2412081103-financial_accounting

1. (a) State the meaning of contingent assets. Explain about the principles to be considered for the measurement of a provision according to AS 29.

- **Contingent Assets:** Possible assets whose existence depends on uncertain future events not wholly within the entity's control. They are *not* recognized in financial statements but disclosed if probable.
- **Measurement of Provision (AS 29):**
  - **Best Estimate:** Amount should be the best estimate of the expenditure required to settle the obligation.
  - **Risk and Uncertainty:** Consider risks and uncertainties through a range of outcomes.
  - **Present Value:** If time value of money is material, provisions should be discounted to present value.
  - **Future Events:** Consider future events that may affect the amount.
  - **Expected Disposal of Assets:** Gains from expected disposal of assets are not considered in measuring a provision.

1. (b) Write short note on:

- **(i) Convention of Full Disclosure:** All material and relevant information must be disclosed in financial statements to enable users to make informed decisions.
- **(ii) Cost Concept:** Assets are recorded at their acquisition cost. This cost forms the basis for subsequent accounting until the asset is disposed of or revalued.

1. (c) State the accounting principle involved in the following statements.

- **(i) Drawings account is debited for cash withdrawn... for his personal expenses.**
  - **Business Entity Concept:** The business is separate from its owner.
- **(ii) Unless there is evidence to the contrary it is assumed that business will not be liquidated...**
  - **Going Concern Concept:** Assumes the business will continue indefinitely.

- **(iii) Advance received from customer is not recorded as sales.**
  - **Revenue Recognition Concept:** Revenue is recognized when earned, not necessarily when cash is received.
- **(iv) Life of a business is broken into several parts called accounting years...**
  - **Accounting Period Concept:** Divides the life of a business into specific periods for performance measurement.
- **(v) A pair of scissors acquired at ₹150 is included in Profit and Loss A/c.**
  - **Materiality Concept:** Small value items are expensed, even if they have a longer life, because their impact on financial statements is immaterial.
- **(vi) ₹1 lakh Capital contributed by the owner results in increase in cash by ₹1 lakh.**
  - **Dual Aspect Concept:** Every transaction has two effects (debit and credit), maintaining the accounting equation (Assets = Liabilities + Capital).

OR

1. (a) What is meant by international financial reporting standards (IFRS). Why there is need for convergence of IFRS?

- **IFRS:** A single set of global accounting standards developed by the IASB (International Accounting Standards Board) to ensure comparability and transparency in financial reporting across countries.
- **Need for Convergence:** To reduce financial reporting costs, facilitate international capital flows, enhance comparability for investors, and improve efficiency for multinational corporations.

1. (b) What are accounting policies as per AS 5? Explain the considerations in the selection of accounting policies. In what conditions change in accounting policy should be made?

- **Accounting Policies (AS 5):** Specific accounting principles and methods adopted by an enterprise in preparing and presenting financial statements.
- **Considerations in Selection:**
  - **Prudence:** Conservatism in accounting.

    - **Substance Over Form:** Economic reality overrides legal form.
    - **Materiality:** Policies should be applied to material items.
- **Conditions for Change:** Only if required by statute/accounting standard, or if it results in a more appropriate presentation of financial statements.

1. (c) Write a note on mercantile basis of accounting.

- **Mercantile (Accrual) Basis:** Revenue and expenses are recognized when earned or incurred, regardless of when cash is received or paid. This provides a more accurate picture of a period's financial performance.

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2. (a) Shoba Traders depreciated its machinery... Show machinery account for the year ended 31st March 2023.

- **Steps:**
    1. Calculate opening WDV of original machinery as of April 1, 2022, using the old diminishing balance method (10% p.a. from April 1, 2020).
    2. Calculate depreciation on the old machine sold for the period April 1, 2022 to October 1, 2022, using the *new* Straight Line Method (8% p.a.).
    3. Determine the profit/loss on sale of old machinery.
    4. Record the purchase and installation of new machinery.
    5. Calculate depreciation on the remaining original machinery and the new machinery for the year ended March 31, 2023, using the Straight Line Method (8% p.a.).
    6. Prepare the Machinery Account, showing opening balance, sale entry, purchase entry, depreciation, and closing balance.

2. (b) Oil India is a leading distributor of petrol... Using periodic system compute the following by FIFO as per AS-2:

- **Steps (FIFO - First-In, First-Out):**
    1. **Cost of Goods Available for Sale:** Opening Inventory + Purchases.
        - Opening: 1,00,000 litres @ ₹3 = ₹3,00,000

    - Purchases: 2,00,000 litres @ ₹2.85 = ₹5,70,000; 1,00,000 litres @ ₹3.03 = ₹3,03,000.
    - Total Cost of Goods Available = ₹3,00,000 + ₹5,70,000 + ₹3,03,000 = ₹11,73,000
    - Total Litres Available = 1,00,000 + 2,00,000 + 1,00,000 = 4,00,000 litres
2. **(i) Value of Inventory on June 30 (Closing Inventory):** 1,30,000 litres. Under FIFO, assume the latest purchases are remaining.
    - 1,00,000 litres @ ₹3.03 = ₹3,03,000
    - 30,000 litres @ ₹2.85 = ₹85,500
    - Total Closing Inventory = ₹3,03,000 + ₹85,500 = ₹3,88,500
3. **(ii) Amount of Cost of Goods Sold for June:**
    - Cost of Goods Available for Sale - Closing Inventory
    - ₹11,73,000 - ₹3,88,500 = ₹7,84,500
4. **(iii) Profit/Loss for the month of June:**
    - Sales (₹9,45,000) - Cost of Goods Sold (₹7,84,500) - General Overheads (₹25,000)
    - Profit = ₹9,45,000 - ₹7,84,500 - ₹25,000 = ₹1,35,500

2. (c) Write down any four revenue sources where AS 9 is not applicable.

- **AS 9 (Revenue Recognition) is not applicable to:**
    1. Revenue arising from construction contracts.
    2. Revenue arising from hire-purchase and lease agreements.
    3. Revenue arising from government grants and subsidies.
    4. Revenue arising from insurance contracts.
    5. Revenue arising from financial instruments.

OR

2. (a) In each of the above cases, you are required to advise, with valid reasons, the amount to be recognised as revenue under the provisions of AS-9 if the company is closing its accounts every year on 31st March.

- **(i) Radhika publications (Magazine Advertising):**

  - **Revenue Recognition:** Revenue from advertising space is recognized when the magazine is published.
  - **Amount for March 2024 Issue:** ₹1,50,000 (received March 5, 2024) + ₹50,000 (received April 15, 2024) = **₹2,00,000**. All pertains to the March 2024 issue which was published before March 31, 2024.
- **(ii) Goods sold on approval basis to Varun Ltd.:**
  - **Revenue Recognition:** When approval is received or period of approval expires without rejection.
  - **Amount:**
    - 60% approved by Jan 30, 2024: 60% of ₹3,50,000 = **₹2,10,000** (recognized).
    - Remaining 40% (₹1,40,000): Approval period expired Feb 10, 2024 (2 months after Dec 10, 2023). So, the entire amount is deemed sold by Feb 10, 2024.
    - Total Revenue = ₹2,10,000 + ₹1,40,000 = **₹3,50,000**.
- **(iii) Sold goods ₹6,00,000 lakhs to R Ltd... delivered on 20-04-2024.**
  - **Revenue Recognition:** When significant risks and rewards of ownership are transferred to the buyer. Delivery is key unless specific terms state otherwise.
  - **Amount: Nil** for the year ended March 31, 2024, as delivery and transfer of risks/rewards occurred after the year-end (April 20, 2024). It will be recognized in the next financial year.
- **(iv) Goods sent on consignment basis... 30% remain unsold...**
  - **Revenue Recognition:** Revenue is recognized by the consignor only when goods are sold by the consignee to third parties.
  - **Amount:** 70% of ₹1,00,000 = **₹70,000** (recognized as sold). The unsold 30% are still inventory of the consignor.

2. (b) M/s Ishan and Co. had a property plant and equipment... Pass journal entries in the following cases:

- **General Note:** Revaluation gains are credited to "Revaluation Surplus" (Other Comprehensive Income) unless they reverse a previous revaluation decrease recognized in P&L. Revaluation losses are debited to P&L, but first set off against any existing Revaluation Surplus for that asset.

- **(i) Fair value was assessed at ₹29,00,000 (Book Value ₹25,00,000):**
    - **Journal Entry:**
        - Property, Plant and Equipment A/c Dr. ₹4,00,000
        - To Revaluation Surplus A/c ₹4,00,000
        - *(Being revaluation gain recognized)*
- **(ii) Previous year revalued downwards by ₹4,00,000 (recognized in P&L); Fair value assessed at ₹29,00,000 (current book value ₹25,00,000):**
    - The current gain of ₹4,00,000 (₹29L - ₹25L) reverses the previous loss of ₹4,00,000.
    - **Journal Entry:**
        - Property, Plant and Equipment A/c Dr. ₹4,00,000
        - To Profit & Loss A/c ₹4,00,000
        - *(Being revaluation gain recognized to the extent of previous loss)*
- **(iii) Previous year revalued downwards by ₹3,00,000 (recognized in P&L); Fair value assessed at ₹29,00,000 (current book value ₹25,00,000):**
    - Current gain of ₹4,00,000 (₹29L - ₹25L). This gain first reverses the previous loss of ₹3,00,000 (to P&L), and the remaining gain of ₹1,00,000 (₹4L - ₹3L) goes to Revaluation Surplus.
    - **Journal Entry:**
        - Property, Plant and Equipment A/c Dr. ₹4,00,000
        - To Profit & Loss A/c ₹3,00,000
        - To Revaluation Surplus A/c ₹1,00,000
        - *(Being revaluation gain recognized, partly reversing previous loss and partly to surplus)*

2. (c) A company acquired a patent... Find out amortisation expense of the patent for each of these years... company changed amortisation method from Straight Line Method to ratio of expected cash flows.

- **Steps:**
    1. **Calculate WDV of Patent after 2 years:**
        - Cost: ₹20,00,000
        - Amortization (SLM) for 2 years: ₹2,50,000/year * 2 years = ₹5,00,000
        - WDV at end of 2 years (beginning of year 3 for new method): ₹20,00,000 - ₹5,00,000 = ₹15,00,000

2. **Remaining Life:** Product life cycle continues for another 5 years.
3. **Total Expected Cash Flows for remaining 5 years:** ₹9,00,000 + ₹11,50,000 + ₹11,00,000 + ₹10,00,000 + ₹8,50,000 = ₹50,00,000
4. **Amortisation Expense each year (Ratio of Cash Flows):** Amortization for each year = (WDV / Total Expected Cash Flows) * Expected Cash Flow for that year.
    - **Year 3:** (₹15,00,000 / ₹50,00,000) * ₹9,00,000 = **₹2,70,000**
    - **Year 4:** (₹15,00,000 / ₹50,00,000) * ₹11,50,000 = **₹3,45,000**
    - **Year 5:** (₹15,00,000 / ₹50,00,000) * ₹11,00,000 = **₹3,30,000**
    - **Year 6:** (₹15,00,000 / ₹50,00,000) * ₹10,00,000 = **₹3,00,000**
    - **Year 7:** (₹15,00,000 / ₹50,00,000) * ₹8,50,000 = **₹2,55,000**

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3. Prepare Trading and P&L A/c for the year ended 31.12.2022 and Balance Sheet as on 31.12.2022.

- **Steps for Trading Account:**
    1. **Opening Stock:** Debit.
    2. **Purchases:** Debit (adjusted for returns outward and unrecorded purchases).
    3. **Direct Expenses:** Freight and Carriage (Debit).
    4. **Sales:** Credit (adjusted for returns inward).
    5. **Closing Stock:** Credit.
    6. Calculate Gross Profit/Loss.
- **Steps for Profit & Loss Account:**
    1. **Gross Profit/Loss:** Transferred from Trading A/c.
    2. **Incomes (Credit):** Miscellaneous Income, Discount Earned.
    3. **Expenses (Debit):** Rent & Taxes, Salaries & Wages, Bank Interest (adjusted for full year), Printing & Advertising (adjusted for prepaid), Discount Allowed, General Expenses, Insurance, Postage & Telegram, Travelling Expenses.
    4. **Adjustments:**

        - **Debtors/Creditors Set-off:** Reduce both by ₹1,000 (Barun's case).
        - **Provision for Doubtful Debts:** 5% on Sundry Debtors (new balance after set-off).
        - **Discount on Debtors:** 2% on Sundry Debtors (after provision for doubtful debts).
        - **Depreciation on Furniture & Fitting:** 10%.
        - **Drawings of Goods:** Reduce Purchases and credit Drawings A/c (at cost + GST). Adjust Input GST.
        - **Bank Loan Interest:** Calculate 6% of ₹20,000 for full year (₹1,200). Adjust for ₹900 already paid.
        - **Printing & Advertising:** 1/4th is prepaid (carry forward).
        - **Unrecorded Purchase:** Add ₹400 to Purchases and Sundry Creditors.
        - **Closing Stock:** (Given)
        - **GST Adjustment:** Net off Input CGST/SGST against Output CGST/SGST. Record any balance payable/receivable.
    5. Calculate Net Profit/Loss.
- **Steps for Balance Sheet:**
    1. **Liabilities Side:** Mr. Amitesh's Capital (add Net Profit, less Drawings), Sundry Creditors (adjusted), Bank Loan, Output GST payable (if any), Outstanding Bank Interest, Outstanding Printing & Advertising (if any).
    2. **Assets Side:** Cash at Bank, Cash in Hand, Sundry Debtors (less provisions), Furniture & Fitting (less depreciation), Closing Stock, Prepaid Printing & Advertising, Input GST recoverable (if any).

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4. (a) Titan club has following balances... How will you deal with the above items while preparing the income and expenditure account for the year ended 31st December 2023 and Balance sheet as on that date. Show the extracts of final statements.

- **Income & Expenditure Account (Extract):**
    - **Income Side:**
        - Interest received on general fund investments: ₹30,000 (Income).

- **Expenditure Side:**
  - Expenses incurred on sports events: ₹4,000 (Expenditure).
- **Balance Sheet (Extract):**
  - **Liabilities Side:**
    - Donation for Prize Fund: ₹1,00,000 (Specific Fund).
    - Prize Fund Received during the year: ₹18,000 (Add to Prize Fund).
    - Interest received on Prize Fund Investments: ₹12,000 (Add to Prize Fund).
    - Prizes Awarded during the year: ₹7,000 (Less from Prize Fund).
    - *Net balance of Prize Fund will appear on Liabilities side.*
  - **Assets Side:**
    - 10% Sports Fund Investments (Face value ₹2,00,000, fully paid): ₹1,00,000 (Asset).

4. (b) The final accounts of a Nano club are prepared annually as at 31st March... Calculate the amount of subscriptions to be credited to income and expenditure account by preparing subscription account for the year 2022-23.

- **Subscription Account (for year 2022-23):**
  - **Debit Side:**
    - To Balance b/d (Subscriptions in arrears 31.03.2022): ₹17,400
    - To Income & Expenditure A/c (Balancing figure - Amount to be credited)
  - **Credit Side:**
    - By Balance b/d (Subscription received in advance 31.03.2022 for 2022-23): ₹14,200
    - By Cash A/c (Subscriptions received during 2022-23): ₹2,42,800
    - By Balance c/d (Subscriptions in arrears 31.03.2023): ₹10,600
    - By Balance c/d (Subscription received in advance 31.03.2023 for 2023-24): ₹21,600
  - **Calculation:** Total Credit = ₹14,200 + ₹2,42,800 + ₹10,600 + ₹21,600 = ₹2,89,200

        - Subscriptions to be credited to Income & Expenditure A/c = ₹2,89,200 - ₹17,400 = **₹2,71,800**

4. (c) How will you deal with the following items while preparing the income and expenditure account for the year ended 31st December 2022 and balance sheet as on that date. During 2022 payments made to the creditors for stationery amounted ₹3,00,000 and cash purchases of stationary amounted to 20% of the total purchase.

- **Steps:**
  1. **Calculate Total Purchases of Stationery:**
     - Let Total Purchases = X. Cash Purchases = 0.20X. Credit Purchases = 0.80X.
     - Creditors for Stationery Account:
       - Opening Creditors (30,000) + Credit Purchases (0.80X) - Payments to Creditors (3,00,000) = Closing Creditors (50,000)
       - 30,000 + 0.80X - 3,00,000 = 50,000
       - 0.80X = 50,000 + 3,00,000 - 30,000 = 3,20,000
       - X = 3,20,000 / 0.80 = ₹4,00,000 (Total Purchases)
  2. **Stationery Consumed (for Income & Expenditure A/c):**
     - Opening Stock of Stationery (90,000) + Total Purchases (4,00,000) - Closing Stock of Stationery (70,000)
     - = ₹90,000 + ₹4,00,000 - ₹70,000 = **₹4,20,000** (This amount will be debited to Income & Expenditure A/c).
- **Balance Sheet (Extract):**
  - **Liabilities:** Creditors for stationery (₹50,000).
  - **Assets:** Stock of stationery (₹70,000).

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5. (a) Diamond Art Co. acquired machinery on lease... (i) Whether the lease is operating lease or finance lease giving reasons? (ii) How would this lease be accounted for in the books of lessor and lessee...

- **(i) Operating Lease or Finance Lease (AS 19):**
  - **Indicators of Finance Lease:**
    1. Lease term (5 years) is a major part of the useful life (15 years) of the asset.

    2. Present Value of Minimum Lease Payments (PVMLP) (calculate using IRR 15% and annual rentals) is likely to be substantially equal to the fair value of machinery (₹35,00,000).
    3. Implicit Rate of Return (IRR) is 15%.
  - **Conclusion:** Given the substantial lease term relative to useful life and implicit rate, this is likely a **Finance Lease**.
- **(ii) Accounting (Lessee's Books - for 1st year):**
  - **Initial Recognition:** Lessee recognizes an asset (Right-of-use asset) and a liability (Lease Liability) at the lower of the fair value of the asset or the PVMLP.
  - **Journal Entries (Lessee):**
    - On acquisition:
      - Right-of-Use Asset A/c Dr. (PVMLP or Fair Value)
      - To Lease Liability A/c (Same amount)
    - Payment of 1st annual rental (₹3,00,000):
      - Lease Liability A/c Dr. (Interest component + Principal repayment)
      - Interest Expense A/c Dr. (Calculated on opening Lease Liability @ 15%)
      - To Bank A/c ₹3,00,000
    - Depreciation on Right-of-Use Asset:
      - Depreciation Expense A/c Dr. (10% on Fair Value/PVMLP)
      - To Accumulated Depreciation A/c
- **Accounting (Lessor's Books - for 1st year):**
  - **Initial Recognition:** Lessor recognizes a Receivable equal to the Net Investment in the lease (Gross Investment discounted at IRR).
  - **Journal Entries (Lessor):**
    - On lease inception:
      - Lease Receivable A/c Dr.
      - To Machinery A/c (Fair Value/Cost)
      - To Unearned Finance Income A/c (Difference)
    - Receipt of 1st annual rental (₹3,00,000):
      - Bank A/c Dr. ₹3,00,000
      - To Lease Receivable A/c (Principal repayment)
      - To Finance Income A/c (Interest earned on net investment @ 15%)

- *No depreciation on machinery in lessor's books for a finance lease.*

5. (b) Anjana Ltd. has two departments A and B... Prepare complete Departmental Accounts including General Profit and Loss Account and Balance Sheet.

- **Steps:**
    1. **Departmental Trading Account:**
        - For each department (A and B), prepare a Trading Account.
        - Allocate Purchases and Sales to respective departments.
        - Calculate Gross Profit for each department.
    2. **Departmental Profit & Loss Account:**
        - Transfer Gross Profit to each department's P&L A/c.
        - Allocate common expenses (Director's Fees, Office Expenses, etc.) based on suitable criteria (e.g., Sales for Sales-related expenses, floor area for rent, etc.).
        - Calculate Net Profit for each department.
    3. **General Profit & Loss Account:**
        - Transfer Net Profits (or losses) from Departmental P&L A/cs.
        - Account for any non-departmental incomes (e.g., Income from Investments).
        - Calculate the overall Net Profit/Loss of the company.
    4. **Balance Sheet:**
        - **Liabilities:** Share Capital, Creditors, etc.
        - **Assets:** Stock (Department A & B), Furniture & Fitting (less depreciation), Office Expenses, Equipment, Cash at Bank, Cash in Hand.

OR

5. (a) Arjun Ltd. has three departments A, B and C... Prepare Departmental Trading A/C of Arjun Ltd. Assuming that the percentage of Gross Profit on Turnover is the same in each case.

- **Steps:**
    1. **Calculate Total Purchases and Sales (Units and Value):**

- Total Purchases (Units): 10,000 + 20,000 + 30,000 = 60,000 units.
- Total Sales (Units): 10,400 + 19,600 + 30,600 = 60,600 units.
- Total Purchases (Value): ₹9,59,000 (given).
- Total Sales (Value): (10,400*₹21) + (19,600*₹22) + (30,600*₹24) = ₹2,18,400 + ₹4,31,200 + ₹7,34,400 = ₹13,84,000.

2. **Calculate Overall Gross Profit Percentage on Turnover:**
    - Overall Cost of Goods Sold: Opening Stock (assume 0 unless given) + Total Purchases (₹9,59,000) - Total Closing Stock (calculate for each department).
    - Closing Stock (Units): A=800, B=1200, C=1400.
    - Closing Stock Value (Units Method): (Total Purchases Value / Total Purchases Units) * Closing Stock Units.
        - Cost per unit = ₹9,59,000 / 60,000 units = ₹15.9833 (approx).
        - Closing Stock A = 800 * 15.9833 = ₹12,786.64
        - Closing Stock B = 1200 * 15.9833 = ₹19,179.96
        - Closing Stock C = 1400 * 15.9833 = ₹22,376.62
    - Total Closing Stock Value = ₹12,786.64 + ₹19,179.96 + ₹22,376.62 = ₹54,343.22
    - Overall Cost of Goods Sold = ₹9,59,000 - ₹54,343.22 = ₹9,04,656.78
    - Overall Gross Profit = Total Sales (₹13,84,000) - Overall Cost of Goods Sold (₹9,04,656.78) = ₹4,79,343.22
    - Gross Profit Percentage on Turnover = (₹4,79,343.22 / ₹13,84,000) * 100 = **34.6346% (approx)**.
3. **Prepare Departmental Trading A/c:**
    - For each department, calculate Cost of Goods Sold using the derived GP % on Turnover (Sales * (1-GP%)).
    - This approach uses the assumption that GP% is same for all departments.

5. (b) Smitha Ltd. Availed a lease from Narayans Ltd...

- **(i) State whether the lease constitute finance lease and also calculate unearned finance income.**
    - **Finance Lease (AS 19):**

        - Lease period (3 years) vs. useful life (5 years) - major part.
        - Fair market value (₹10,00,000) vs. PVMLP (needs calculation using IRR 10% and annual payments).
        - Property reverts to lessor after termination.
        - Unguaranteed residual value (₹1,00,000).
        - Given IRR 10%.
    - **Conclusion:** Given the lease term is a major part of useful life and considering the present value factors for annual payments, it is likely a **Finance Lease**.
    - **Unearned Finance Income Calculation:**
        - Calculate PVMLP (PV of 3 equal annual payments using 10% IRR factors: 0.7513 for 3rd year, 2.4868 for annuity of 3 years). Let 'x' be the annual payment. PVMLP = x * 2.4868.
        - Fair Value = ₹10,00,000.
        - **Gross Investment:** Total of 3 annual payments + Unguaranteed Residual Value (₹1,00,000).
        - **Net Investment:** PVMLP.
        - **Unearned Finance Income = Gross Investment - Net Investment.**
- **(ii) Differentiate between Operating and Financial lease.**

Feature	**Operating Lease**	**Financial Lease**
Risk & Reward	Retained by Lessor.	Transferred substantially to Lessee.
Ownership	Remains with Lessor.	Can be transferred, or option to purchase.
Term	Shorter than asset's useful life.	Covers major part of asset's useful life.
Accounting	Lease rentals expensed by lessee.	Asset and liability recognized by lessee.
Depreciation	By Lessor.	By Lessee (on leased asset).
Nature	Like a rental agreement.	Like purchasing an asset with borrowed funds.