. With the improved method of production, the probability of defects occurring in the products has reduced considerably. Hence, the company has decided not to make provision for such expenses but to account for the same as and when expenses are incurred. Due to this change, the profit for the year is increased by Rs. 12 crores than would have been the case if the old policy were to continue.

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(b) Recently a growing trend has developed for outsourcing the accounting function to a third party. The consideration for doing this is to save cost and to utilise the expertise of the outsourced party. The third party maintains the accounting software and the client data, does the processing and hands over the report from time to time.

Benefits of outsourcing the accounting function to a third party:

1. **Saving of Time:** The organisation that outsources its accounting function is able to save time to concentrate on the core area of business activity.
2. **Expertise of the third party:** The organisation is able to utilise the expertise of the third party in undertaking the accounting work.
3. **Maintenance of data:** Storage and maintenance of the data is in the hand of professional people.
4. **Economical:** The organisation is not bothered about people leaving the organization in key accounting positions. The proposition is proving to be economically and more sensible as they do not have train the people again. Hence, the training cost is saved.

(c) When Net Realizable Value of the Chemical Y is Rs. 800 per unit

NRV is greater than the cost of Finished Goods Y i.e. Rs. 660 (Refer W.N.)

Hence, Raw Material and Finished Goods are to be valued at cost.

Value of Closing Stock:

	Qty.	*Rate (Rs.)*	*Amount (Rs.)*
Raw Material X	1,000	440	4,40,000
Finished Goods Y	2,400	660	15,84,000
Total Value of Closing Stock			20,24,000

Working Note:

Statement showing cost calculation of Raw material X and Chemical Y

Raw Material X	***Rs.***
Cost Price	380
Add: Freight Inward	40
Unloading charges	20
Cost	440
Chemical Y	***Rs.***
Materials consumed	440
Direct Labour	120
Variable overheads	80
Fixed overheads (Rs.4,00,000/20,000 units)	20
Cost	660

(d) According to AS 14, 'consideration' for the amalgamation means the aggregate of the shares and other securities issued and the payment made in the form of cash or other assets by the transferee company to the shareholders of the transferor company. Therefore, debentures issued to the debenture holders will not be included in purchase consideration.

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Purchase consideration

	Rs.	*Form*
Preference shareholders : 5,000 × 3/4 × 100	3,75,000	9% Pref. shares
Equity shareholders: 12,500 × Rs. 20	2,50,000	Cash
12,500 × 6/5 × 125	18,75,000	Equity shares
Total Purchase Consideration	25,00,000	

(e) 1st payment is made after 12 months from the date of loan.

2nd payment is made after 18 months from the date of loan.

3rd payment is made after 24 months from the date of loan.

4th payment is made after 30 months from the date of loan.

5th payment is made after 36 months from the date of loan.

Sum of the months =120

Average due date =

$$\text{Date of loan} + \frac{\text{Sum of months from 1st January, 2018 to the date of each installment}}{\text{Number of installments}}$$

$$= 1^{st} \text{ January, 2017} + \frac{120 \text{ months}}{5}$$

= 1st January, 2017+ 24 months

= 1st January, 2019

Interest = Rs. 50,000 x 10/100 x 2 years = Rs.10,000

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