SUGGESTED SOLUTION

# INTER CA NOVEMBER 2018 EXAM

**SUBJECT- ACCOUNTS**

**Test Code - CIN 5007**

**BRANCH - () (Date : 05/08/2018)**

**Head Office :Shraddha, 3rd Floor, Near Chinai College, Andheri (E), Mumbai – 69.**

**Tel : (022) 26836666**

**Answer 1:**

**(A) Fellow Travellers Ltd.**

**Statement showing calculation of profit /losses for pre and post incorporation Periods**

| | Ratio | Pre-incorporation | Post-incorporation |
|---|---|---|---|
| Gross profit allocated on the basis of sale | 1:2 | 20,000 | 40,000 |
| Less:AdministrativeExpenses allocated | | | |
| On time basis: | | | |
| (i) Salariesandwages 10,000 | | | |
| (ii) Depreciation 1,000 | | | |
| 11,000 | 5:7 | 4,583 | 6,417 |
| Selling Commission on the basis of sales | 1:2 | 3,000 | 6,000 |
| Interest on Purchase Consideration | | | |
| (Time basis) | 5:1 | 7,500 | 1,500 |
| Expenses applicable wholly to the | | | |
| Post-incorporation period: | | | |
| DebentureInterest 5,250 (1,50,000 x 7% x 6/12) | | | |
| Director'sFee 600 | | | 5,850 |
| Preliminary expenses | | | 900 |
| Provision for taxes | | | 6,000 |
| Balance c/d to Balance Sheet | | 4,917 | 13,333 |

### Time Ratio

Pre incorporation period = 1 January 20X1 to 31 May 20X1 = 5 months Post incorporation period = 1 June 20X1 to 31 December 20X1 = 7 months Time ratio = 5:7

### Sales Ratio

Sales in pre incorporation period (1 January 20X1 to 31 May 20X1) = Rs.60,000
Sales in post incorporation period (1 June 20X1 to 31 December 20X1) = Rs.1,20,000
Sales ratio =1:2

Fellow Travellers Ltd.

Extract from the Balance Sheet as on 31st Dec.,20X1

| | Particulars | Notes | Rs: |
|---|---|---|---|
| | Equity and Liabilities | | |
| 1 | Shareholders' funds | | |
| a | **Share capital** | 1 | **2,00,000** |
| | **Reserves and Surplus** | 2 | **33,250** |
| 2 | Non-current liabilities | | |
| a | **Long-term borrowings** | 3 | **1,50,000** |

| | Current liabilities | | |
|---|---|---|---|
| 3 a | **Short term provisions** | **4** | **6,000** |
| | Total | | **3,89,250** |

Notes to accounts

| | | |
|---|---|---|
| 1. ShareCapital | | |
| 20,000 equity shares of Rs. 10 each fully paid | | 2,00,000 |
| 2. Reserves andSurplus | | |
| Profit Prior to Incorporation | | 4,917 |
| Securities Premium Account | | 20,000 |
| Profit andlossAccount | 13,333 | |
| Less: Dividend onequityshare | (5,000) | 8,333 |
| Total | | 33,250 |
| 3. Long termborrowings | | |
| Secured | | |
| 7% Debentures | | 1,50,000 |
| 4. Other Currentliabilities | | |
| Provision for Taxes | | 6,000 |

**(B)**

**i) Calculation of Interest and CashPrice**

| *No. of installments* | *Outstanding balance at the end after the payment ofinstallment* | *Amount due at the time of installment* | *Outstanding balance at the end before the payment of installment* | Interest | *Outstanding balance at thebeginning* |
|---|---|---|---|---|---|
| *[1]* | *[2]* | *[3]* | *[4] = 2 +3* | *[5] = 4 x 10/110* | *[6]4-5* |
| 3rd | - | 5,50,000 | 5,50,000 | 50,000 | 5,00,000 |
| 2nd | 5,00,000 | 4,90,000 | 9,90,000 | 90,000 | 9,00,000 |
| 1st | 9,00,000 | 4,20,000 | 13,20,000 | 1,20,000 | 12,00,000 |

Total cash price = Rs. 12,00,000+ 6,00,000 (down payment) = Rs. 18,00,000.

**(ii) In the books ofSrikumar**

**Cars Account**

| *Date* | *Particulars* | *Rs.* | *Date* | *Particulars* | *Rs.* |
|---|---|---|---|---|---|
| 1.4.2014 | To Fair Value Motors A/c | 18,00,000 | 31.3.2015 | By Depreciation A/c<br>By Balance c/d | 4,50,000<br>13,50,000 |
| | | 18,00,000 | | | 18,00,000 |
| 1.4.2015 | To Balance b/d | 13,50,000 | 31.3.2016 | By Depreciation A/c | 3,37,500 |

| | | | | By Balance c/d | 10,12,500 |
|---|---|---|---|---|---|
| | | 13,50,000 | | | 13,50,000 |
| 1.4.2016 | To Balance b/d | 10,12,500 | 31.3.2017 | By Depreciation A/c | 2,53,125 |
| | | | | By Fair ValueMotorsA/c (Value of 1 Car taken over after depreciation for 3 years @ 40% p.a.) [9,00,000-(3,60,000+2,16,000 + 1,29,600)] | 1,94,400 |
| | | | | By Loss transferred to ProfitandLoss A/c on surrender (Bal.fig.) | 1,85,288 |
| | | | | By Balancec/d ½ (10,12,500-2,53,125) | 3,79,687 |
| | | **10,12,500** | | | **10,12,500** |

**Answer 2:**

**(A)** Thedecisionofmakingprovisionfornon-movinginventoriesonthebasisoftechnical evaluation does not amount to change in accounting policy. Accounting policy of a company may require that provision for non-moving inventories should be made. The method of estimating the amount of provision may be changed in case a more prudent estimate can bemade.

In the givencase,consideringthetotalvalueofinventory,thechangeintheamountof required provision of non-moving inventory from Rs. 3.5 lakhs to Rs. 2.5 lakhs is also not material. The disclosure can be made for such change in the following lines by way of notes to the accounts in the annual accounts of ABC Ltd. for the year2016-17:

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

**(B)** AS-5on'NetProfitorLossforthePeriod,PriorPeriodItemsandChangesinAccounting Policies', defines Prior Period items as "income or expenses which arise in the current period as a result of errors or omissions in the preparation of the financial statements of one or more priorperiods".

Rectification of error in inventory valuation is a prior period item vide AS 5. Separatedisclosure of this item as a prior period item is required as per AS 5.

**(C) Capital Account of ShriMoti**

| | | 1-4-2015 | | 1-4-2017 |
|---|---|---|---|---|
| | Rs. | Rs. | Rs. | Rs. |
| **Assets** | | | | |
| Cash in hand | | 25,500 | | 16,000 |
| Inventory | | 56,000 | | 91,500 |
| Sundry debtors | | 41,500 | | 52,500 |
| Land & Building | | 1,90,000 | | 1,90,000 |

| | | | | |
|---|---|---|---|---|
| Wife's Jewellery | | 75,000 | | 1,25,000 |
| Motor Car | | — | | 1,25,000 |
| Loan to Moti's Brother | | — | | 20,000 |
| | | 3,88,000 | | 6,20,000 |
| **Liabilities:** | | | | |
| Owing to Moti's Brother | 40,000 | | — | |
| Sundry creditors | 35,000 | 75,000 | 55,000 | 55,000 |
| Capital | | 3,13,000 | | 5,65,000 |
| Income during the two years : | | | | |
| Capital as on 1-4-2017 | | | | 5,65,000 |
| Add: Drawings – Domestic Expenses for the two years (Rs. 4,000 × 24 months) | | | | 96,000 |
| | | | | 6,61,000 |
| Less: Capital as on 1-4-2015 | | | | (3,13,000) |
| Income earned in 2015-2016 and 2016-2017 | | | | 3,48,000 |
| Income declared (Rs. 1,05,000 + Rs. 1,23,000) | | | | 2,28,000 |
| Suppressed Income | | | | 1,20,000 |

The Income-tax officer's contention that ShriMoti has not declared his true income is correct. ShriMoti's true income is in excess of the disclosed income by Rs. 1,20,000.

**Answer 3:**

**(A) Calculation of unrealised profit of each department and total unrealized profit**

| | DepartmentA (Rs. ) | DepartmentB (Rs. ) | DepartmentC (Rs. ) | Total (Rs. ) |
|---|---|---|---|---|
| Unrealised Profit of: | | | | |
| Department A | | 45,000 x 50/150 = 15,000 | 42,000 x 20/120 = 7,000 | 22,000 |
| Department B | 40,000 x .25 = 10,000 | | 72,000 x .15 = 10,800 | 20,800 |
| Department C | 39,000 x 30/130 = 9,000 | 42,000 x 40/140 = 12,000 | | 21,000 |
| | | | | 63,800 |

**(B)** Constructingoracquiringanewassetmayresultinincrementalcoststhatwouldhave been avoided if the asset had not been constructed or acquired. The costs are not to be included in the cost of the asset if they are not directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the mannerintendedbymanagement.Thecoststobeincurredbythecompanyareinthe nature of costs of relocating or reorganizing operations of the company and do not meet the requirement of AS 10 (Revised) and therefore, cannot be capitalized.

**(C) In the books of Head Office**

| | Rs. | | Rs. |
|---|---|---|---|
| To Balance b/d | | By Stock reserve (opening) | 6,000 |
| Stock | 30,000 | By Remittances: | |
| Debtors | 18,000 | Cash Sales 1,00,000 | |
| Cash in hand | 800 | Cash from Debtors 60,000 | 1,60,000 |
| Furniture | 3,000 | By Goods sent to branch (loading) | 32,000 |
| To Goods sent to branch | 1,60,000 | By Goods returned by branch (Return to H.O.) | 2,000 |
| To Goods returned by branch (loading) | 400 | By Balance c/d | |
| | | Stock | 28,000 |
| To Bank (expenses paid by H.O.) | | Debtors | 16,880 |
| Rent 1,800 | | Cash (800-600) | 200 |
| Salary 3,200 | | Furniture (3,000-300) | 2,700 |
| Stationary & printing 800 | 5,800 | | |
| To Stock reserve (closing) | 5,600 | | |
| To Profit transferred to General Profit & Loss A/c | 24,180 | | |
| | **2,47,780** | | **2,47,780** |

**Working Note:**

**Debtors Account**

| | Rs. | | Rs. |
|---|---|---|---|
| To Balance b/d | 18,000 | By Cash account | 60,000 |
| To Sales account (credit) | 60,000 | By Sales return account | 960 |
| | | By Discount allowed account | 160 |
| | | By Balance c/d | 16,880 |
| | 78,000 | | 78,000 |

**Note:** It is assumed that goods returned by branch are at invoice price.

**Answer 4:**

(A) As per the amendment in AS 4 "Contingencies and Events Occurring After the Balance Sheet Date" vide Companies (Accounting Standards) Amendments Rules, 2016 dated 30th March, 2016, the events which take place after the balance sheet date, are sometimes reflected in the financial statements because of statutory requirements or because of their special nature.

However, dividends declared after the balance sheet date but before approval of financial statements are not recognized as a liability at the balance sheet date because no statutory obligation exists at that time. Hence such dividends are disclosed in the notes to financial statements.

Provision for proposed dividends is not required to be made as per the amendment in AS 4. Such proposed dividends are to be disclosed in the notes to financial statements. Accordingly, the dividend of Rs. 4 crores recommended by New Graphics Ltd. in its Board meeting on 18th April, 2017 shall not be accounted for in the books for the year 2016-17 irrespective of the fact that it pertains to the year 2016-17 and will be paid after approval in the Annual General Meeting of the members/shareholders.

**(B) In the books of RamLtd.**

**If the grant is credited to Fixed Assets Account:**

**i. Journal Entry (at the time of refund ofgrant)**

| | | Inlakhs Rs. | Inlakhs Rs. |
|---|---|---|---|
| I | Fixed Assets Dr.<br>To Bank A/c<br>(Being grant refunded) | 32 | <br>32 |

**ii. ValueofFixedAssetsaftertwoyearsbutbeforerefundofgrant**

Fixed assets initially recorded in the books = Rs. 80 lakhs – Rs. 32 lakhs

= Rs. 48 lakhs

Depreciation for each year = (Rs. 48 lakhs – Rs.8 lakhs)/4 years

= Rs. 10 lakhs per year for first two years.

Value of the assets before refund of grant =Rs. 48 lakhs - Rs. 20 lakhs

= Rs. 28 lakhs

**iii. Value of Fixed Assets after refund ofgrant**

| | |
|---|---|
| Value of Fixed Assets before refund ofgrant | Rs. 28lakhs |
| Add Refundofgrant | Rs. 32lakhs |
| | Rs. 60lakhs |

**iv. Amount of depreciation for remaining twoyears**

Value of the fixed assets after refund of grant –residual value of the assets / No. of years

= Rs. 60 lakhs - Rs. 8 lakhs / 2

= Rs. 26 lakhs per annum will be charged for next two years.

**(C) Shri Ramesh**

**Trading Account for 20X1**
**(to determine the rate of gross profit)**

| | | Rs. | | | Rs. | Rs. |
|---|---|---|---|---|---|---|
| To | Opening Stock | 73,500 | By | SalesA/c | | 4,87,000 |
| To | Purchases | 3,98,000 | By | Closing Stock : | | |
| To | Gross Profit (b.f.) | 97,400 | | Asvalued | 79,600 | |
| | | | | Add : Amount written off to restore stock to full cost | 2,300 | 81,900 |
| | | 5,68,900 | | | | 5,68,900 |

$$\text{The(normal)rateofgrossprofittosalesis} = \frac{97,400}{4,87,000} \times 100 = 20\%$$

**Memorandum Trading Account upto March 31, 20X2**

| | Normal items | Abnormal items | Total | | Normal items | Abnormal items | Total items |
|---|---|---|---|---|---|---|---|
| | Rs. | Rs. | Rs. | | Rs. | Rs. | Rs. |
| To Opening Stock | 75,000 | 6,900* | 81,900 | By Sales<br>By Loss | 2,28,000<br>— | 3,200<br>250 | 2,31,200<br>250 |
| To Purchases | 1,62,000 | — | 1,62,000 | By Closing | | | |
| To Gross Profit | | | | Stock (bal. fig.) | | | |
| (20% on Rs. 2,28,000) | 45,600 | — | 45,600 | | 54,600 | 3,450** | 58,050 |
| | 2,82,600 | 6,900 | 2,89,500 | | 2,82,600 | 6,900 | 2,89,500 |

* at cost, book value is Rs. 4,600

** Book value will also be restored for remaining unsold abnormal stock since the remainder of this stock was now estimated to be worth its original cost.

**Calculation of Insurance Claim**

| | |
|---|---|
| Value of Stock on March 31, 20X2 | 58,050 |
| Less : Salvage | (5,800) |
| Loss of stock | 52,250 |

**Claim Subject to average clause:**

=(Amount of policy / Value of stock) * Actual loss of stock

= (50000 / 58050) * 52250

= 45004

**Answer 5:**

**(A) Statement showing calculation of profits for pre and post incorporation periods for the year ended 31.3.20X2**

| | | |
|---|---|---|
| Gross profit (1:3) | 80,000 | 2,40,000 |
| Less: Salaries (1:2) | 16,000 | 32,000 |
| Stationery (1:2) | 1,600 | 3,200 |
| Advertisement (1:3) | 4,000 | 12,000 |
| Travelling expenses | 4,000 | 8,000 |
| (W.N.4) | 1,200 | 3,600 |
| Sales promotion expenses | 12,600 | 25,200 |
| (W.N.4) Misc. trade expenses (1:2) | 8,000 | 18,400 |
| Rent (office building) | 1,400 | 2,800 |
| (W.N.3) Electricity charges | - | 11,200 |
| (1:2) | 800 | 2,400 |
| Director's fee (post-incorporation) | 4,000 | 12,000 |
| Bad debts (1:3) | 1,500 | 4,500 |
| Selling agents commission (1:3) | - | 3,000 |
| Audit fee (1:3) | 2,800 | 1,400 |
| Debenture interest (post-incorporation) | 6,300 | 18,900 |
| Interest paid to vendor (2:1) (W.N.5) | | |
| Selling expenses (1:3) | | |
| Depreciation on fixed assets (W.N.6) | 3,000 | 6,600 |
| Capital reserve (Bal.Fig.) | 12,800 | - |
| Net profit (Bal.Fig.) | - | 74,800 |

**WorkingNotes:**

**1. TimeRatio**

Pre incorporation period = 1st April, 20X1 to 31st July, 20X1

i.e. 4 months

Post incorporation period is 8 months

Time ratio is 1: 2.

**2. Salesratio**

**Let the monthly sales for first 6 months (i.e. from 1.4.20X1 to 30.09.20X1) be x Then, sales for 6 months = 6x**

**Monthly sales for next 6 months (i.e. from 1.10.X1 to 31.3.20X2) = x + 2x/3 = 5x/3**

Then ,sales for next 6 months = (5x / 3 * 6) = 10x

Total sales for the year = 6x + 10x = 16x

Monthly sales in the pre incorporation period = Rs. 19,20,000/16 = Rs. 1,20,000

Total sales for pre-incorporation period = Rs. 1,20,000 x 4 = Rs. 4,80,000

Total sales for post incorporation period = Rs. 19,20,000 – Rs. 4,80,000 = Rs. 14,40,000 Sales Ratio = 4,80,000 : 14,40,000 = 1 : 3

**3. Rent**

| | | |
|---|---|---|
| **Rent for pre-incorporation period (Rs. 2,000 x 4) Rent for post incorporation period August,20X1 & September, 20X1 (Rs. 2,000 x2)** | **4,000** | **8,000(pre)** |
| **October,20X1 to March,20X2 (Rs. 2,400 x 6)** | **14,400** | **18,400(post)** |

4. Travelling expenses and sales promotionexpenses

| | | |
|---|---|---|
| **Traveling expenses Rs. 12,000 (i.e. Rs. 16,800- Rs. 4,800) distributed in Time ratio (1:2)** | **4,000** | **8,000** |
| **Sales promotion expenses Rs. 4,800 distributed in Sales ratio (1:3)** | **1,200** | **3,600** |

5. Interest paid to vendor till 30th September,20X1

| | | |
|---|---|---|
| **Interest for pre-incorporation period (4200/6)*4** | **2,800** | |
| **Interest for post incorporation period i.e. for August, 20X1 & September, 20X1 = (4200 / 6) * 2** | | **1,400** |

**6. Depreciation**

| | | |
|---|---|---|
| | | |
| **Total depreciation** **9,600**<br>**Less:Depreciationexclusivelyforpostincorporationperiod** **(600)**<br>**Remaining (for pre and postincorporationperiod) 9,000**<br><br>**Depreciationforpre-incorporationperiod (9000/4)*12**<br><br>**Depreciationforpostincorporationperiod (9000/8)*12**<br>*** Time ratio = 1:2** | **3000** | **600**<br><br>**6,000** |
| | **3000** | **6,600** |

(B) In the Books of M/s Omega

Departmental Trading and Profit and Loss Account
for the year ended 31st March, 20X1

| Particulars | Deptt. X | Deptt. Y | Deptt.Z | Total | Particulars | Deptt.X | Deptt.Y | Deptt. Z | Total |
|---|---|---|---|---|---|---|---|---|---|
| | Rs. | Rs. | Rs. | Rs. | | Rs. | Rs. | Rs. | Rs. |
| To Stock (opening) | 36,000 | 24,000 | 20,000 | 80,000 | By Sales | 1,80,000 | 1,35,000 | 90,000 | 4,05,000 |
| To Purchases | 1,32,000 | 88,000 | 44,000 | 2,64,000 | By Stock (closing) | 45,000 | 17,500 | 21,000 | 83,500 |
| To Carriage Inwards | 1,500 | 1,000 | 500 | 3,000 | | | | | |
| To Gross Profit c/d (b.f.) | 55,500 | 39,500 | 46,500 | 1,41,500 | | | | | |
| | 2,25,000 | 1,52,500 | 1,11,000 | 4,88,500 | | 2,25,000 | 1,52,500 | 1,11,000 | 4,88,500 |
| To Carriage Outwards | 1,200 | 900 | 600 | 2,700 | By Gross Profit b/d | 55,500 | 39,500 | 46,500 | 1,41,500 |
| To Electricity | 1,500 | 1,000 | 500 | 3,000 | By Discount received | 900 | 600 | 300 | 1,800 |
| To Salaries | 20,000 | 16,000 | 12,000 | 48,000 | | | | | |
| To Advertisement | 1,200 | 900 | 600 | 2,700 | | | | | |
| To Discount allowed | 1,000 | 750 | 500 | 2,250 | | | | | |
| To Rent, Rates and Taxes | 3,000 | 2,500 | 2,000 | 7,500 | | | | | |
| To Depreciation | 400 | 400 | 200 | 1,000 | | | | | |
| To Provision for Bad Debts @ 5% of debtors | 750 | 500 | 500 | 1,750 | | | | | |

| | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|
| To Labour welfare expenses | 1,000 | 800 | 600 | 2,400 | | | | | |
| To Net Profit (b.f.) | 26,350 | 16,350 | 29,300 | 72,000 | | | | | |
| | 56,400 | 40,100 | 46,800 | 1,43,300 | | 56,400 | 40,100 | 46,800 | 1,43,300 |

**Working Note:**

| Basis of allocation of expenses | |
|---|---|
| Carriage inwards | Purchases (3:2:1) |
| Carriage outwards | Turnover (4:3:2) |
| Salaries | No. of Employees (5:4:3) |
| Advertisement | Turnover (4:3:2) |
| Discount allowed | Turnover (4:3:2) |
| Discount received | Purchases (3:2:1) |
| Rent, Rates and Taxes | Floor Space occupied (6:5:4) |
| Depreciation on furniture | Value of furniture (2:2:1) |
| Labour welfare expenses | No. of Employees (5:4:3) |
| Electricity expense | Units consumed (3:2:1) |
| Provision for bad debts | Debtors balances (3:2:2) |

**Answer 6:**

**(A)** (i) Interest for the period2016-17

= US $ 10 lakhs x 4% × Rs. 62 per US$ = Rs. 24.80 lakhs

(ii)(ii) (ii)

Increaseintheliabilitytowardstheprincipalamount

US $10 lakhs× Rs. (62 - 56) = Rs. 60 lakhs

(iii) Interestthatwouldhaveresultediftheloanwastakeninlndiancurrency

= US $ 10 lakhs × Rs. 56 x 10.5% = Rs. 58.80 lakhs

(iv) Difference between interest on local currency borrowing and foreign currencyborrowing
= Rs. 58.80 lakhs- Rs. 24.80 lakhs = Rs. 34 lakhs.

Therefore, out of Rs. 60 lakhs increase in the liability towards principal amount, only Rs. 34 lakhs will be considered as the borrowing cost. Thus, total borrowing cost would be Rs. 58.80 lakhs being the aggregate of interest of Rs. 24.80 lakhs on foreign currency borrowings plus the exchange difference to the extent of difference between interest on local currency borrowing and interest on foreign currency borrowing of Rs. 34 lakhs.

Hence, Rs. 58.80 lakhs would be considered as the borrowing cost to be accounted for as per AS 16 and the remaining Rs. 26 lakhs (60 - 34) would be considered as the exchange difference to be accounted for as per AS11.

**(B)** XLtd. InvestedRs.600lakhsintheequitysharesofYLtd.Outofthesame,the company intends to hold 50% shares for long term period i.e. Rs. 300 lakhs and remaining as temporary(current)investmenti.e.Rs.300lakhs.Irrespectiveofthefactthatinvestment hasbeenheldbyXLtd. Onlyfor3months(from1.1.2017to31.3.2017),AS-13(Revised) laysemphasisonintentionoftheinvestortoclassifytheinvestmentascurrentorlong term even though the long term investment may be readily marketable.

In the given situation, the realizable value of all such investments on 31.3.2017 became Rs. 200 lakhs i.e. Rs. 100 lakhs in respect of current investment and Rs. 100 lakhs in respect of long term investment.

As per AS 13 (Revised), 'Accounting for Investment', the carrying amount for current investments is the lower of cost and fair value. In respect of current investments for which an active market exists, market value generally provides the best evidence of fair value. Accordingly, the carrying value of investment held as temporary investment shouldbeshownatrealisablevaluei.e.atRs.100lakhs.ThereductionofRs.200lakhsinthe carrying value of current investment will be charged to the profit and loss account.

Standard further states that long-term investments are usually carried at cost. However, when there is a decline, other than temporary, in the value of long term investment, the carrying amount is reduced to recognize the decline.

Here, Y Ltd. lost a case of copyright which drastically reduced the realizable value of its shares to one third which is quiet a substantial figure. Losing the case of copyright may affect the business and the performance of the company in long run. Accordingly, it will be appropriate to reduce the carrying amount of long term investment by Rs.200 lakhs and show the investments at Rs.100lakhs, since the downfall in the value of shares is other than temporary. The reduction of Rs.200 lakhs in the carrying value of long term investment will also be charged to the Statement of profit and loss.

**(C) (i) Computation of average accumulated expenses**

| | | Rs. |
|---|---|---|
| Rs.2,00,000 x 12 / 12 | = | 2,00,000 |
| Rs.2,50,000 x 9 / 12 | = | 1,87,500 |
| Rs.4,50,000 x 6 / 12 | = | 2,25,000 |
| Rs.1,20,000 x 1 / 12 | = | 10,000 |
| | | 6,22,500 |

**(ii) Calculation of average interest rate other than for specific borrowings**

| Amount of loan (Rs.) | Rate of interest | | Amount ofinterest (Rs.) |
|---|---|---|---|
| 5,00,000 | 11% | = | 55,000 |
| 9,00,000 | 13% | = | 1,17,000 |
| 14,00,000 | | | 1,72,000 |
| Weighted average rate of interest $\left(\frac{1,72,000}{14,00,000}\right)\times100$ | | = | 12.285% (approx) |

**(iii) Interest on average accumulatedexpenses**

| | | Rs. |
|---|---|---|
| Specific borrowings (Rs.1,00,000x10%) | = | 10,000 |
| Non-specific borrowings (Rs.5,22,500*x12.285%) | = | 64,189 |
| Amount of interest tobecapitalised | = | 74,189 |

(iv) Total expenses to be capitalised forbuilding

| | Rs. |
|---|---|
| **Cost of building** Rs.**(2,00,000 + 2,50,000 + 4,50,000 + 1,20,000)**<br><br>**Add: Amount of interest to be capitalised** | **10,20,000**<br><br>**74,189** |
| | **10,94,189** |

(v) Journal Entry

| Date | Particulars | | Dr. (Rs.) | Cr. (Rs.) |
|---|---|---|---|---|
| **31.12.2016** | **Building account To Bank account**<br><br>**(Being amount of cost of building and borrowing cost thereon capitalised)** | **Dr.** | **10,94,189** | **10,94,189** |

* (Rs.6,22,500 – Rs.1,00,000)

**(D)** Yes, one of the characteristics of financial statements is neutrality. To be reliable, the information contained in financial statement must be neutral, that is freefrom bias.

Financial Statements are not neutral if by the selection or presentation of information, the focus of analysis could shift from one area of business to another thereby arriving at a totally different conclusion on the business results.

For example, if the assets of a company primarily consist of trade receivables and insurance claims and the financial statements do not specify that the insurance claims have been lying unrealized for a number of years or that a few key trade receivables have not given balance confirmation certificates, an erroneous conclusion may be drawn on the liquidity of the company. Financial statements are said to depict the true and fair view of the business of the organization by virtue of neutrality.