ADVANCED ACCOUNTING

(New Syllabus)

Prof. Rahul Malkan

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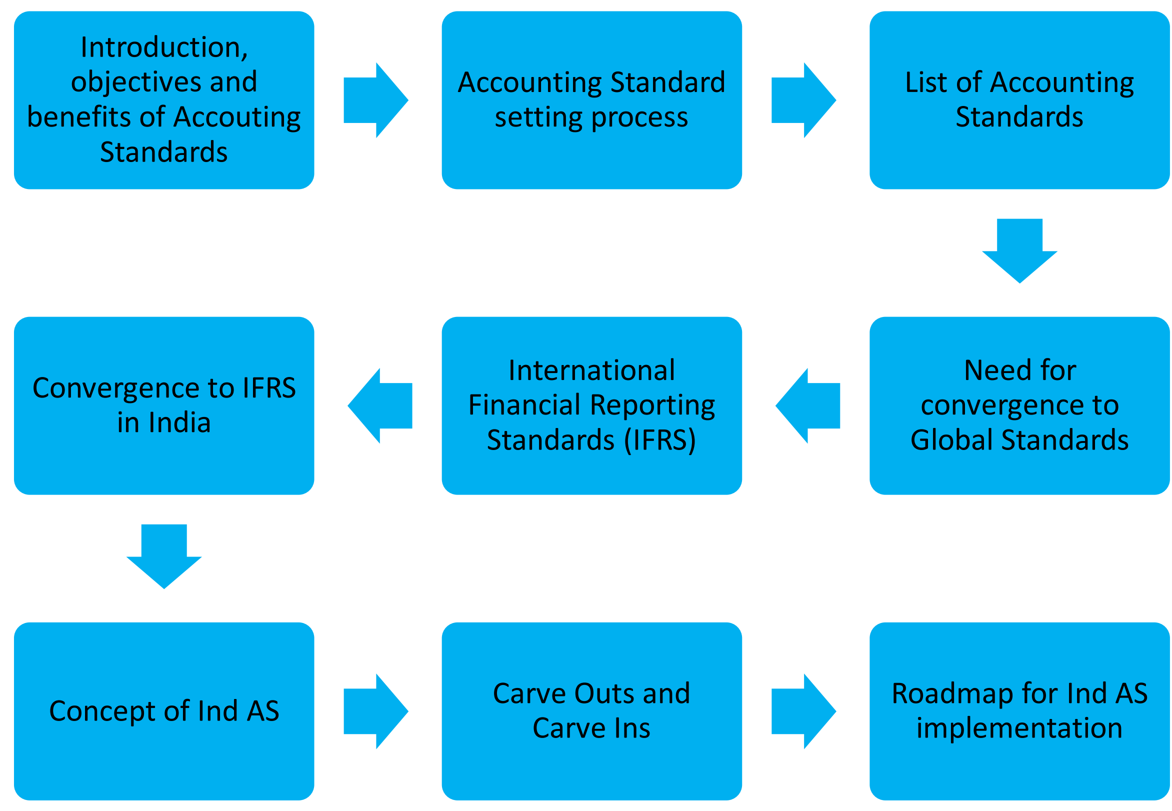
Chapter 1

INTRODUCTION TO ACCOUNTING STANDARD

CHAPTER DESIGN

1. INTRODUCTION
2. BENEFITS OF ACCOUNTING STANDARDS
3. STANDARD SETTING PROCESS
4. ACCOUNTING STANDARDS
5. NEED FOR CONVERGENCE TOWARDS GLOBAL STANDARDS
6. INTERNATIONAL ACCOUNTING STANDARD BOARD
7. INTERNATIONAL FINANCIAL REPORTING STANDARDS
8. WHAT ARE CARVE OUTS/INS IN IND AS?
9. WHAT ARE INDIAN ACCOUNTING STANDARDS (IND AS)
10. GOVERNMENT OF INDIA'S COMMITMENT TO IND AS
11. LIST OF IND AS

CHAPTER OVERVIEW



1. INTRODUCTION :

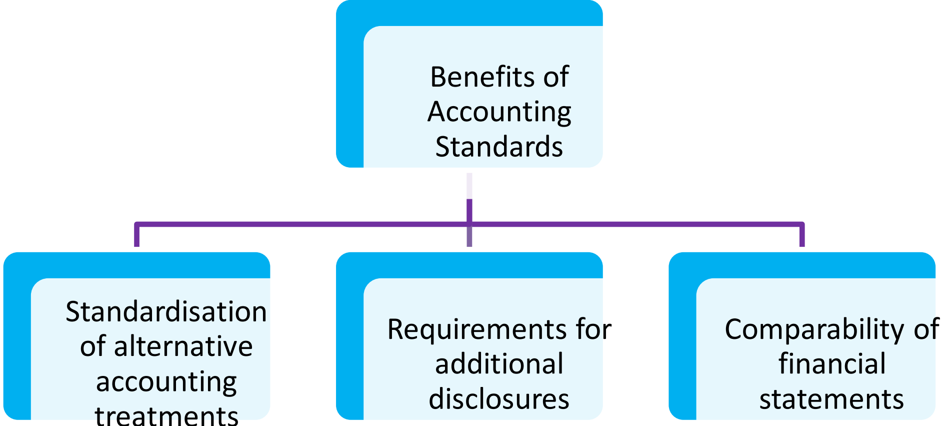
Generally accepted accounting principles (GAAP) refer to a common set of accepted accounting principles, standards, and procedures that business reporting entity must follow when it prepares and present its financial statements.

At international level such authoritative standards are known as International Financial Reporting Standards (IFRS) and in India we have authoritative standards named as AS and IND-AS.

Accounting Standards Deal with			
Recognition of events and transactions	Measurement of trasaction and Events	Presentation of transactions and Events	Disclosure requirements

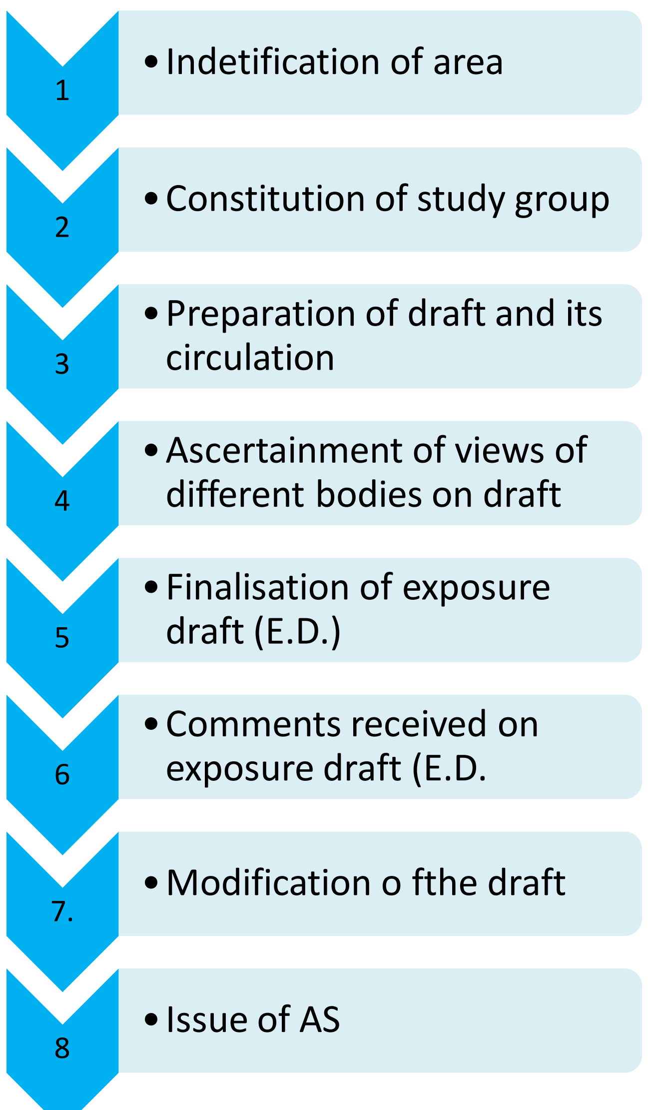
2. BENEFITS OF ACCOUNTING STANDARDS :

1. Standardisation of alternative accounting treatments:
2. Requirements for additional disclosures:
3. Comparability of financial statements:



3. STANDARD SETTING PROCESS :

The Institute of Chartered Accountants of India (ICAI), being a premier accounting body in the country, took upon itself the leadership role by constituting the Accounting Standards Board (ASB) in 1977.



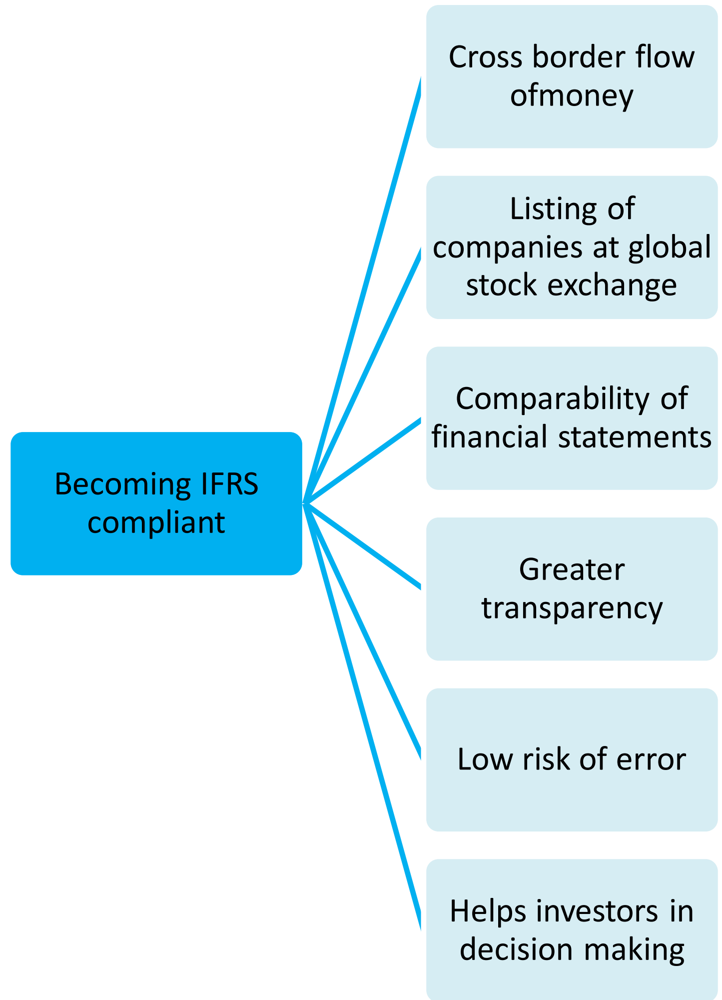
4. ACCOUNTING STANDARDS :

AS No	AS title	Date
1.	Disclosure of Accounting Policies	01/04/1993
2.	Valuation of Inventories (Revised)	01/04/1999
3.	Cash Flow Statement	01/04/2001
4.	Contingencies and Events Occurring after the Balance Sheet Date (Revised)	01/04/1998
5.	Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies	01/04/1996
7.	Construction Contracts	01/04/2002
9.	Revenue Recognition	01/04/1993
10.	Property, Plant and Equipment (Revised)	01/04/2016
11.	The Effects of Changes in Foreign Exchange Rates	01/04/2004
12.	Accounting for Government Grants	01/04/1994
13.	Accounting for Investments (Revised)	01/04/1995
14.	Accounting for Amalgamations (Revised)	01/04/1995
15.	Employee Benefits	01/04/2006
16.	Borrowing Costs	01/04/2000
17.	Segment Reporting	01/04/2001
18	Related Party Disclosures	01/04/2001
19.	Leases	01/04/2001
20	Earnings per share	01/04/2001
21.	Consolidated Financial Statements (Revised)	01/04/2001
22.	Accounting for Taxes on Income	01/04/2006
23.	Accounting for Investments in Associates in Consolidated Financial Statements	01/04/2002
24.	Discontinuing Operations	01/04/2004
25.	Interim Financial Reporting	01/04/2002
26	Intangible Assets	01/04/2003
27.	Financial Reporting of Interests in Joint Ventures	01/04/2002
28.	Impairment of Assets	01/04/2008
29.	Provisions, Contingent Liabilities and Contingent Assets (Revised)	01/04/2004

NOTE: AS 1; AS 2 (Revised); AS 3; AS 10 (Revised); AS 11; AS 12; AS 13 (Revised); AS 16 are covered in the syllabus of this paper at Intermediate Level.

5. NEED FOR CONVERGENCE TOWARDS GLOBAL STANDARDS :

1. **Standardization :** A single set of accounting standard would enable standardization. In fact, they establish broad rules rather than dictating specific treatments. Standardization would ensure better quality of financial statements.
2. **International capital Flow :** It would also permit international capital to flow more freely, enabling companies to develop consistent global practices on accounting problems.
3. **Beneficial to regulators :** It would be beneficial to the regulators too, as complexity associated with understanding various reporting regimes would be reduced.



6. INTERNATIONAL ACCOUNTING STANDARD BOARD :

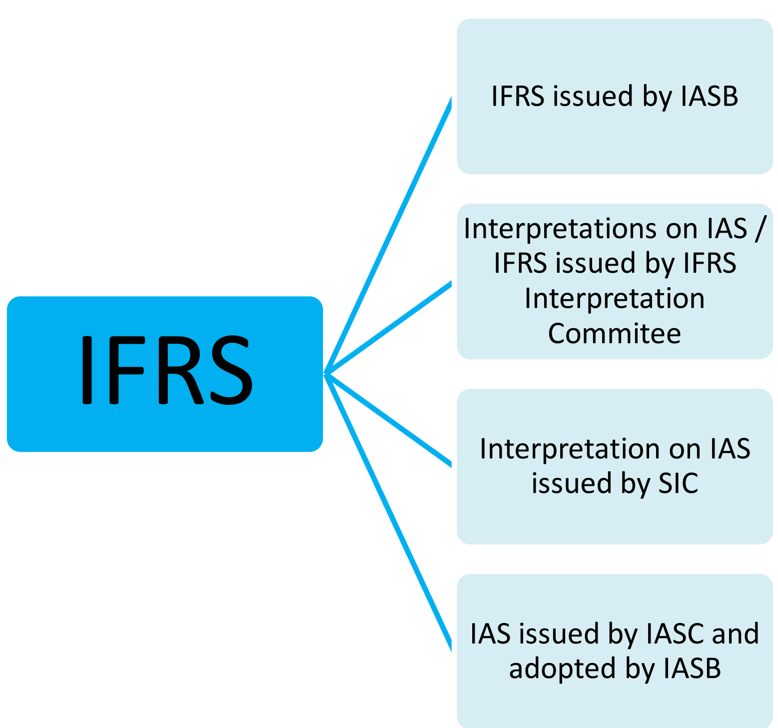
With a view of achieving these objectives, the London based group namely the International Accounting Standards Committee (IASC), responsible for developing International Accounting Standards, was established in June, 1973. It is presently known as International Accounting Standards Board (IASB), The IASC comprises the professional accountancy bodies of over 75 countries (including the Institute of Chartered Accountants of India).

Between 1973 and 2001, the International Accounting Standards Committee (IASC) released International Accounting Standards. Between 1997 and 1999, the IASC restructured their

organisation, which resulted in formation of International Accounting Standards Board (IASB). These changes came into effect on 1st April, 2001. Subsequently, IASB issued statements about current and future standards IASB publishes its Standards in a series of pronouncements called International Financial Reporting Standards (IFRS). However, IASB has not rejected the standards issued by the ISAC. Those pronouncements continue to be designated as "International Accounting Standards" (IAS).

7. INTERNATIONAL FINANCIAL REPORTING STANDARDS :

International Accounting Standards (IAS) (Upto April 2001) / International Financial Reporting Standards (IFRS) (Collectively referred as IFRS) issued by International Accounting Standards Board (IASB) since 1973 are now widely recognised as Global Accounting Standard. Note : Standing Interpretation Committee (SIC) and International Financial Reporting Interpretation Committee (IFRIC) are also part of IFRS.



8. WHAT ARE CARVE OUTS/INS IN IND AS? :

The Government of India in consultation with the ICAI decided to converge and not to adopt IFRS issued by the IASB. The decision of convergence rather than adoption was taken after the detailed analysis of IFRS requirements and extensive discussion with various stakeholders.

Accordingly, while formulating IFRS converged Indian Accounting Standards (Ind AS), efforts have been made to keep these Standards, as far as possible, in line with the corresponding IAS/IFRS and departures have been made where considered absolutely essential. These changes have been made considering various factors, such as

- Various terminology related changes have been made to make it consistent with the terminology used in law, e.g., 'statement of profit and loss' in place of 'statement of comprehensive income' and 'balance sheet' in place of 'statement of financial position'.

- Removal of options in accounting principles and practices in Ind AS vis-a-vis IFRS, have been made to maintain consistency and comparability of the financial statements to be prepared by following Ind AS. However, these changes will not result into carve outs
- Certain changes have been made considering the economic environment of the country, which is different as compared to the economic environment presumed to be in existence by IFRS. These differences are due to differences in economic conditions prevailing in India. These differences which are in deviation to the accounting principles and practices stated in IFRS, are commonly known as 'Carve-outs'.
- Additional guidance given in Ind AS over and above what is given in IFRS, is termed as 'Carve in'.

9. WHAT ARE INDIAN ACCOUNTING STANDARDS (IND AS) :

Indian Accounting Standards (Ind AS) are IFRS converged standards issued by the Central Government of India under the supervision and control of Accounting Standards Board (ASB) of ICAI and in consultation with NFRA.

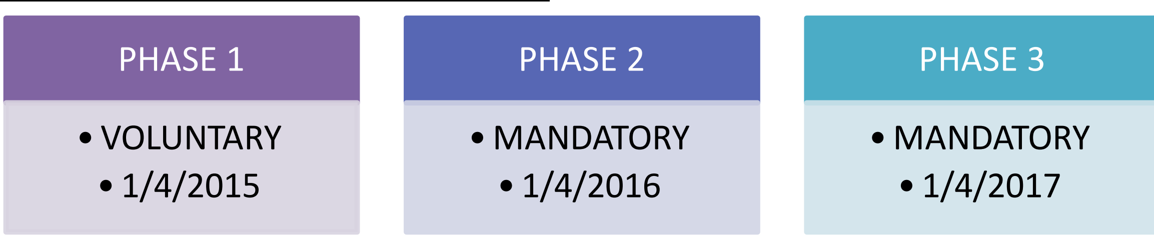
Indian Accounting Standards			
Globalisation and Liberalisation	Transparency of Financial Statements	Comparability of Financial Statements	Enhanced Disclosure requirements

10. GOVERNMENT OF INDIA'S COMMITMENT TO IND AS :

Consistent, comparable and understandable financial reporting is essential to develop a robust economy. With a view to achieve international benchmarks of financial reporting, the Institute of Chartered Accountants of India (ICAI), as a proactive role in accounting, set out to introduce Indian Accounting Standards (Ind AS) converged with the International Financial Reporting Standards (IFRS). This endeavour of the ICAI is supported by the Government of India.

Initially Ind AS were expected to be implemented from the year 2011. However, keeping in view the fact that certain issues including tax issues were still to be addressed, the Ministry of Corporate Affairs decided to postpone the date of implementation of Ind AS.

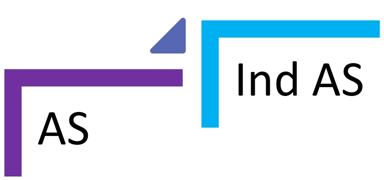
ROAD MAP TO IMPLEMENTATION OF IND AS



PHASE 1	1st April 2015 or thereafter: Voluntary Basis for all companies

PHASE 2	1st April 2016: Mandatory Basis	
	A	Companies listed / in process of listing on Stock Exchanges in India or Outside India having net worth =/> 500 crore
	B	Unlisted Companies having net worth =/> 500 crore
	C	Parent, Subsidiary, Associate and Joint venture of above
PHASE 3	1st April 2017: Mandatory Basis	
	A	All companies which are listed/or in process of listing inside or outside India on Stock Exchanges not covered in Phase I (other than companies listed on SME Exchanges)
	B	Unlisted companies having net worth =/> 250 crore
	C	Parent, Subsidiary, Associate and Joint venture of above

11. LIST OF IND AS :



No	Ind AS
1	Ind AS 101 : First-time Adoption of Indian Accounting Standards
2	Ind AS 102 : Share-based Payment
3	Ind AS 103 : Business Combinations
4	Ind AS 104 : Insurance Contracts
5	Ind AS 105 : Non-current Assets Held for Sale and Discontinued Operations
6	Ind AS 106 : Exploration for and Evaluation of Mineral Resources
7	Ind AS 107 : Financial Instruments: Disclosures
8	Ind AS 108 : Operating Segments
9	Ind AS 109 : Financial Instruments
10	Ind AS 110 : Consolidated Financial Statements
11	Ind AS 111 : Joint Arrangements
12	Ind AS 112 : Disclosure of Interests in Other Entities
13	Ind AS 113 : Fair Value Measurement
14	Ind AS 114 : Regulatory Deferral Accounts
15	Ind AS 1 : Presentation of Financial Statements

16	Ind AS 2 : Inventories
17	Ind AS 7 : Statement of Cash Flows
18	Ind AS 8 : Accounting Policies, Changes in Accounting Estimates and Errors
19	Ind AS 10 : Events after the Reporting Period
20	Ind AS 11 : Construction Contracts
21	Ind AS 12 : Income Taxes
22	Ind AS 16 : Property, Plant and Equipment
23	Ind AS 17 : Leases
24	Ind AS 18 : Revenue
25	Ind AS 19 : Employee Benefits
26	Ind AS 20 : Accounting for Government Grants and Disclosure of Government Assistance
27	Ind AS 21 : The Effects of Changes in Foreign Exchange Rates
28	Ind AS 23 : Borrowing Costs
29	Ind AS 24 : Related Party Disclosures
30	Ind AS 27 : Separate Financial Statements
31	Ind AS 28 : Investments in Associates and Joint Ventures
32	Ind AS 29 : Financial Reporting in Hyperinflationary Economies
33	Ind AS 32 : Financial Instruments: Presentation
34	Ind AS 33 : Earnings per Share
35	Ind AS 34 : Interim Financial Reporting
36	Ind AS 36 : Impairment of Assets
37	Ind AS 37 : Provisions, Contingent Liabilities and Contingent Assets
38	Ind AS 38 : Intangible Assets
39	Ind AS 40 : Investment Property
40	Ind AS 41 : Agriculture

MCQs :

1. Accounting Standards for non-corporate entities in India are issued by
   - (a) Central Govt.
   - (b) State Govt.
   - (c) Institute of Chartered Accountants of India.
2. Accounting Standards

(a) Harmonise accounting policies and eliminate the non-comparability of financial statements.

(b) Improve the reliability of financial statements.

(c) Both (a) and (b).

3. It is essential to standardize the accounting principles and policies in order to ensure

(a) Transparency. (b) Consistency.

(c) Both (a) and (b).

4. Which committee is responsible for approval of accounting standards and their modification for the purpose of applicability to companies?

(a) NFRA.

(b) MCA.

(c) Central Government Advisory Committee.

5. Global Standards facilitate

(a) Cross border flow of money.

(b) Comparability of financial statements.

(c) Both (a) and (b).

6. Additional guidance given in Ind AS over and above what is given in IFRS are called

(a) Carve-outs. (b) Carve-ins.

(c) Carve clarifications.

7. IASB stands for

(a) International Accounting Standards Bureau

(b) International Advisory Standards Board

(c) International Accounting Standard Board.

8. IFRS stands for

(a) International Financial Reporting System

(b) International Finance Reporting Standard

(c) International Financial Reporting Standard.

9. Phase I of Ind AS was applicable to:

(a) All listed companies in India or outside India

(b) Companies with turnover INR 500 crores or more

(c) Companies with net worth INR 500 crores or more.

Thanks ....

Rahul Malkan

Chapter 2

FRAMEWORK FOR PREPARATION & PRESENTATION OF FINANCIAL STATEMENTS

CHAPTER DESIGN

1. PURPOSE OF THE FRAMEWORK
2. COMPONENTS OF FINANCIAL STATEMENTS
3. OBJECTIVES AND USERS OF FINANCIAL STATEMENTS
4. ASSUMPTIONS UNDERLYING FINANCIAL STATEMENTS
5. QUALITATIVE CHARACTERISTICS OF FINANCIAL STATEMENTS
6. ELEMENTS OF FINANCIAL STATEMENTS
7. MEASUREMENTS OF ELEMENTS OF FINANCIAL STATEMENTS
8. CONCEPT OF CAPITAL AND CAPITAL MAINTENANCE

1. PURPOSE OF THE FRAMEWORK :

The framework sets out the concepts underlying the preparation and presentation of general-purpose financial statements prepared by enterprises for external users. The main purpose of the framework is to assist:

(a) Enterprises in preparation of their financial statements in compliance with Accounting Standards and in dealing with the topics not yet covered by any Accounting Standard,

(b) ASB in its task of development and review of Accounting Standards,

(c) ASB in promoting harmonisation of regulations, Accounting Standards and procedures relating to the preparation and presentation of financial statements by providing a basis for reducing the number of alternative accounting treatments permitted by Accounting Standards,

(d) Auditors in forming an opinion as to whether financial statements conform to the Accounting Standards,

(e) Users in interpretation of financial statements,

(f) Those who are interested in in the work of ASB with information about its information to the formulation of Accounting Standards.

2. COMPONENTS OF FINANCIAL STATEMENTS :

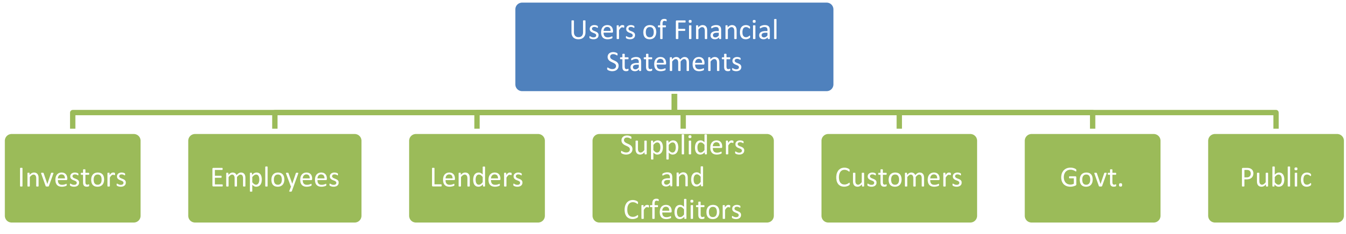
The major information contents of different components of financial statements are explained as below:

1. Balance sheet
2. Profit and Loss Account
3. Cash flow statement
4. Notes to Accounts

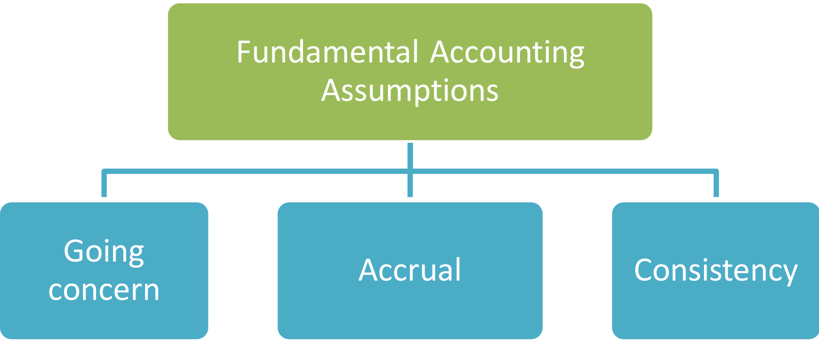
3. OBJECTIVES AND USERS OF FINANCIAL STATEMENTS :

The objective of financial statements is to provide information about the financial position, performance and cash flows of an enterprise that is useful to a wide range of users.

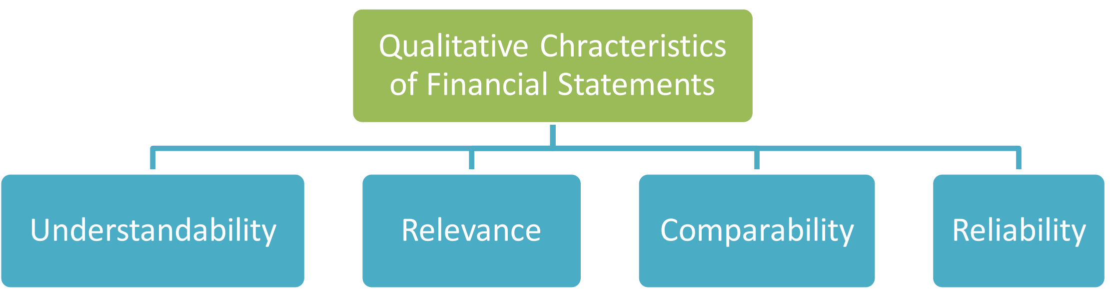
The framework identifies seven broad groups of users of financial statements.



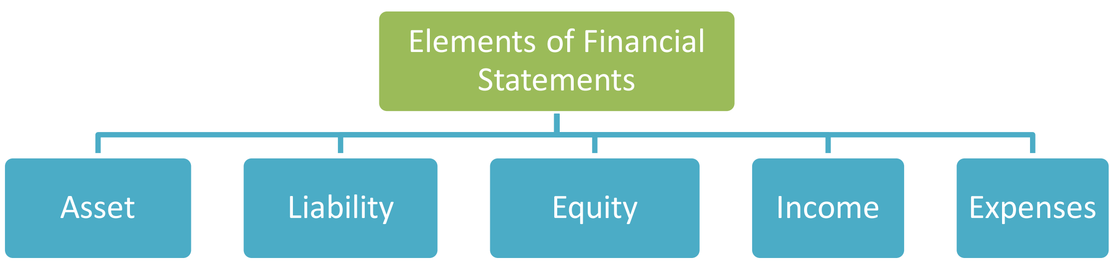
4. FUNDAMENTAL ACCOUNTING ASSUMPTIONS :



5. QUALITATIVE CHARACTERISTICS :



6. ELEMENTS OF FINANCIAL STATEMENTS :



1. **Assets:** An asset is a resource controlled by the enterprise as a result of past events from which future economic benefits are expected to flow to the enterprise.

2. **Liability:** A liability is a 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.

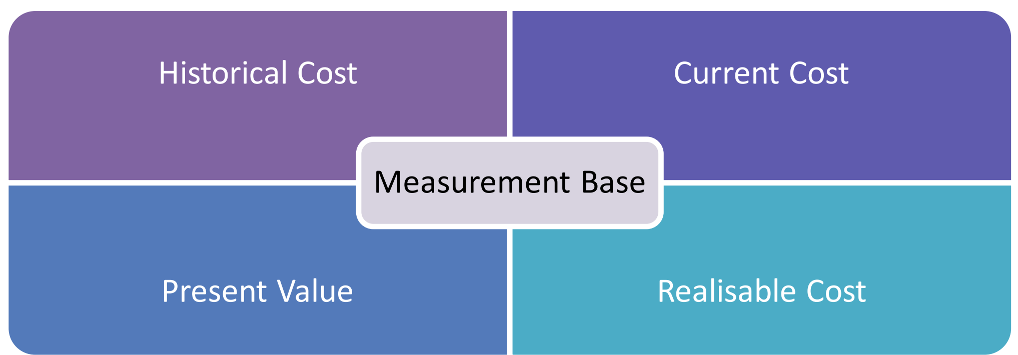
3. **Equity:** Equity is defined as residual interest in the assets of an enterprise after deducting all its liabilities.

Balance sheet of an enterprise can be written in form of: A – L = E.

4. **Income:** Income is 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.

5. **Expense:** An expense is decrease in economic benefits during the accounting period in the form of outflows or depletions of assets or incurrence of liabilities that result in decrease in equity other than those relating to distributions to equity participants.

7. MEASUREMENT OF ELEMENTS OF FINANCIAL STATEMENTS :



1. **Historical Cost:** Historical cost means acquisition price. For example, the businessman paid Rs.7,00,000 to purchase the machine, its acquisition price including installation charges is Rs. 8,00,000. The historical cost of machine would be Rs.8,00,000.
2. **Current Cost:** Current cost gives an alternative measurement basis. Assets are carried out at the amount of cash or cash equivalent that would have to be paid if the same or an equivalent asset was acquired currently. Liabilities are carried at the undiscounted amount of cash or cash equivalents that would be required to settle the obligation currently.
3. **Realisable (Settlement) Value:** For assets, this is the amount of cash or cash equivalents currently realisable on sale of the asset in an orderly disposal. For liabilities, this is the undiscounted amount of cash or cash equivalents expected to be paid on settlement of liability in the normal course of business.
4. **Present Value:** Assets are carried at the present value of the future net cash inflows that the item is expected to generate in the normal course of business. Liabilities are carried at the present value of the future net cash outflows that are expected to be required to settle the liabilities in the normal course of business.

8. CONCEPT OF CAPITAL AND CAPITAL MAINTENANCE :

Capital refers to net assets of a business. Since a business uses its assets for its operations, a fall in net assets will usually mean a fall in its activity level. It is therefore important for any business

to maintain its net assets in such a way, as to ensure continued operations at least at the same level year after year.

A business must ensure that Retained Profit (RP) is not negative, i.e. closing equity should not be less than capital to be maintained, which is sum of opening equity and capital introduced.

It should be clear from above that the value of retained profit depends on the valuation of assets and liabilities. In order to check maintenance of capital, i.e. whether or not retained profit is negative, we can use any of following three bases

1. **Financial capital maintenance at historical cost:** Under this convention, opening and closing assets are stated at respective historical costs to ascertain opening and closing equity. If retained profit is greater than or equals to zero, the capital is said to be maintained at historical costs. This means the business will have enough funds to replace its assets at historical costs. This is quite right as long as prices do not rise.
2. **Financial capital maintenance at current purchasing power:** Under this convention, opening and closing equity at historical costs are restated at closing prices using average price indices. (For example, suppose opening equity at historical cost is Rs.3,00,000 and opening price index is 100. The opening equity at closing prices is Rs. 3,60,000 if closing price index is 120). A positive retained profit by this method means the business has enough funds to replace its assets at average closing price.
3. **Physical capital maintenance at current costs:** Under this convention, the historical costs of opening and closing assets are restated at closing prices using specific price indices applicable to each asset. The liabilities are also restated at a value of economic resources to be sacrificed to settle the obligation at current date, i.e. closing date. The opening and closing equity at closing current costs are obtained as an excess of aggregate of current cost values of assets over aggregate of current cost values of liabilities. A positive retained profit by this method ensures retention of funds for replacement of each asset at respective closing prices.

Practical Questions :

Questions 1 :

Balance sheet of a trader on 31st March, 20X1 is given below:

Liabilities	Rs.	Assets	Rs.
Capital	60,000	Property, Plant and Equipment	65,000
Profit and Loss Account	25,000	Stock	30,000
10% Loan	35,000	Trade receivables	20,000

Trade payables	10,000	Deferred expenditure	10,000
		Bank	5,000
	1,30,000		**1,30,000**

Additional information:

(a) The remaining life of Property, Plant and Equipment is 5 years. The pattern of use of the asset is even. The net realisable value of Property, Plant and Equipment on 31.03.X2 was Rs. 60,000.

(b) The trader's purchases and sales in 20X1-X2 amounted to Rs. 4 lakh and Rs. 4.5 lakh respectively.

(c) The cost and net realisable value of stock on 31.03.X2 were Rs. 32,000 and Rs. 40,000 respectively.

(d) Expenses (including interest on 10% Loan of Rs. 3,500 for the year) amounted to Rs. 14,900.

(e) Deferred expenditure is amortised equally over 4 years.

(f) Trade receivables on 31.03.X2 is Rs. 25,000, of which Rs. 2,000 is doubtful. Collection of another Rs. 4,000 depends on successful re-installation of certain product supplied to the customer.

(g) Closing trade payable is Rs. 12,000, which is likely to be settled at 5% discount.

(h) Cash balance on 31.03.X2 is Rs. 37,100.

(i) There is an early repayment penalty for the loan Rs. 2,500.

You are required to prepare Profit and Loss Accounts and Balance Sheets of the trader in both cases (i) assuming going concern (ii) not assuming going concern.

Questions 2 :

A trader commenced business on 01/01/20X1 with Rs. 12,000 represented by 6,000 units of a certain product at Rs. 2 per unit. During the year 20X1 he sold these units at Rs. 3 per unit and had withdrawn Rs. 6,000. Let us assume that the price of the product at the end of year is Rs. 2.50 per unit. In other words, the specific price index applicable to the product is 125.

Current cost of opening stock = (Rs. 12,000 / 100) x 125 = 6,000 x Rs. 2.50 = Rs. 15,000

Current cost of closing cash = Rs. 12,000 (Rs. 18,000 – Rs. 6,000)

Opening equity at closing current costs = Rs. 15,000

Closing equity at closing current costs = Rs. 12,000

Retained Profit = Rs. 12,000 – Rs. 15,000 = (-) Rs. 3,000

The negative retained profit indicates that the trader has failed to maintain his capital. The available fund of Rs. 12,000 is not sufficient to buy 6,000 units again at increased price of Rs. 2.50 per unit. The drawings should have been restricted to Rs. 3,000 (Rs. 6,000 – Rs.

3,000). Had the trader withdrawn Rs. 3,000 instead of Rs. 6,000, he would have left with Rs.15,000, the fund required to buy 6,000 units at Rs. 2.50 per unit.

You are required to compute the Capital maintenance under all three bases ie. (i) Historical costs, (ii) Current purchasing power and (iii) Physical capital maintenance.

MCQs :

1. The 'going concern' concept assumes that
   (a) The business can continue in operational existence for the foreseeable future.
   (b) The business cannot continue in operational existence for the foreseeable future.
   (c) The business is continuing to be profitable.
   (d) The business cannot continue if it is not able to earn profits.
2. Two principal qualitative characteristics of financial statements are
   (a) Understandability and materiality
   (b) Relevance and reliability
   (c) Relevance and materiality
   (d) Comparability and materiality.
3. All of the following are components of financial statements except
   (a) Balance sheet
   (b) Statement of Profit and loss
   (c) Human responsibility report
   (d) Social responsibility report.
4. An accounting policy can be changed if the change is required
   (a) By statute or accounting standard
   (b) For more appropriate presentation of financial statements
   (c) Both (a) and (b)
   (d) By statute as well as accounting standards.
5. Value of equity may change due to
   (a) Contribution from or Distribution to equity participants
   (b) Income earned
   (c) expenses incurred
   (d) All the three.

Thanks ....

Rahul Malkan

Chapter 3

APPLICABILITY OF ACCOUNTING STANDARDS

CHAPTER DESIGN

1. INTRODUCTION
2. STATUS OF ACCOUNTING STANDARDS
3. APPLICABILITY OF ACCOUNTING STANDARDS

1. INTRODUCTION :

Status of AS → Applicability of AS for Corporate Entities → Applicability of AS for Non-Corporate Entities

2. STATUS OF ACCOUNTING STANDARDS :

It has already been mentioned in chapter 1 that the standards are developed by the Accounting Standards Board (ASB) of the Institute of Chartered Accountants of India and are issued under the authority of its Council which are approved by the MCA (Ministry of Corporate Affairs) for Corporate entities. The standards cannot override laws and local regulations. The Accounting Standards are nevertheless made mandatory from the dates notified by the MCA and are generally applicable to all enterprises, subject to certain exceptions as stated below. The implication of mandatory status of an Accounting Standard depends on whether the statute governing the enterprise concerned requires compliance with the Standard, e.g., the Ministry of Corporate Affairs have notified Accounting Standards for companies incorporated under the Companies Act, 1956 (or the Companies Act, 2013). In assessing whether an accounting standard is applicable, one must find correct answer to the following three questions. (a) Does it apply to the enterprise concerned? If yes, the next question is: (b) Does it apply to the financial statement concerned? If yes, the next question is: (c) Does it apply to the financial item concerned? The preface to the statements of accounting standards answers the above questions.

3. APPLICABILITY OF ACCOUNTING STANDARDS :

Criteria for classification of Non-company entities for applicability of Accounting Standards

The Council of the ICAI, at its 400th meeting, held on March 18-19, 2021, considered the matter relating to applicability of Accounting Standards issued by the ICAI, to Non-company entities (Enterprises). The scheme for applicability of Accounting Standards to Non-company entities shall come into effect in respect of accounting periods commencing on or after 1 April 2020.

1. For the purpose of applicability of Accounting Standards, Non-company entities are classified into four categories, viz., Level I, Level II, Level III and Level IV.

Level I entities are large size entities, Level II entities are medium size entities, Level III entities are small size entities and Level IV entities are micro entities. Level IV, Level III and Level II entities are referred to as Micro, Small and Medium size entities (MSMEs). The criteria for classification of Non-company entities into different levels are given in Annexure 1.

The terms 'Small and Medium Enterprise' and 'SME' used in Accounting Standards shall be read as 'Micro, Small and Medium size entity' and 'MSME' respectively.

2. Level I entities are required to comply in full with all the Accounting Standards.
3. Certain exemptions/relaxations have been provided to Level II, Level III and Level IV Non-company entities. Applicability of Accounting Standards and exemptions/relaxations to such entities are given in Annexure 2.
4. This Announcement supersedes the earlier Announcement of the ICAI on '**Harmonisation of various differences between the Accounting Standards issued by the ICAI and the Accounting Standards notified by the Central Government'** issued in February 2008, to the extent it prescribes the criteria for classification of Non-company entities (Non-corporate entities) and applicability of Accounting Standards to non-company entities, and the Announcement '**Revision in the criteria for classifying Level II non-corporate entities**' issued in January 2013.
5. This Announcement is not relevant for Non-company entities who may be required to follow Ind AS as per relevant regulatory requirements applicable to such entities. recurrence

Annexure 1

Criteria for classification of Non-company Entities as decided by the Institute of Chartered Accountants of India

Level I Entities

Non-company entities which fall in any one or more of the following categories, at the end of the relevant accounting period, are classified as Level I entities:

(i) Entities whose securities are listed or are in the process of listing on any stock exchange, whether in India or outside India.

(ii) Banks (including co-operative banks), financial institutions or entities carrying on insurance business.

(iii) All entities engaged in commercial, industrial or business activities, whose turnover (excluding other income) exceeds rupees two-fifty crore in the immediately preceding accounting year.

(iv) All entities engaged in commercial, industrial or business activities having borrowings (including public deposits) in excess of rupees fifty crore at any time during the immediately preceding accounting year.

(v) Holding and subsidiary entities of any one of the above.

Level II Entities

Non-company entities which are not Level I entities but fall in any one or more of the following categories are classified as Level II entities:

(i) All entities engaged in commercial, industrial or business activities, whose turnover (excluding other income) exceeds rupees fifty crore but does not exceed rupees two-fifty crore in the immediately preceding accounting year.

(ii) All entities engaged in commercial, industrial or business activities having borrowings (including public deposits) in excess of rupees ten crore but not in excess of rupees fifty crore at any time during the immediately preceding accounting year.

(iii) Holding and subsidiary entities of any one of the above.

Level III Entities

Non-company entities which are not covered under Level I and Level II but fall in any one or more of the following categories are classified as Level III entities:

(i) All entities engaged in commercial, industrial or business activities, whose turnover (excluding other income) exceeds rupees ten crore but does not exceed rupees fifty crore in the immediately preceding accounting year.

(ii) All entities engaged in commercial, industrial or business activities having borrowings (including public deposits) in excess of rupees two crore but does not exceed rupees ten crore at any time during the immediately preceding accounting year.

(iii) Holding and subsidiary entities of any one of the above.

Level IV Entities

Non-company entities which are not covered under Level I, Level II and Level III are considered as Level IV entities.

Additional requirements

(1) An MSME which avails the exemptions or relaxations given to it shall disclose (by way of a note to its financial statements) the fact that it is an MSME, the Level of MSME and that it has complied with the Accounting Standards insofar as they are applicable to entities falling in Level II or Level III or Level IV, as the case may be.

(2) Where an entity, being covered in Level II or Level III or Level IV, had qualified for any exemption or relaxation previously but no longer qualifies for the relevant exemption or relaxation in the current accounting period, the relevant standards or requirements become applicable from the current period and the figures for the corresponding period of the previous accounting period need not be revised merely by reason of its having

ceased to be covered in Level II or Level III or Level IV, as the case may be. The fact that the entity was covered in Level II or Level III or Level IV, as the case may be, in the previous period and it had availed of the exemptions or relaxations available to that Level of entities shall be disclosed in the notes to the financial statements. The fact that previous period figures have not been revised shall also be disclosed in the notes to the financial statements.

(3) Where an entity has been covered in Level I and subsequently, ceases to be so covered and gets covered in Level II or Level III or Level IV, the entity will not qualify for exemption/relaxation available to that Level, until the entity ceases to be covered in Level I for two consecutive years. Similar is the case in respect of an entity, which has been covered in Level II or Level III and subsequently, gets covered under Level III or Level IV.

(4) If an entity covered in Level II or Level III or Level IV opts not to avail of the exemptions or relaxations available to that Level of entities in respect of any but not all of the Accounting Standards, it shall disclose the Standard(s) in respect of which it has availed the exemption or relaxation.

(5) If an entity covered in Level II or Level III or Level IV opts not to avail any one or more of the exemptions or relaxations available to that Level of entities, it shall comply with the relevant requirements of the Accounting Standard.

(6) An entity covered in Level II or Level III or Level IV may opt for availing certain exemptions or relaxations from compliance with the requirements prescribed in an Accounting Standard:

Provided that such a partial exemption or relaxation and disclosure shall not be permitted to mislead any person or public.

(7) In respect of Accounting Standard (AS) 15, *Employee Benefits*, exemptions/ relaxations are available to Level II and Level III entities, under two sub-classifications, viz., (i) entities whose average number of persons employed during the year is 50 or more, and (ii) entities whose average number of persons employed during the year is less than 50. The requirements stated in paragraphs (1) to (6) above, mutatis mutandis, apply to these sub-classifications.

Annexure 2

Applicability of Accounting Standards to Non-company Entities

The Accounting Standards issued by the ICAI, as on April 1, 2020, and such standards as issued from time-to-time are applicable to Non-company entities subject to the relaxations and exemptions in the announcement. The Accounting Standards issued by ICAI as on April 1, 2020, are:

AS 1	Disclosure of Accounting Policies
AS 2	Valuation of Inventories

AS 3	Cash Flow Statements
AS 4	Contingencies and Events Occurring After the Balance Sheet Date
AS 5	Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies
AS 7	Construction Contracts
AS 9	Revenue Recognition
AS 10	Property, Plant and Equipment
AS 11	The Effects of Changes in Foreign Exchange Rates
AS 12	Accounting for Government Grants
AS 13	Accounting for Investments
AS 14	Accounting for Amalgamations
AS 15	Employee Benefits
AS 16	Borrowing Costs
AS 17	Segment Reporting
AS 18	Related Party Disclosures
AS 19	Leases
AS 20	Earnings Per Share
AS 21	Consolidated Financial Statements
AS 22	Accounting for Taxes on Income
AS 23	Accounting for Investments in Associates in Consolidated Financial Statements
AS 24	Discontinuing Operations
AS 25	Interim Financial Reporting
AS 26	Intangible Assets
AS 27	Financial Reporting of Interests in Joint Ventures
AS 28	Impairment of Assets
AS 29	Provisions, Contingent Liabilities and Contingent Assets

(1) Applicability of the Accounting Standards to Level 1 Non- company entities.

Level I entities are required to comply in full with all the Accounting Standards.

(2) Applicability of the Accounting Standards and exemptions/relaxations for Level II, Level III and Level IV Non-company entities

Accounting Standards applicable to Non-company entities

AS	Level II Entities	Level III Entities	Level IV Entities
AS 1	Applicable	Applicable	Applicable
AS 2	Applicable	Applicable	Applicable
AS 3	Not Applicable	Not Applicable	Not Applicable

AS 4	Applicable	Applicable	Applicable
AS 5	Applicable	Applicable	Applicable
AS 7	Applicable	Applicable	Applicable
AS 9	Applicable	Applicable	Applicable
AS 10	Applicable	Applicable with disclosures exemption	Applicable with disclosures exemption
AS 11	Applicable	Applicable with disclosures exemption	Applicable with disclosures exemption
AS 12	Applicable	Applicable	Applicable
AS 13	Applicable	Applicable	Applicable with disclosures exemption
AS 14	Applicable	Applicable	Not Applicable (Refer note 2(C))
AS 15	Applicable with exemptions	Applicable with exemptions	Applicable with exemptions
AS 16	Applicable	Applicable	Applicable
AS 17	Not Applicable	Not Applicable	Not Applicable
AS 18	Applicable	Not Applicable	Not Applicable
AS 19	Applicable with disclosures exemption	Applicable with disclosures exemption	Applicable with disclosures exemption
AS 20	Not Applicable	Not Applicable	Not Applicable
AS 21	Not Applicable (Refer note 2(D))	Not Applicable (Refer note 2(D))	Not Applicable (Refer note 2(D))
AS 22	Applicable	Applicable	Applicable only for current tax related provisions (Refer note 2(B)(vi))
AS 23	Not Applicable (Refer note 2(D))	Not Applicable (Refer note 2(D))	Not Applicable (Refer note 2(D))
AS 24	Applicable	Not Applicable	Not Applicable
AS 25	Not Applicable (Refer note 2(D))	Not Applicable (Refer note 2(D))	Not Applicable (Refer note 2(D))
AS 26	Applicable	Applicable	Applicable with disclosures exemption
AS 27	Not Applicable (Refer notes and 2(D))	Not Applicable (Refer notes 2(C) and 2(D))	Not Applicable (Refer notes 2(C) and 2(D))
AS 28	Applicable disclosures exemption	Applicable with disclosures exemption	Not Applicable

AS 29	Applicable disclosures exemption	Applicable with disclosures exemption	Applicable with disclosures exemption

MCQs :

1. Non-corporate entities which are not Level I entities whose turnover (excluding other income) exceeds rupees ___________ but does not exceed rupees two-fifty crores in the immediately preceding accounting year are classified as Level II entities.
   (a) five crores. (b) two crores.
   (c) fifty crores. (d) ten crores.
2. The following Accounting Standard is not applicable to Non-corporate Entities falling in Level II in its entirety
   (a) AS 10. (b) AS 17.
   (c) AS 2. (d) AS 13.
3. All non-corporate entities engaged in commercial, industrial and business reporting entities, whose turnover (excluding other income) exceeds rupees 250 crores in the immediately preceding accounting year, are classified as
   (a) Level II entities. (b) Level I entities.
   (c) Level III entities. (d) Level IV entities.
4. All non-corporate entities engaged in commercial, industrial or business activities having borrowings (including public deposits) in excess of rupees two crores but does not exceed rupees ten crores at any time during the immediately preceding accounting year.
   (a) Level II entities. (b) Level IV entities.
   (c) Level III entities. (d) Level I entities.
5. "Small and Medium Sized Company" (SMC) means, a company-
   (a) which may be a bank, financial institution or an insurance company.
   (b) whose turnover (excluding other income) does not exceed rupees two-fifty crores in the immediately preceding accounting year;
   (c) whose turnover (excluding other income) does not exceed rupees fifty crores in the immediately preceding accounting year;
   (d) whose turnover (excluding other income) does not exceed rupees five hundred crores in the immediately preceding accounting year.

Thanks ....

Rahul Malkan

Chapter 4

AS 1 – DISCLOSURE OF ACCOUNTING POLICIES

CHAPTER DESIGN

1. ACCOUNTING POLICIES
2. OBJECTIVE OF AS 1
3. FUNDAMENTAL ACCOUNTING ASSUMPTIONS
4. AREAS IN WHICH DIFFERENT ACCOUNTING POLICIES ARE ENCOUNTERED
5. SELECTION OF ACCOUNTING POLICIES
6. MANNER OF DISCLOSURE
7. CHANGES IN ACCOUNTING POLICIES

1. ACCOUNTING POLICIES :

The accounting policies refer to the specific accounting principles and the methods of applying those principles adopted by the enterprise in the preparation and presentation of financial statements.

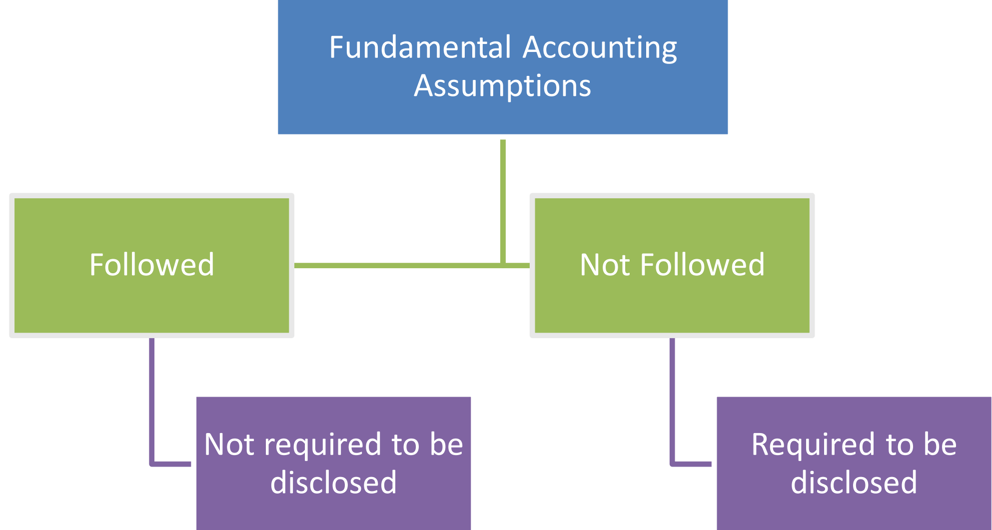
2. OBJECTIVE OF AS 1 :

- Accounting standard cannot and do not cover all possible areas of accounting and enterprise have reasonable degree of freedom in adopting accounting policies in areas not covered by standard.
- Also, since entities operate in diverse situations, it is impossible to develop a single set of policies applicable to all enterprises for all time.
- Accounting standard therefore permits more than one policy even in the areas covered by it. Such difference in accounting policies lead to difference in reported information even if underlying transactions are same.
- Due to the above reasons AS 1, requires enterprise to disclose significant accounting policies actually adopted by them in preparation of financial statements.

3. FUNDAMENTAL ACCOUNTING ASSUMPTIONS :

Going concern → Consistency → Accrual

1. **Going concern :**
   It is assumed that the enterprise will continue its operations for the foreseeable future. The enterprise has neither the necessity nor the intention of liquidation or of curtailing materially the scale of operations.
2. **Consistency :**
   It is assumed that accounting policies are consistent from one period to another.
3. **Accrual :**
   Revenues and costs are accrued, i.e. , recognized as they are earned or incurred (and not as money is received or paid) and recorded in the financial statements of the periods to which they relate.

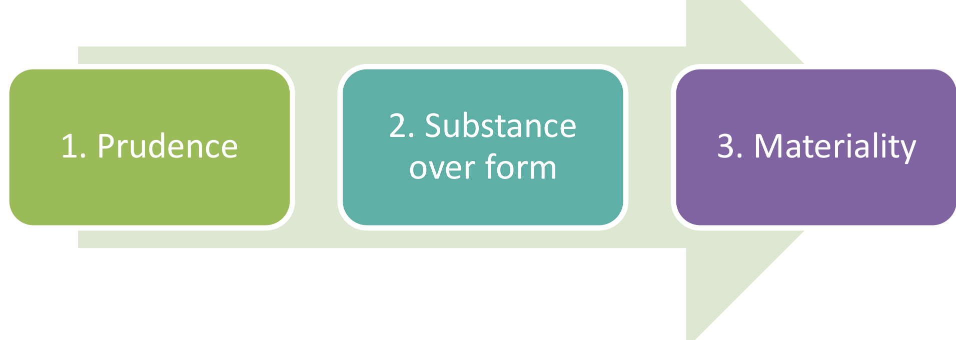


4. AREAS IN WHICH DIFFERENT ACCOUNTING POLICIES ARE ENCOUNTERED :

- Method of depreciation
- Valuation of inventories
- Treatment of goodwill
- Valuation of investments
- Treatment of retirement benefits
- Valuation of Fixed Assets
- Treatment of contingent liabilities

5. SELECTION OF ACCOUNTING POLICIES :

Financial statements are prepared to present true and fair view of performance and position of the entity. In selecting a policy, alternative accounting policies should be evaluated keeping the above objective in mind. Major consideration governing the selection of accounting policies are



1. **Prudence (Conservatism) :**

   Profits are not anticipated, but losses are provided for. Exercise of prudence will help in ensuring that

   1. Profits are not overstated
   2. Losses are not understated

3. Assets are not overstated
4. Liabilities are not understated

Example :

1. A trader is holding 100 units of its product in closing stock. Cost is 10,000 and NRV is 15,000
2. A trader is holding 100 units of its product in closing stock. Cost is 15,000 and NRV is 10,000

2. Substance over form :

Transactions and Events should be governed by their substance (actual facts) and not merely by legal form.

Example : When an asset is leased, in case of finance lease, the lessee charges the depreciation in the asset and not the lessor, the owner of the asset.

3. Materiality :

Financial statements should disclose all 'material items' i.e the items the knowledge of which might influence the users of financial statements.

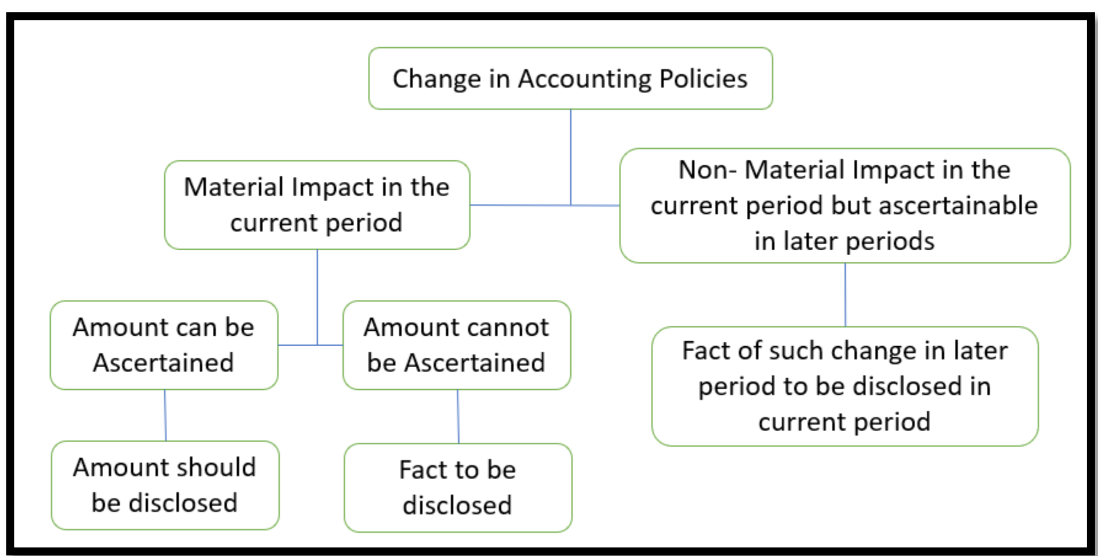
6. MANNER OF DICLOSURE :

All significant Accounting policies adopted in the preparation and presentation of financial statements should be disclosed.

The disclosure of the significant accounting policies as such should form the part of financial statements and significant accounting policies should normally be disclosed in one place.

Note : Being a part of the financial statements, the opinion of auditors should cover the disclosures of accounting policies.

7. CHANGES IN ACCOUNTING POLICIES :



PRACTICAL QUESTIONS :

Question 1 : M/s Prashant Ltd.

In the books of M/s Prashant Ltd., closing inventory as on 31.03.2015 amounts to Rs 1,63,000 (on the basis of FIFO method).

The company decides to change from FIFO method to weighted average method for ascertaining the cost of inventory from the year 2014-15.

On the basis of weighted average method, closing inventory as on 31.03.2015 amounts to Rs 1,47,000. Realisable value of the inventory as on 31.03.2015 amounts to Rs 1,95,000. Discuss disclosure requirement of change in accounting policy as per AS-1.

Question 2 : ABC Ltd.

ABC Ltd. was making provision for non-moving inventories based on issues for the last 12 months up to 31.3.2016.

The company wants to provide during the year ending 31.3.2017 based on technical evaluation:

Total value of inventory	Rs 100 lakhs
Provision required based on 12 months issue	Rs 3.5 lakhs
Provision required based on technical evaluation	Rs 2.5 lakhs

Does this amount to change in Accounting Policy?

Can the company change the method of provision?

Question 3 : Jagannath Ltd.

Jagannath Ltd. had made a rights issue of shares in 2004. In the offer document to its members, it had projected a surplus of Rs. 40 crores during the accounting year to end on 31st March, 2015. The draft results for the year, prepared on the hitherto followed accounting policies and presented for perusal of the board of directors showed a deficit of Rs. 10 crores. The board in consultation with the managing director, decided on the following:

i. Value year-end inventory at works cost (Rs. 50 crores) instead of the hitherto method of valuation of inventory at prime cost (Rs. 30 crores).

ii. Provide depreciation for the year on straight line basis on account of substantial additions in gross block during the year, instead of on the reducing balance method, which was hitherto adopted. As a consequence, the charge for depreciation at Rs. 27 crores is lower than the amount of Rs. 45 crores which would have been provide had the old method been followed, by Rs. 18 cores.

iii. Not to provide for “after sales expenses” during the warranty period. Till the last year, provision at 2% of sales used to be made under the concept of “matching of

costs against revenue" and actual expenses used to be charged against the provision. The board now decided to account for expenses as and when actually incurred. Sales during the year total to Rs. 600 crores.

iv. Provide for permanent fall in the value of investments – which fall had taken place over the past five years – the provision being Rs. 10 crores.

As chief accountant of the company, you are asked by the managing director to draft the notes on accounts for inclusion in the annual report for 2014-2015.

MCQs :

1. Which of the following is NOT a major consideration in selection and application of accounting policies?
   (a) Prudence (b) Comparability
   (c) Materiality (d) Substance over form

2. Adoption of different accounting policies by different companies operating in the same industry affects which of the qualitative characteristics the most?
   (a) Comparability (b) Relevance
   (c) Faithful representation (d) Reliability

3. Which of the following statement would not be correct in relation to disclosures to be made in the financial statements after making any change in an accounting policy?
   (a) Any change in an accounting policy which has a material effect should be disclosed.
   (b) The amount by which any item in the financial statements is affected by such change should be disclosed to the extent ascertainable. Where such amount is not ascertainable, wholly or in part, the fact should be indicated.
   (c) If a change is made in the accounting policies which has no material effect on the financial statements for the current period but which is reasonably expected to have a material effect in later periods, the fact of such change should be appropriately disclosed in the period in which the change is adopted.
   (d) If a change is made in an accounting policy which has material effect on the financial statements for the current period and is reasonably expected to have a material effect in later periods, the fact of such change should be appropriately disclosed only in the later periods i.e. year(s) next to the year in which the change is adopted.

Thanks ....

Chapter 5

AS 2 – VALUATION OF INVENTORY

CHAPTER DESIGN

1. OBJECTIVE
2. SCOPE
3. DEFINITIONS
4. MEASUREMENT OF INVENTORIES
5. COST OF INVENTORY
6. NET REALIZABLE VALUE
7. INVENTORY VALUATION TECHNIQUES
8. RECOGNITION AS EXPENSES
9 DISCLOSURE

1. OBJECTIVE :

The objective of this standard is to

- Prescribe accounting treatment for inventory
- Guidance on measurement of its cost
- Recognition as an expense
- Methods of cost determination (FIFO, Wt average ....)

2. SCOPE :

AS - 2 does not apply to:

a) WIP of Construction Contracts, (AS - 7)

b) WIP of Service Providers,

c) Shares, Debentures, other financial instruments etc. held as stock in trade.

d) Producers' inventories of livestock, agricultural and forest products, and mineral oils, ores and gases to the extent that they are measured at net realizable value in accordance with well - established practices in those industries.

3. DEFINITIONS :

1. Inventory: Inventory are assets :

a. held for sale in ordinary course of business (FG)

b. in process of production for sale (WIP)

c. in form of material or supplies to be consumed in production process or in rendering the services (RM)

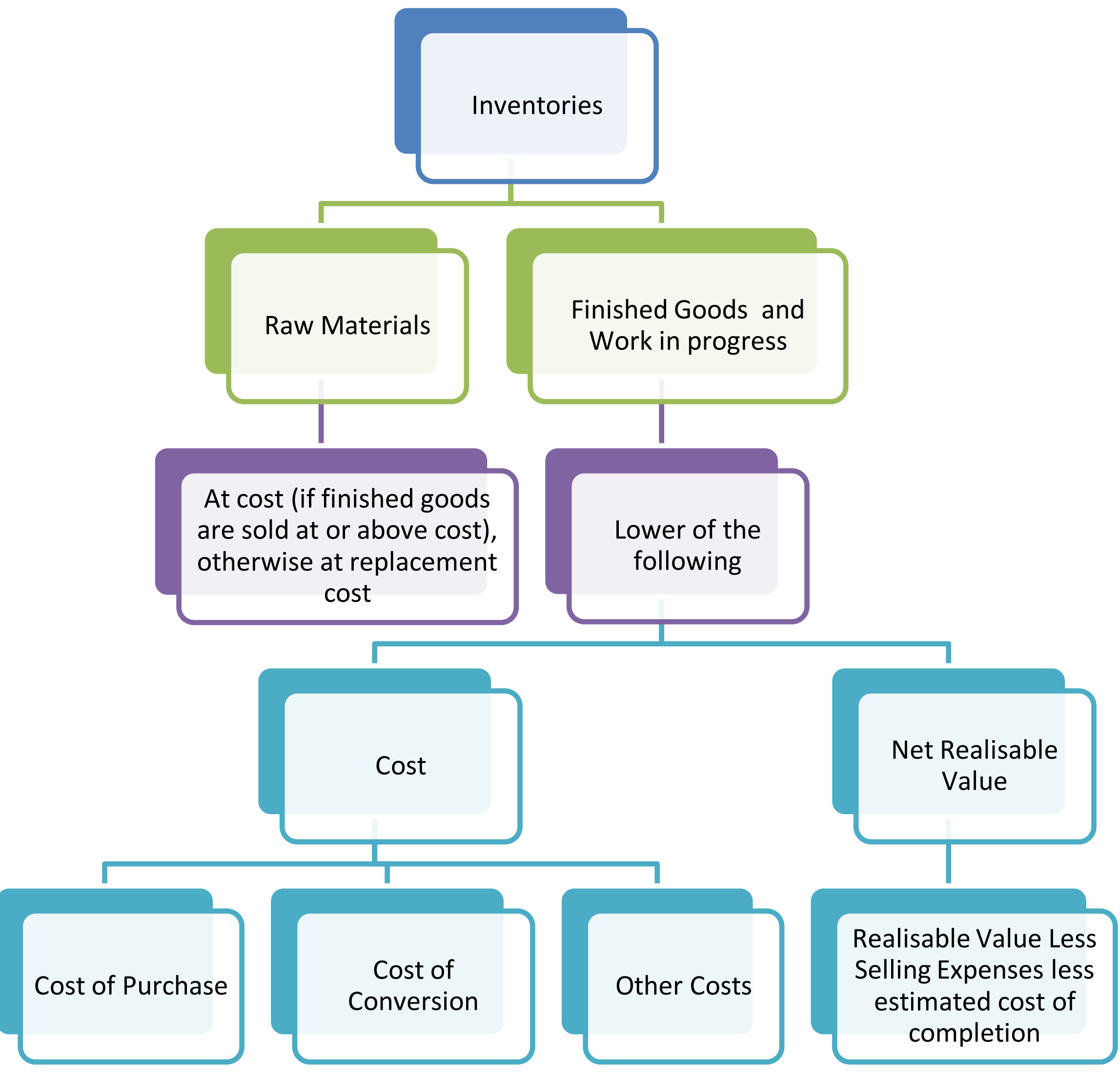
2. Net Realizable Value :

Net Realizable Value = Estimated Selling Price in the ordinary course of business
(-) Estimated Cost of Completion
(-) Estimated costs necessary to make the sale.

4. MEASUREMENT :

As per IND AS 2 Inventory should be measured at

"Cost or Net realizable Value whichever is less"



Question 1 :

Cost of a partly finished unit at the end of 2016-17 is Rs 150. The unit can be finished next year by a further expenditure of Rs 100. The finished unit can be sold at Rs 250, subject to payment of 4% brokerage on selling price. Determine the value of inventory.

5. COST OF INVENTORY :

Cost of inventory includes

1. Cost of purchase
2. Cost of conversion

3. other cost incurred in bringing the inventory to its present condition and location.

1. Cost of Purchase includes :

a. Purchase price
b. Import duty and taxes (non-refundable)
c. Transport handling charges
d. Other direct cost
e. trade discounts and rebates (Subtracted)

2. Cost of conversion :

a. Direct Material
b. Direct Labor
c. Direct Overheads
d. Fixed Overheads
e. Variable overheads

Note : Fixed overheads should be absorbed at Normal (budgeted cost) or Actual production Cost whichever is lower. That is any inefficiency should be transferred to P & L A/c

3. Other costs :

Other cost to be included in the valuation of inventory should be only to the extent of those costs that are incurred in bringing the inventory to its present location and condition.

Exclusions

1. Abnormal Wastages
2. Storage cost (Costs after inventory is ready)
3. Administration cost
4. Selling cost.

Question 2 : Pluto Ltd.

Pluto Ltd. has a plant with the normal capacity to produce 5,00,000 unit of a product per annum and the expected fixed overhead is Rs.15,00,000. Fixed overhead on the basis of normal capacity is Rs.3 per unit (15,00,000/5,00,000). How shall u treat Fixed overheads under following circumstances a. Actual production is 5,00,000 units b. Actual production is 3,75,000 units c. Actual production is 7,50,000 units.

Question 3 : Venus Trading Company

Venus Trading Company purchases cars from several countries and sells them to Asian countries. During the current year, this company has incurred following expenses:

1. Trade discounts on purchase
2. Handling costs relating to imports

3. Salaries of accounting department
4. Sales commission paid to sales agents
5. After sales warranty costs
6. Import duties
7. Costs of purchases (based on supplier's invoices)
8. Freight expense
9. Insurance of purchases
10. Brokerage commission paid to indenting agents

Evaluate which costs are allowed by Ind AS 2 for inclusion in the cost of inventory in the books of Venus.

Joint product and By – product

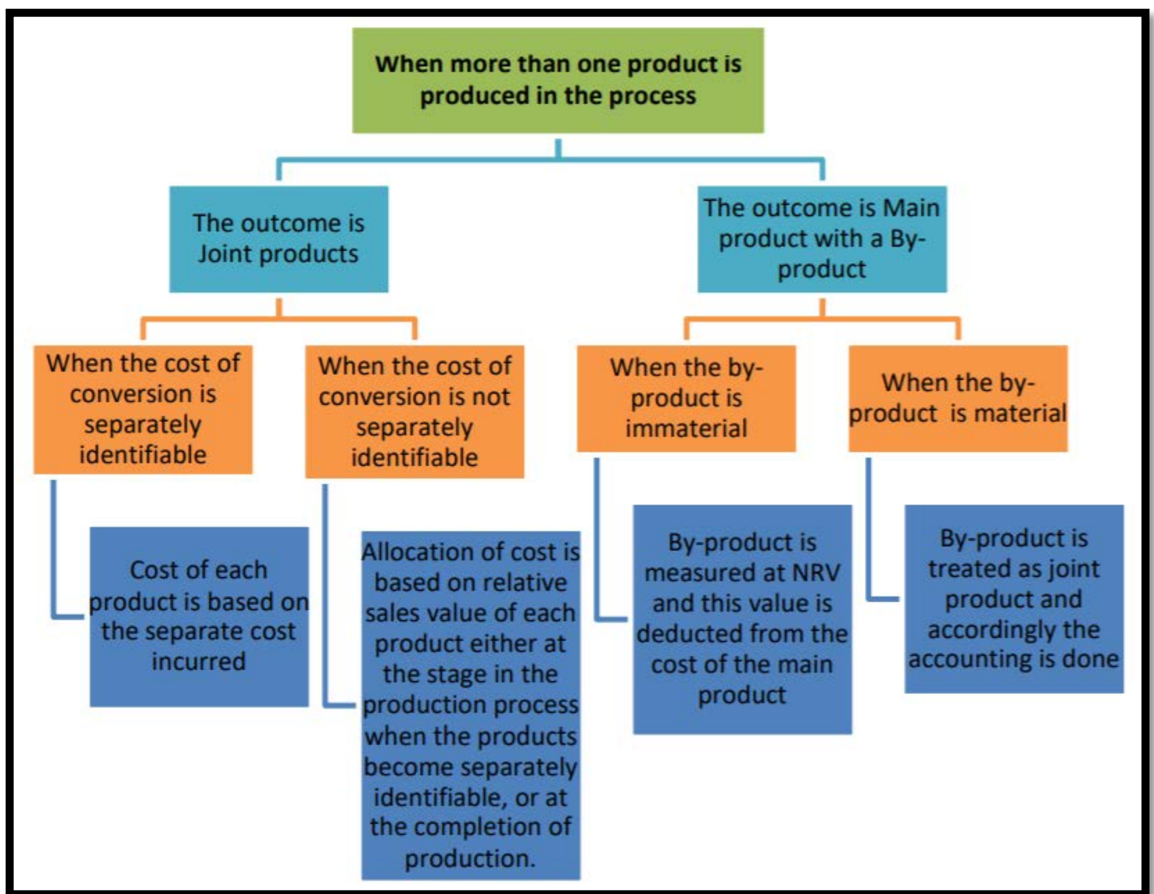
A production process may result into more than one product produced simultaneously. There may be a case where joint product or main product and by product may be produced together.

Valuation process

Scrap = valued at scrap

By product = Valued at NRV (Profit element should be ignored)

Joint product = the remaining cost should be allocated on rational and consistent basis.



Question 4 : Mars Ltd.

In a manufacturing process of Mars Ltd., one by-product BP emerges besides two main products MP1 and MP2 apart from scrap. Details of cost of production process are here under:

Item	Unit	Amount	Output	Closing Stock 31/3/2011
Raw Material	14,500	1,50,000	MP – I 5,000 units	250
Wages		90,000	MP – II 4,000 units	100
Fixed Overhead		65,000	BP – 2,000 units	
Variable Overhead		50,000		

Average market price of MP1 and MP2 is Rs.60 per unit and Rs.50 per unit respectively, by product is sold @ Rs.20 per unit. There is a profit of Rs.5,000 on sale of by-product after incurring separate processing charges of Rs.8,000 and packing charges of Rs.2,000, Rs.5,000 was realised from sale of scrap.

Required: Calculate the value of closing stock of MP1 and MP2 as on 31-03-2011

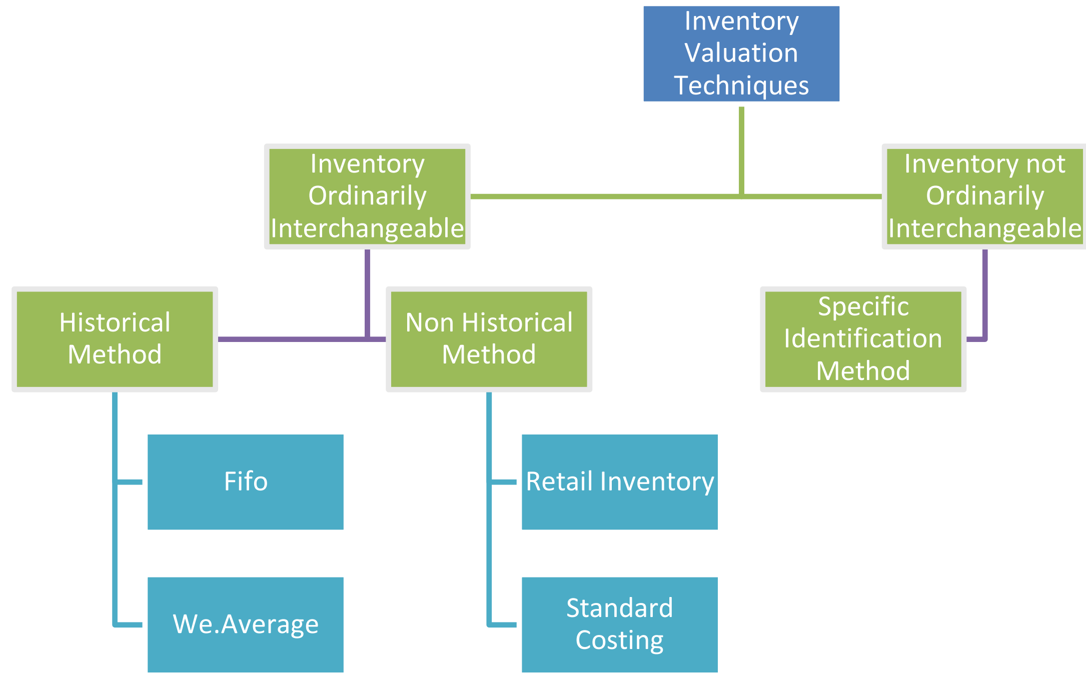
6. NET REALIZABLE VALUE :

Net Realizable Value = Estimated Selling Price in the ordinary course of business

(-) Estimated Cost of Completion

(-) Estimated costs necessary to make the sale.

7. INVENTORY VALUATION TECHNIQUES :



Question 5 : The trader

The trader purchased certain articles for Rs.85,000. He sold certain articles for Rs.1,05,000. The average percentage of gross margin is 25% on cost. Opening stock of inventory at cost was Rs.15,000. Calculate closing stock.

Question 6 : Mars Fashions

Mars Fashions is a new luxury retail company located in Lajpat Nagar, New Delhi. Kindly advise the accountant of the company on the necessary accounting treatment for the following items:

(a) One of Company's product lines is beauty products, particularly cosmetics such as lipsticks, moisturizers and compact make-up kits. The company sells hundreds of different brands of these products. Each product is quite similar, is purchased at similar prices and has a short lifecycle before a new similar product is introduced. The point of sale and inventory system is not yet fully functioning in this department. The sales manager of the cosmetic department is unsure of the cost of each product but is confident of the selling price and has reliably informed you that the Company, on average, make a gross margin of 65% on each line.

(b) Mars Fashions also sells handbags. The Company manufactures their own handbags as they wish to be assured of the quality and craftsmanship which goes into each handbag. The handbags are manufactured in India in the head office factory which has made handbags for the last fifty years. Normally, Mars manufactures 100,000 handbags a year in their handbag division which uses 15% of the space and overheads of the head office factory. The division employs ten people and is seen as being an efficient division within the overall company. In accordance with Ind AS 2, explain how the items referred to in a) and b) should be measured.

Question 7 : Mercury Ltd.

Mercury Ltd. uses a periodic inventory system. The following information relates to 2011 – 2012

Date	Particulars	Unit	CPU	Total Cost
April	Inventory	200	10	2000
May	Purchase	50	11	550
Sept	Purchase	400	12	4800
Feb	Purchase	350	14	4900
	Total	**1000**		**12,250**

Physical inventory at 31.03.2012 400 units. Calculate ending inventory value and cost of sales using: (a) FIFO (b) Weighted Average.

Question 8 : Sun Pharma Limited

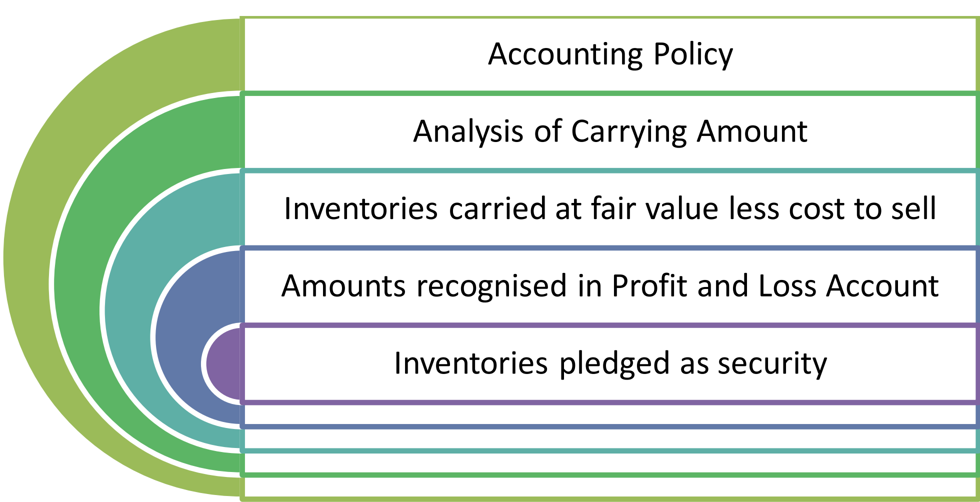
Sun Pharma Limited, a renowned company in the field of pharmaceuticals has the following four items in inventory: The Cost and Net realizable value is given as follows:

Item	Cost	Net Realizable Value
A	2000	1900
B	5000	5100
C	4400	4550
D	3200	2990

8. RECOGNITION AS EXPENSE :

1) The amount of inventories recognised as an expense in the period will generally be:
   a) carrying amount of the inventories sold in the period in which related revenue is recognised; and
   b) the amount of any write-down of inventories to net realisable value and all losses of inventories shall be recognised as an expense in the period the write-down or loss occurs; reduced by the amount of any reversal in the period of any write-down of inventories, arising from an increase in net realisable value shall be recognized as a reduction in the amount of inventories recognised as an expense in the period in which the reversal occurs.
2) Some inventories may be allocated to other asset accounts, for example, inventory used as a component of self-constructed property, plant or equipment. Inventories allocated to another asset in this way are recognised as an expense during the useful life of that asset through charging of depreciation on that asset.

9. DISCLOSURE :



PRACTICAL QUESTIONS :

Question 9 :

The company deals in three products, A, B and C, which are neither similar nor interchangeable. At the time of closing of its account for the year 2016-17, the Historical Cost and Net Realisable Value of the items of closing stock are determined as follows:

Items	Historical Cost	Net Realisable Value
A	40	28
B	32	32
C	16	24

What will be value of Closing stock?

Question 10 : X Co. Limited

X Co. Limited purchased goods at the cost of Rs.40 lakhs in October, 2016. Till March, 2017, 75% of the stocks were sold. The company wants to disclose closing stock at Rs.10 lakhs. The expected sale value is Rs.11 lakhs and a commission at 10% on sale is payable to the agent. Advise, what is the correct closing stock to be disclosed as at 31.3.2017.

Question 11 :

In a production process, normal waste is 5% of input. 5,000 MT of input were put in process resulting in wastage of 300 MT. Cost per MT of input is Rs.1,000. The entire quantity of waste is on stock at the year end. State with reference to Accounting Standard, how will you value the inventories in this case?

Question 12 :

You are required to value the inventory per kg of finished goods consisting of:

	Rs per kg.
Material cost	200
Direct labour	40
Direct variable overhead	20

Fixed production charges for the year on normal working capacity of 2 lakh kgs is Rs 20 lakhs. 4,000 kgs of finished goods are in stock at the year end.

MCQs :

1. Which item of inventory is under the scope of AS 2 (Revised)?
   - (a) WIP arising under construction contracts
   - (b) Raw materials
   - (c) Shares

(d) Debentures held as stock in trade.

2. Materials and other supplies held for use in the production of inventories are not written down below cost if the finished products in which they will be incorporated are expected to be
   (a) sold at or above cost.
   (b) sold above cost.
   (c) sold less than cost.
   (d) sold at market value(where market value is more than cost).

3. All of the following costs are excluded while computing value of inventories except?
   (a) Selling and Distribution costs
   (b) Allocated fixed production overheads based on normal capacity.
   (c) Abnormal wastage
   (d) Storage costs (which is necessary part of the production process)

4. Identify the statement(s) which is/are incorrect.
   (a) Storage costs which is a necessary part of the production process is included in inventory valuation.
   (b) Administration overheads are never included in inventory valuation.
   (c) Full amount of variable production overheads incurred are included in inventory valuation.
   (d) Administration overheads are always included in inventory valuation.

Thanks ....

Chapter 6

AS 3 – CASH FLOW STATEMENTS

CHAPTER DESIGN

1. OBJECTIVE
2. CASH AND CASH EQUIVALENT
3. MEANING OF CASH FLOW
4. CLASSIFICATION OF CASH FLOW
5. CASH FLOW FROM OPERATION ACTIVITY

1. OBJECTIVE :

Cash flow Statement (CFS) is an additional information provided to the users of accounts in the form of an statement, which reflects the various sources from where cash was generated (inflow of cash) by an enterprise during the relevant accounting year and how these inflows were utilised (outflow of cash) by the enterprise.

2. CASH AND CASH EQUIVALENT :

Cash and cash equivalents for the purpose of cash flow statement consists of the following:

(a) Cash in hand and deposits repayable on demand with any bank or other financial institutions and

(b) Cash equivalents, which are short term, highly liquid investments that are readily convertible into known amounts of cash and are subject to insignificant risk or change in value. A short-term investment is one, which is due for maturity within three months from the date of acquisition. Investments in shares are not normally taken as cash equivalent, because of uncertainties associated with them as to realisable value.

Note : For the purpose of cash flow statement, 'cash and cash equivalent' consists of at least three balance sheet items, viz. cash in hand; demand deposits with banks etc. and investments regarded as cash equivalents. For this reason, the AS 3 requires enterprises to give a break-up of opening and closing cash shown in their cash flow statements. This is presented as a note to cash flow statement.

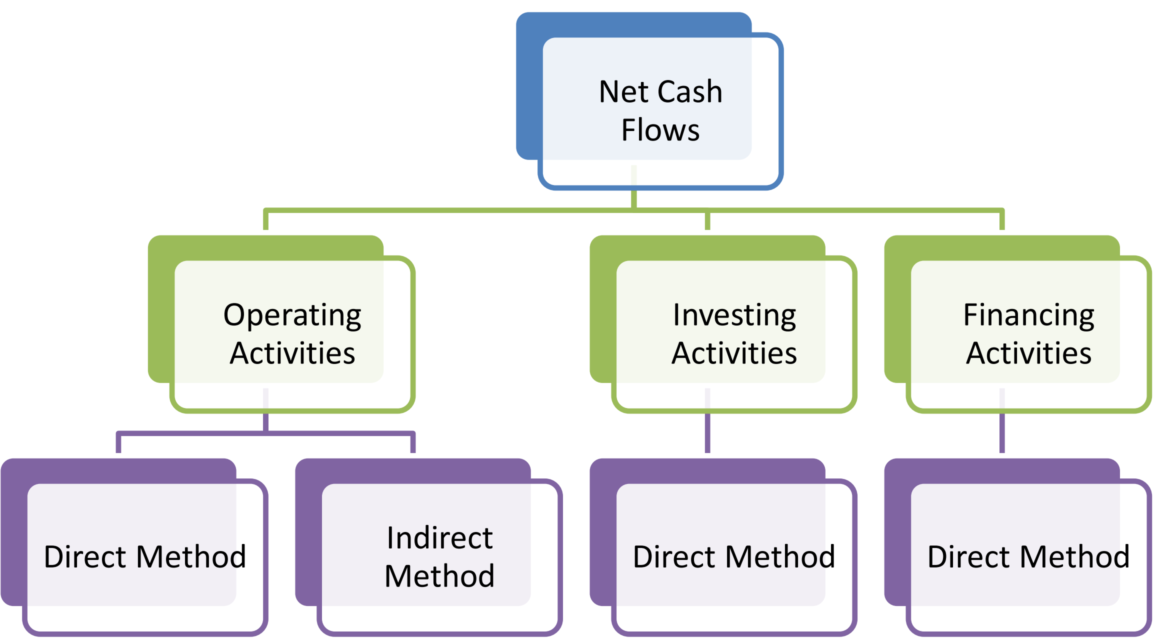
3. MEANING OF CASH FLOW :

Cash flows are inflows (i.e. receipts) and outflows (i.e. payments) of cash and cash equivalents. Any transaction, which does not result in cash flow, should not be reported in the cash flow statement. Movements within cash or cash equivalents are not cash flows because they do not change cash as defined by AS 3, which is sum of cash, bank and cash equivalents. For example, acquisitions of cash equivalent investments or cash deposited into bank are not cash flows. It is important to note that a change in cash does not necessarily imply cash flow.

For example suppose an enterprise has a bank balance of USD 10,000, stated in books at Rs 4,90,000 using the rate of exchange Rs 49/USD prevailing on date of receipt of dollars. If the closing rate of exchange is Rs 50/USD, the bank balance will be restated at Rs 5,00,000 on the balance sheet date. The increase is however not a cash flow because neither there is any cash inflow nor there is any cash outflow.

4. CLASSIFICATION OF CASH FLOWS :

The standard identifies three types of cash flows, i.e. operating cash flows, investing cash flows and financing cash flows. Separate presentation of each type of cash flow in the cash flow statement improves usefulness of cash flow information.



A few typical cases are discussed below.

1. Loans/Advances given and Interests earned :

(a) Loans and advances given and interests earned on them in the ordinary course of business are operating cash flows for financial enterprises.

(b) Loans and advances given and interests earned on them are investing cash flows for non-financial enterprises.

(c) Loans and advances given to subsidiaries and interests earned on them are investing cash flows for all enterprises.

(d) Loans and advances given to employees and interests earned on them are operating cash flows for all enterprises.

(e) Advance payments to suppliers and interests earned on them are operating cash flows for all enterprises.

(f) Interests earned from customers for late payments are operating cash flows for non-financial enterprises.

2. Loans/Advances taken and interests paid :

(a) Loans and advances taken and interests paid on them in the ordinary course of business are operating cash flows for financial enterprises.

(b) Loans and advances taken and interests paid on them are financing cash flows for non-financial enterprises.

(c) Loans and advances taken from subsidiaries and interests paid on them are financing cash flows for all enterprises.

(d) Advance taken from customers and interests paid on them are operating cash flows for non-financial enterprises.

(e) Interests paid to suppliers for late payments are operating cash flows for all enterprises.

(f) Interests taken as part of inventory costs in accordance with AS 16 are operating cash flows.

3. Investments made and dividends earned :

(a) Investments made and dividends earned on them in the ordinary course of business are operating cash flows for financial enterprises.

(b) Investments made and dividends earned on them are investing cash flows for non-financial enterprises.

(c) Investments in subsidiaries and dividends earned on them are investing cash flows for all enterprises.

4. Dividends Paid :

Dividends paid are financing cash outflows for all enterprises.

5. Income Tax :

(a) Tax paid on operating income is operating cash outflows for all enterprises

(b) Tax deducted at source against income are operating cash outflows if concerned incomes are operating incomes and investing cash outflows if the concerned incomes are investment incomes, e.g. interest earned.

(c) Tax deducted at source against expenses are operating cash inflows if concerned expenses are operating expenses and financing cash inflows if the concerned expenses are financing expenses, e.g. interests paid.

6. Insurance claims received :

(a) Insurance claims received against loss of stock or loss of profits are extraordinary operating cash inflows for all enterprises.

(b) Insurance claims received against loss of fixed assets are extraordinary investing cash inflows for all enterprises.

AS 3 requires separate disclosure of extraordinary cash flows, classifying them as cash flows from operating, investing or financing activities, as may be appropriate.

5. CASH FLOW FROM OPERATING ACTIVITY :

Net cash flow from operating activities can be reported either as direct method or as indirect method.

Cash flow statement of X Ltd for the year ended 31st March, XXXX as per AS – 3 (Revised)
Direct Method

Particulars	Rs.	Rs.
Operating Activity		
Receipts		
Cash received from cash Sales	XXX	
Cash received from debtors	XXX	
Cash received from sale of services	XXX	XXX
Less: Payments		
Payment for cash Purchase	XXX	
Payment to creditors	XXX	
Payment for rent	XXX	
Payment for wages & Salaries	XXX	
Payment for operating expenses	XXX	XXX
Cash from operations		XXX
Less Payment for Income tax		XXX
		XXX
Adjustment for extra ordinary Activities		XXX
Cash from operating Activity		XXX

Cash flow statement of X Ltd for the year ended 31st March, XXXX as per AS – 3 (Revised)
Indirect Method

Particulars	Rs.	Rs.
Operating Activity		
Closing Balance of Profit and Loss A/c		XXX
Less: Opening Balance of Profit and Loss A/c		XXX
		XXX
Add: Appropriation		
1. Transfer to Reserves	XXX	
2. Proposed Dividend	XXX	XXX
		XXX
Add: Non cash Non-Operating Expenses		
1. Depreciation of FA	XXX	
2. Loss on sale of Asset	XXX	
3. Others	XXX	XXX
		XXX

Less: Non Cash Non-Operating Income		
1. Profit on sale of Assets	XXX	
2. Others	XXX	XXX
Funds from Operations		XXX
Add : Decrease in Working Capital		
1. Decrease in Stock	XXX	
2. Decrease in Debtors	XXX	
3. Increase in Creditors	XXX	XXX
		XXX
Less : Increase in Working Capital		
1. Increase in Bills receivable	XXX	
2. Decrease in Bills payable	XXX	XXX
Cash from Operations		XXX
Less Tax Paid		XXX
		XXX
Adjust Extra ordinary Items		XXX
Cash From operating Activity		XXX

Some important transactions

1. Business Purchase :

The aggregate cash flows arising from acquisitions and disposals of subsidiaries or other business units should be presented separately and classified as cash flow from investing activities.

(a) The cash flows from disposal and acquisition should not be netted off.

(b) An enterprise should disclose, in aggregate, in respect of both acquisition and disposal of subsidiaries or other business units during the period each of the following:

(i) The total purchase or disposal consideration; and

(ii) The portion of the purchase or disposal consideration discharged by means of cash and cash equivalents.

Treatment of current assets and liabilities taken over on business purchase Business purchase is not operating activity. Thus, while taking the differences between closing and opening current assets and liabilities for computation of operating cash flows, the closing balances should be reduced by the values of current assets and liabilities taken over. This ensures that the differences reflect the increases/decreases in current assets and liabilities due to operating activities only.

2. Exchange gains and losses :

The foreign currency monetary assets (e.g. balance with bank, debtors etc.) and liabilities (e.g. creditors) are initially recognised by translating them into reporting currency by the rate of exchange transaction date. On the balance sheet date, these are restated using the rate of exchange on the balance sheet date. The difference in values is exchange gain/loss. The exchange gains and losses are recognised in the statement of profit and loss.

The exchange gains/losses in respect of cash and cash equivalents in foreign currency (e.g. balance in foreign currency bank account) are recognised by the principle aforesaid, and these balances are restated in the balance sheet in reporting currency at rate of exchange on balance sheet date. The change in cash or cash equivalents due to exchange gains and losses are however not cash flows. This being so, the net increases/decreases in cash or cash equivalents in the cash flow statements are stated exclusive of exchange gains and losses. The resultant difference between cash and cash equivalents as per the cash flow statement and that recognised in the balance sheet is reconciled in the note on cash flow statement.

PRACTICAL QUESTIONS :

Question 1 :

Classify the following activities as (a) Operating Activities, (b) Investing Activities, (c) Financing Activities (d) Cash Equivalents.

(a) Purchase of Machinery.
(b) Proceeds from issuance of equity share capital
(c) Cash Sales.
(d) Proceeds from long-term borrowings.
(e) Proceeds from Trade receivables.
(f) Cash receipts from Trade receivables.
(g) Trading Commission received.
(h) Purchase of investment.
(i) Redemption of Preference Shares.
(j) Cash Purchases.
(k) Proceeds from sale of investment
(l) Purchase of goodwill.
(m) Cash paid to suppliers.
(n) Interim Dividend paid on equity shares.
(o) Wages and salaries paid.
(p) Proceed from sale of patents.
(q) Interest received on debentures held as investment.

(r) Interest paid on Long-term borrowings.
(s) Office and Administration Expenses paid
(t) Manufacturing Overheads paid.
(u) Dividend received on shares held as investments.
(v) Rent Received on property held as investment.
(w) Selling and distribution expense paid.
(x) Income tax paid
(y) Dividend paid on Preference shares.
(z) Underwritings Commission paid.
(aa) Rent paid.
(bb) Brokerage paid on purchase of investments.
(cc) Bank Overdraft
(dd) Cash Credit
(ee) Short-term Deposits
(ff) Marketable Securities
(gg) Refund of Income Tax received.

Question 2 : X Ltd.

X Ltd. purchased debentures of Rs.10 lacs of Y Ltd., which are redeemable within three months. How will you show this item as per AS 3 while preparing cash flow statement for the year ended on 31st March, 2017?

Question 3 :

Classify the following activities as per AS 3 Cash Flow Statement:
(i) Interest paid by financial enterprise
(ii) Tax deducted at source on interest received from subsidiary company
(iii) Deposit with Bank for a term of two years
(iv) Insurance claim received towards loss of machinery by fire
(v) Bad debts written off

Question 4 : Alpha Ltd.

Following is the cash flow abstract of Alpha Ltd. for the year ended 31st March, 2017:

Cash Flow (Abstract)

Inflow	Rs.	Outflow	Rs.
Opening balance:		Payment for Account Payables	90,000
Cash	10,000	Salaries and wages	25,000
Bank	70,000	Payment of overheads	15,000

Share capital – shares issued	5,00,000	Fixed assets acquired	4,00,000
Collection on account of Trade Receivables	3,50,000	Debentures redeemed	50,000
Sale of fixed assets	70,000	Bank loan repaid	2,50,000
		Taxation	55,000
		Dividends (including dividend distribution tax)	1,00,000
		Closing balance:	
		Cash	5,000
		Bank	10,000
	10,00,000		**10,00,000**

Prepare Cash Flow Statement for the year ended 31st March, 2017 in accordance with Accounting standard 3.

Question 5 : M/s. Creative Furnishings Limited

Prepare Cash Flow from Investing Activities of M/s. Creative Furnishings Limited for the year ended 31-3-2017.

	Rs.
Plant acquired by the issue of 8% Debentures	1,56,000
Claim received for loss of plant in fire	49,600
Unsecured loans given to subsidiaries	4,85,000
Interest on loan received from subsidiary companies	82,500
Pre-acquisition dividend received on investment made	62,400
Debenture interest paid	1,16,000
Term loan repaid	4,25,000
Interest received on investment	68,000
(TDS of Rs.8,200 was deducted on the above interest)	
Book value of plant sold (loss incurred Rs.9,600)	84,000

MCQs :

1. Crown Ltd. wants to prepare its cash flow statement. It sold equipment of book value of Rs. 60,000 at a gain of Rs. 8,000. The amount to be reported in its cash flow statement under operating activities is

   (a) Nil (b) Rs. 8,000

   (c) Rs. 68,000 (d) Rs. 60,000

2. While preparing cash flows statement, an entity (other than a financial institution) should disclose the dividends received from its investment in shares as

(a) operating cash inflow (b) investing cash inflow
(c) financing cash inflow (d) cash & cash equivalent

3. XYZ Co. is a financial enterprise. In its cash flow statement, interest paid and dividends received should be
   (a) classified as operating cash flows.
   (b) classified as financing cash flows.
   (c) Not shown in cash flow statement.
   (d) classified as investing cash flows.
4. In the cash flow statement, 'cash and cash equivalents' donot include
   (a) Bank balances .
   (b) Short-term investments readily convertible into Cash are subject to an insignificant risk of changes in value.
   (c) Cash balances.
   (d) Loan from bank.
5. While preparing a Cash Flow Statement using the Indirect method as required under AS 3, which of the following will not be deducted from/added to the Net Profit to arrive at the "Cash flow from Operating activities"?
   (a) Interest income (b) Gain on sale of a fixed asset.
   (c) Depreciation. (d) Gain on sale of inventory

Thanks ....

Chapter 7

AS 4 – CONTINGENCIES & EVENTS OCCURING AFTER THE BALANCE SHEET DATE

CHAPTER DESIGN

1. DEFINITIONS
2. TYPES OF EVENTS
3. TREATMENT OF ADJUSTING AND NON-ADJUSTING EVENTS
4. DISCLOSURE
5. EXCEPTION TO RULE

1. DEFINITIONS :

1. **Contingencies :** Contingency is a condition or situation, the ultimate outcome of which, gain or loss, will be known or determined only on the occurrence, or non-occurrence, of one or more uncertain future events.
2. **Events Occurring after the Balance Sheet Date :** Events occurring after the balance sheet date are those significant events, both favourable and unfavourable, that occur between the balance sheet date and the date on which the financial statements are approved by the Board of Directors in the case of a company, and, by the corresponding approving authority in the case of any other entity.

For example, for the year ending on 31st March 2017, financial statement is finalised and approved by the Board of the directors of the company in its meeting held on 04th September 2017. In this case the events taking place between 01st April 2017 to 04th September 2017 are termed as events occurring after the balance sheet date.

2. TYPES OF EVENTS :

a. **Adjusting events-** those which provide further evidence of conditions that existed at the balance sheet date. For example a trade receivable declared insolvent and estate unable to pay full amount against whom provision for doubtful debt was created.

b. **Non-adjusting events-** those which are indicative of conditions that arose subsequent to the balance sheet date.

Adjusting

those which provide further evidence of conditions that existed at the balance sheet date

those which are indicative of conditions that arose subsequent to the balance sheet date.

Non Adjusting Event

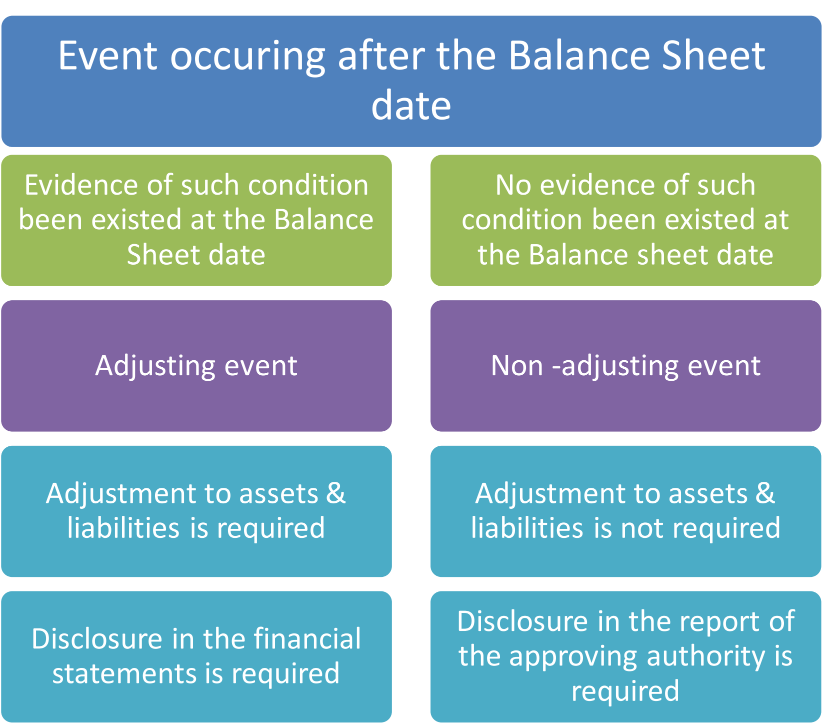
3. TREATMENT OF ADJUSTING AND NON ADJUSTING EVENTS :

A. **Adjusting Events :** Adjustments to assets and liabilities are required for events occurring after the balance sheet date that provide additional information materially affecting the determination of the amounts relating to conditions existing at the balance sheet date. For example, an adjustment may be made for a loss on a trade receivable account which is confirmed by the insolvency of a customer which occurs after the balance sheet date.

B. Non-Adjusting Events : Adjustments to assets and liabilities are not appropriate for events occurring after the balance sheet date, if such events do not relate to conditions existing at the balance sheet date. An example is the decline in market value of investments between the balance sheet date and the date on which the financial statements are approved. Ordinary fluctuations in market values do not normally relate to the condition of the investments at the balance sheet date, but reflect circumstances which have occurred in the following period.

Events occurring after the balance sheet date which do not affect the figures stated in the financial statements would not normally require disclosure in the financial statements although they may be of such significance that they may require a disclosure in the report of the approving authority to enable users of financial statements to make proper evaluations and decisions.

There are events which, although take place after the balance sheet date, are sometimes reflected in the financial statements because of statutory requirements or because of their special nature. For example, if dividends are declared after the balance sheet date but before the financial statements are approved for issue, the dividends are not recognised as a liability at the balance sheet date because no obligation exists at that time unless a statute requires otherwise. Such dividends are disclosed in the notes. Thus, no liability for proposed dividends needs to be recognised for financial statements for year ended 2016-17 and subsequent years. Such proposed dividends are to be disclosed in the notes as per Companies (Accounting Standards) Amendment Rules, 2016 issued on 30 March 2016.



4. DISCLOSURE :

Disclosure of events occurring after the balance sheet date requires the following information should be provided:

(a) The nature of the event;

(b) An estimate of the financial effect, or a statement that such an estimate cannot be made.

Example A company follows April-March as its financial year. The company recognises cheques dated 31st March or before, received from customers after balance sheet date but before approval of financial statement by debiting Cheques in hand A/c and crediting the Debtors A/c. The Cheques in hand is shown in balance sheet as an item of cash and cash equivalents. All Cheques in hand are presented to bank in the month of April and are also realised in the same month in normal course after deposit in the bank.

Even if the cheques bear the date 31st March or before, the cheques received after 31st March do not represent any condition existing on 31st March. Thus the collection of cheques after balance sheet date is not an adjusting event. Recognition of cheques in hand is therefore not consistent with requirements of AS 4 (Revised). Moreover, the collection of cheques after balance sheet date does not represent any material change or commitments affecting financial position of the enterprise, and so no disclosure of such collections in the Directors' Report is necessary.

It should also be noted that, the Framework for Preparation and Presentation of Financial Statement defines assets as resources controlled by an enterprise as a result of past events from which economic benefits are expected to flow to the enterprise. Since the company acquires custody of the cheques after 31st March, it does not have any control over the cheques on 31st March and hence cheques in hand do not qualify to be recognised as asset on 31st March.

5. EXCEPTION TO THE RULE :

Events indicating going concern assumption inappropriate:

As per AS 4 (Revised), an event occurring after the balance sheet date should be an adjusting event even if it does not reflect any condition existing on the balance sheet date, if the event is such as to indicate that the fundamental accounting assumption of going concern is no longer appropriate.

Suppose a fire occurred in the factory and office premises of an enterprise after 31/03/17 but before approval of financial statement of 2016-17. The loss on fire is of such a magnitude that it is not reasonable to expect the enterprise to start operations again, i.e., the going concern assumption is not valid. Since the fire occurred after 31/03/17, the loss on fire is not a result of

any condition existing on 31/03/17. In such a case, the entire accounts need to be prepared on a liquidation basis with adequate disclosures.

PRACTICAL QUESTIONS :

Questions 1 : X Co. Ltd.

In X Co. Ltd., theft of cash of Rs 5 lakhs by the cashier in January, 2017 was detected only in May, 2017. The accounts of the company were not yet approved by the Board of Directors of the company. Whether the theft of cash has to be adjusted in the accounts of the company for the year ended 31.3.2017. Decide.

Questions 2 :

An earthquake destroyed a major warehouse of ACO Ltd. on 20.5.2017. The accounting year of the company ended on 31.3.2017. The accounts were approved on 30.6.2017. The loss from earthquake is estimated at Rs. 30 lakhs. State with reasons, whether the loss due to earthquake is an adjusting or non-adjusting event and how the fact of loss is to be disclosed by the company.

Questions 3 :

A company has filed a legal suit against the debtor from whom Rs 15 lakh is recoverable as on 31.3.2017. The chances of recovery by way of legal suit are not good as per legal opinion given by the counsel in April, 2017. Can the company provide for full amount of Rs 15 lakhs as provision for doubtful debts? Discuss.

Questions 4 : R Ltd.

In preparing the financial statements of R Ltd. for the year ended 31st March, 2017, you come across the following information. State with reasons, how you would deal with this in the financial statements:

The company invested 100 lakhs in April, 2017 before approval of Financial Statements by the Board of directors in the acquisition of another company doing similar business, the negotiations for which had started during the year.

Question 5 :

A Limited Company closed its accounting year on 30.6.2017 and the accounts for that period were considered and approved by the board of directors on 20th August, 2017. The company was engaged in laying pipe line for an oil company deep beneath the earth. While doing the boring work on 1.9.2017 it had met a rocky surface for which it was estimated that there would be an extra cost to the tune of Rs. 80 lakhs. You are required to state with

reasons, how the event would be dealt with in the financial statements for the year ended 30.6.2017.

Question 6 :

While preparing its final accounts for the year ended 31st March, 2017 a company made a provision for bad debts @ 5% of its total trade receivables. In the last week of February, 2017 a trade receivable for Rs.2 lakhs had suffered heavy loss due to an earthquake; the loss was not covered by any insurance policy. In April, 2017 the trade receivable became a bankrupt. Can the company provide for the full loss arising out of insolvency of the trade receivable in the final accounts for the year ended 31st March, 2017?

Question 7 : Raj Ltd.

During the year 2015-2016, Raj Ltd. was sued by a competitor for Rs.15 lakhs for infringement of a trademark. Based on the advice of the company's legal counsel, Raj Ltd. provided for a sum of Rs.10 lakhs in its financial statements for the year ended 31st March, 2016. On 18th May, 2016, the Court decided in favour of the party alleging infringement of the trademark and ordered Raj Ltd. to pay the aggrieved party a sum of Rs. 14 lakhs. The financial statements were prepared by the company's management on 30th April, 2016, and approved by the board on 30th May, 2016.

MCQs :

1. Cash amounting to Rs. 4 lakhs, stolen by the cashier in the month of March 20X1, was detected in April, 20X1. The financial statements for the year ended 31st March, 20X1 were approved by the Board of Directors on 15th May, 20X1. As per Accounting Standards, this is ______ for the financial statements year ended on 31st March, 20X1.
   (a) An Adjusting event. (b) Non-adjusting event.
   (c) Contingency. (d) Provision
2. As per Accounting Standards, events occurring after the balance sheet date are
   (a) Only favourable events that occur between the balance sheet date and the date when the financial statements are approved by the Board of directors.
   (b) Only unfavourable events that occur between the balance sheet date and the date when the financial statements are approved by the Board of directors.
   (c) Those significant events, both favourable and unfavourable, that occur between the balance sheet date and the date on which the financial statements are approved by the Board of directors.
   (d) Those significant events, both favourable and unfavourable, that occur between the balance sheet date and the date on which the financial statements are not approved by the Board of directors.

3. AS 4 does not apply to
   (a) Obligation under retirement benefit plans.
   (b) Commitments arising from long term lease contracts.
   (c) liabilities of life assurance and general insurance enterprises arising from policies issued
   (d) Both (a) & (b).

4. A Ltd. sold its building for Rs. 50 lakhs to B Ltd. and has also given the possession to B Ltd. The book value of the building is Rs. 30 lakhs. As on 31st March, 20X1, the documentation and legal formalities are pending. For the financial year ended 31st March, 20X1
   (a) The company should record the sale.
   (b) The company should recognise the profit of Rs. 20 lakhs in its profit and loss account.
   (c) Both (a) and (b).
   (d) The company should disclose the profit of Rs. 20 lakhs in notes to accounts.

Thanks ....

Chapter 8

AS 5 – NET PROFIT OR LOSS FOR THE PERIOD, PRIOR PERIOD ITEMS & CHANGES IN ACCOUNTING POLICIES

CHAPTER DESIGN

1. INTRODUCTION
2. NET PROFIT OR LOSS FOR THE PERIOD
3. PRIOR PERIOD ITEMS
4. CHANGES IN ACCOUNTING ESTIMATES
5. CHANGES IN ACCOUNTING POLICY

1. INRODUCTION :

The objective of AS 5 is to prescribe the classification and disclosure of certain items in the statement of profit and loss so that all enterprises prepare and present such a statement on a uniform basis. This enhances the comparability of the financial statements of an enterprise over time and with the financial statements of other enterprises. Accordingly, AS 5 requires the classification and disclosure of extraordinary and prior period items, and the disclosure of certain items within profit or loss from ordinary activities. It also specifies the accounting treatment for changes in accounting estimates and the disclosures to be made in the financial statements regarding changes in accounting policies.

This Statement does not deal with the tax implications of extraordinary items, prior period items, changes in accounting estimates, and changes in accounting policies for which appropriate adjustments will have to be made depending on the circumstances.

2. NET PROFIT OR LOSS FOR THE PERIOD :

All items of income and expense which are recognised in a period should be included in the determination of net profit or loss for the period unless an Accounting Standard requires or permits otherwise.

Net Profit or Loss for the period

- Ordinary Items
- Extra ordinary items
- Prior Period Items
- Changes in Accounting Estimates
- Changes in Accounting Policies

The net profit or loss for the period comprises the following components, each of which should be disclosed on the face of the statement of profit and loss:

(a) Profit or loss from ordinary activities:

Any activities which are undertaken by an enterprise as part of its business and such related activities in which the enterprise engages in furtherance of, incidental to, or arising from, these activities. For example profit on sale of merchandise, loss on sale of unsold inventory at the end of the season.

(b) Extraordinary items :

Income or expenses that arise from events or transactions that are clearly distinct from the ordinary activities of the enterprise and, therefore, are not expected to recur frequently or regularly.

Extraordinary items should be disclosed in the statement of profit and loss as a part of net profit or loss for the period.

The nature and the amount of each extraordinary item should be separately disclosed in the statement of profit and loss in a manner that its impact on current profit or loss can be perceived. Whether an event or transaction is clearly distinct from the ordinary activities of the enterprise is determined by the nature of the event or transaction in relation to the business ordinarily carried on by the enterprise rather than by the frequency with which such events are expected to occur. Therefore, an event or transaction may be extraordinary for one enterprise but not so for another enterprise because of the differences between their respective ordinary activities. For example, losses sustained as a result of an earthquake may qualify as an extraordinary item for many enterprises. However, claims from policyholders arising from an earthquake do not qualify as an extraordinary item for an insurance enterprise that insures against such risks.

Examples of events or transactions that generally give rise to extraordinary items for most enterprises are:

– attachment of property of the enterprise
– an earthquake

(c) Exceptional items* :

When items of income and expense within profit or loss from ordinary activities are of such size, nature or incidence that their disclosure is relevant to explain the performance of the enterprise for the period, the nature and amount of such items should be disclosed separately.

Circumstances which may give rise to the separate disclosure of items of income and expense include:

(a) The write-down of inventories to net realisable value as well as the reversal of such write-downs
(b) A restructuring of the activities of an enterprise and the reversal of any provisions for the costs of restructuring
(c) Disposals of items of fixed assets
(d) Disposals of long-term investments

(e) Legislative changes having retrospective application

(f) Litigation settlements

(g) Other reversals of provisions

*There is no such term as 'exceptional item' under AS 5 and Schedule III to the Companies Act, 2013, however, the same has been used for better understanding of the requirement. Students may provide a suitable note in this regard in the examination

3. PRIOR PERIOD ITEMS :

Prior period items are 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 prior periods.

Errors in the preparation of the financial statements of one or more prior periods may be discovered in the current period. Errors may occur as a result of mathematical mistakes, mistakes in applying accounting policies, misinterpretation of facts, or oversight.

The nature and amount of prior period items should be separately disclosed in the statement of profit and loss in a manner that their impact on the current profit or loss can be perceived.

4. CHANGES IN ACCOUNTING ESTIMATES :

An estimate may have to be revised if changes occur in the circumstances based on which the estimate was made, or as a result of new information, more experience or subsequent developments. The revision of the estimate, by its nature, does not bring the adjustment within the definitions of an extraordinary item or a prior period item.

Accounting estimates by their nature are approximations that may need revision as additional information becomes known. For example, income or expense recognised on the outcome of a contingency which previously could not be estimated reliably does not constitute a prior period item.

For example, Sachin purchased a new machine costing Rs. 10 lacs. Useful life was taken to be for 10 years, therefore, depreciation was charged at 10% on original cost each year. After 5 years when carrying amount was Rs. 5 lacs for the machine, management realises that machine can work for another 2 years only and they decide to write off Rs. 2.5 lacs each year. This is not an example of prior period item but change in accounting estimate. In the same example management by mistake calculates the depreciation in the fifth year as 10% of Rs. 6,00,000 i.e. Rs. 60,000 instead of Rs. 1,00,000 and in the next year decides to write off Rs. 1,40,000. In such a case, Rs. 1,00,000 current year's depreciation and Rs. 40,000 will be considered as prior period item.

As per AS 10 (Revised), Property, Plant and Equipment, residual value and the useful life of an asset should be reviewed at least at each financial year-end and, if expectations differ from previous estimates, the change should be accounted for as a change in an accounting estimate in accordance with AS 5 'Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies'.

The effect of a change in an accounting estimate should be included in the determination of net profit or loss in:

(a) The period of the change, if the change affects the period only; or

(b) The period of the change and future periods, if the change affects both.

For example, a change in the estimate of the amount of bad debts is recognised immediately and therefore affects only the current period. However, a change in the estimated useful life of a depreciable asset affects the depreciation in the current period and in each period during the remaining useful life of the asset.

The effect of a change in an accounting estimate should be classified using the same classification in the statement of profit and loss as was used previously for the estimate.

To ensure the comparability of financial statements of different periods, the effect of a change in an accounting estimate which was previously included in the profit or loss from ordinary activities is included in that component of net profit or loss.

The effect of a change in an accounting estimate that was previously included as an extraordinary item is reported as an extraordinary item.

The nature and amount of a change in an accounting estimate which has a material effect in the current period, or which is expected to have a material effect in subsequent periods, should be disclosed. If it is impracticable to quantify the amount, this fact should be disclosed.

5. CHANGES IN ACCOUNTING POLICY :

Accounting policies are the specific accounting principles and the methods of applying those principles adopted by an enterprise in the preparation and presentation of financial statements.

Accounting Policies can be changed only:

- when the adoption of a different accounting policy is required by statute; or
- for compliance with an Accounting Standard; or

- when it is considered that the change would result in a more appropriate presentation of the financial statements of the enterprise.

The following are not changes in accounting policies:

(a) The adoption of an accounting policy for events or transactions that differ in substance from previously occurring events or transactions, e.g., introduction of a formal retirement gratuity scheme by an employer in place of ad hoc exgratia payments to employees on retirement;

(b) The adoption of a new accounting policy for events or transactions which did not occur previously or that were immaterial.

PRACTICAL QUESTIONS :

Question :1

Fuel surcharge is billed by the State Electricity Board at provisional rates. Final bill for fuel surcharge of Rs. 5.30 lakhs for the period October, 2008 to September, 2015 has been received and paid in February, 2016. However, the same was accounted in the year 2016-17. Comment on the accounting treatment done in the said case.

Question 2 :

(i) During the year 2016-2017, a medium size manufacturing company wrote down its inventories to net realisable value by Rs. 5,00,000. Is a separate disclosure necessary?

(ii) A company signed an agreement with the Employees Union on 1.9.2016 for revision of wages with retrospective effect from 30.9.2015. This would cost the company an additional liability of Rs. 5,00,000 per annum. Is a disclosure necessary for the amount paid in 2016-17?

Question : 3

The company finds that the inventory sheets of 31.3.2016 did not include two pages containing details of inventory worth Rs 14.5 lakhs. State, how you will deal with the following matters in the accounts of Omega Ltd. for the year ended 31st March, 2017.

Question 4 :

Explain whether the following will constitute a change in accounting policy or not as per AS 5.

(i) Introduction of a formal retirement gratuity scheme by an employer in place of ad hoc ex-gratia payments to employees on retirement.

(ii) Management decided to pay pension to those employees who have retired after completing 5 years of service in the organisation. Such employees will get pension of Rs. 20,000 per month. Earlier there was no such scheme of pension in the organisation.

MCQs :

1. A change in the estimated life of the asset, which necessitates adjustment in the depreciation is an example of
   (a) Prior period item. (b) Ordinary item.
   (c) Extraordinary item. (d) Change in accounting estimate.
2. Which of the following is considered as an extraordinary item as per AS 5?
   (a) Write down or write-off of receivables, inventory and intangible assets.
   (b) Gains and losses from sale or abandonment of equipment used in a business.
   (c) Effects of a strike, including those against competitors and major suppliers.
   (d) Flood damage from unusually heavy rain or a normally dry environment.
3. Which one of the following is an example of extraordinary item?
   (a) The write down of inventories to their net realisable value
   (b) Reversal of write down of inventories
   (c) Government grants become refundable
   (d) Reversal of provisions.
4. Extraordinary items are income or expenses
   (a) That arise from events clearly distinct from the ordinary activities of the enterprise.
   (b) That are not expected to recur frequently or regularly.
   (c) Both (a) and (b).
   (d) None of the three.
5. An audit stock verification during the year ended 31st March, 20X1 revealed that opening stock of the year was understated by ` 5 lakhs due to wrong counting. While finalizing accounts, your opinion will be
   (a) It is not a prior period item and no separate disclosure is required
   (b) It should be treated as a prior period adjustment and should be separately disclosed in the current year's financial statement
   (c) The adjustment of ` 5 lakhs in both opening stock of current year and profit brought forward from previous year should be made
   (d) Both (b) and (c).

Thanks ....

Rahul Malkan

Chapter 9

AS 7 – CONSTRUCTION CONTRACTS

CHAPTER DESIGN

1. INTRODUCTION
2. CONSTRUCTION CONTRACT
3. TYPES OF CONSTRUCTION CONTRACTS
4. MEASUREMENT OF CONTRACT REVENUE
5. STAGE OF COMPLETION
6. COMBINING AND SEGMENTING CONSTRUCTION CONTRACTS
7. CHANGES IN ESTIMATES

1. INRODUCTION :

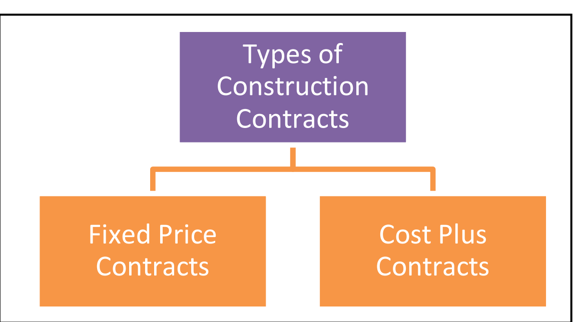
Accounting Standard 7 prescribes the principles of accounting for construction contracts in the financial statements of contractors. The focus of the standard is on principles of revenue recognition by the contractors.

2. CONSTRUCTIONS CONTACTS :

A construction contract may be negotiated for the construction of a single asset such as a bridge, building, dam, pipeline, road, ship or tunnel. A construction contract may also deal with the construction of a number of assets which are closely interrelated or interdependent in terms of their design, technology and function or their ultimate purpose or use; examples of such contracts include those for the construction of refineries and other complex pieces of plant or equipment.

3. TYPES OF CONSTRUCTION CONTACTS :

1. **Fixed Price Contracts :** In a **fixed price contract**, the price is agreed as fixed sum or a fixed rate per unit of output. In some cases, the contract may require the customer to pay additional sums to compensate the contractor against cost escalations.



2. **Cost Plus Contracts :** A cost plus contract is a construction contract in which the contractor is reimbursed for allowable or otherwise defined costs, plus percentage of these costs or a fixed fee.

4. MEASUREMENT OF CONTRACT REVENUE :

Percentage Completion Method :

Construction contracts are mostly long term, i.e. they take more than one accounting year to complete. This means, the final outcome (profit/ loss) of a construction contract can be determined only after a number of years from the year of commencement of construction are over. It is nevertheless possible to recognise revenue annually in proportion of progress of work to be matched with corresponding construction costs incurred in that year. This method of accounting, called the stage of completion method (percentage completion method), provides useful information on the extent of contract activity and performance during an accounting period.

The percentage completion method may suffer from a serious drawback viz. anticipation of profit. Since the method recognises revenue pending final outcome of a contract is known, it is possible

that an enterprise may distribute dividend based on reported profit of a year, while final result is loss. To avoid such possibilities, percentage completion method should be used with caution. AS 7 prescribes that the percentage completion method should not be used unless it is possible to make a reasonable estimate of the final outcome of the contract.

Also, AS 7 provides that whenever total contract cost is expected to exceed the total contract revenue, the loss should be recognised as an expense immediately.

As per AS 7, the outcome of fixed price contracts can be estimated reliably **when all the following conditions are satisfied:**

(i) total contract revenue can be measured reliably;

(ii) it is probable that the economic benefits associated with the contract will flow to the enterprise;

(iii) both the contract costs to complete the contract and the stage of contract completion at the reporting date can be measured reliably; and

(iv) the contract costs attributable to the contract can be clearly identified and measured reliably so that actual contract costs incurred can be compared with prior estimates.

The outcome of a cost plus contract can be estimated reliably when all the following conditions are satisfied:

(i) it is probable that the economic benefits associated with the contract will flow to the enterprise; and

(ii) the contract costs attributable to the contract, whether or not specifically reimbursable, can be clearly identified and measured reliably.

Question 1 : X Ltd.

X Ltd. commenced a construction contract on 01/04/13. The fixed contract price agreed was Rs 2,00, 000. The company incurred Rs 81,000 in 2013-14 for 45% work and received Rs 79,000 as progress payment from the customer. The cost incurred in 2014-15 was Rs 89,000 to complete the rest of work.

Question 2 : XYZ ltd.

XYZ Ltd. commenced a construction contract on 01/04/13. The contract price agreed was reimbursable cost plus 20%. The company incurred Rs 1,00,000 in 2013-14, of which Rs 90,000 is reimbursable. The further non-reimbursable costs to be incurred to complete the contract are estimated at Rs 5,000. The other costs to complete the contract could not be estimated reliably.

Treatment of Costs Relating to Future Activity :

Under the percentage of completion method, contract revenue is recognised as revenue in the statement of profit and loss in the accounting periods in which the work is performed. Contract costs are usually recognised as an expense in the statement of profit and loss in the accounting periods in which the work to which they relate is performed. The contract costs that relate to future activity on the contract are however recognised as an asset provided it is probable that they will be recovered. Such costs represent an amount due from the customer and are often classified as contract work in progress.

Uncollectable Contract Revenue :

When an uncertainty arises about the collectability of an amount already included in contract revenue, and already recognised in the statement of profit and loss, the uncollectable amount or the amount in respect of which recovery has ceased to be probable is recognised as an expense rather than as an adjustment of the amount of contract revenue.

5. STAGE OF COMPLETION :

The stage of completion of a contract may be determined in a variety of ways. The enterprise uses the method that measures reliably the work performed. Depending on the nature of the contract, the methods may include:

(a) the proportion that contract costs incurred for work performed upto the reporting date bear to the estimated total contract costs; or

(b) surveys of work performed; or

(c) completion of a physical proportion of the contract work.

Progress payments and advances received from customers may not necessarily reflect the work performed.

Question 3 :

Show Profit & Loss A/c (Extract) in books of a contractor in respect of the following data.

	Rs. 000
Contract price (Fixed)	600
Cost incurred to date	390
Estimated cost to complete	260

6. COMBININ AND SEGMENTING CONSTRUICTION CONTRACTS :

A contractor may undertake a number of contracts. The standard identifies certain cases where for the purposes of accounting, (i) More than one contract can be taken as one and (ii) a single contract can be taken as to comprise of more than one contract.

(a) When a contract covers a number of assets, the construction of each asset should be treated as a separate construction contract when:
   (i) separate proposals have been submitted for each asset;
   (ii) 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
   (iii) the costs and revenues of each asset can be identified.

(b) A group of contracts, whether with a single customer or with several customers, should be treated as a single construction contract when:
   (i) the group of contracts is negotiated as a single package;
   (ii) the contracts are so closely interrelated that they are, in effect, part of a single project with an overall profit margin; and
   (iii) the contracts are performed concurrently or in a continuous sequence.

(c) A contract may provide for the construction of an additional asset at the option of the customer or may be amended to include the construction of an additional asset. The construction of the additional asset should be treated as a separate construction contract when:
   (i) the asset differs significantly in design, technology or function from the asset or assets covered by the original contract; or
   (ii) the price of the asset is negotiated without regard to the original contract price.

Question 4 : Mr. Shyam

Mr. Shyam, a construction contractor undertakes the construction of an industrial complex. He has separate proposals raised for each unit to be constructed in the industrial complex. Since each unit is subject to separate negotiation, he is able to identify the costs and revenues attributable to each unit. Should Mr. Shyam treat construction of each unit as a separate construction contract according to AS 7?

7. CHANGES IN ESTIMATES :

The percentage of completion method is applied on a cumulative basis in each accounting period to the current estimates of contract revenue and contract costs. Therefore, the effect of a change in the estimate of contract revenue or contract costs, or the effect of a change in the estimate of the outcome of a contract, is accounted for as a change in accounting estimate in accordance with AS 5. The changed estimates are used in determination of the amount of revenue and expenses recognised in the statement of profit and loss in the period in which the change is made and in subsequent periods.

PRACTICAL QUESTIONS :

Question 5 :

A firm of contractors obtained a contract for construction of bridges across river Revathi. The following details are available in the records kept for the year ended 31st March, 2017.

	(Rs in lakhs)
Total Contract Price	1,000
Work Certified	500
Work not Certified	105
Estimated further Cost to Completion	495
Progress Payment Received	400
To be Received	140

The firm seeks your advice and assistance in the presentation of accounts keeping in view the requirements of AS 7 issued by your institute.

Question 6 : Vishwakarma Construction Co. Ltd.

On 1st December, 2016, Vishwakarma Construction Co. Ltd. undertook a contract to construct a building for Rs 85 lakhs. On 31st March, 2017, the company found that it had already spent Rs 64,99,000 on the construction. Prudent estimate of additional cost for completion was Rs 32,01,000. What amount should be charged to revenue in the final accounts for the year ended 31st March, 2017 as per provisions of Accounting Standard 7 (Revised)?

Question 7 : M/s. Highway constructions

M/s. Highway constructions undertook the construction of a highway on 01.04.2013. the contract was to be completed in 10 years. The contract price was estimated at Rs. 150 cores. Up to 31.03.2014 the company incurred Rs. 120 cores on the construction. The engineers involved in the project estimated that a further Rs. 45 cores would be incurred for completing the work.

What amount should be charged to revenue for the year 2013-14 as per the provisions of AS 7 'Construction Contracts? Show the extract of the Profit & Loss Account in the e-books of M/s. Highway Constructions.

Question 8 : Five Star Construction Limited

Five Star Construction Limited commenced a construction contract on 1st April, 2014. The fixed contract price agreed was Rs.50,00,000. The company incurred Rs.21,00,000 in 2014-15 for 40% work and received Rs.19,00,000 as progress payment from the customer.

The company estimated that a further Rs 31,50,000 would be incurred to complete it. What amount should be charged to revenue for the year 2014-15 as per AS 7?
Show the extract of Profit & Loss A/c and Customer A/c for the year 2014-15 in the books of the company.

MCQs :

The below information relates to Questions 1 – 3:

XY Ltd. agrees to construct a building on behalf of its client GH Ltd. on 1st April 20X1. The expected completion time is 3 years. XY Ltd. incurred a cost of Rs. 30 lakh up to 31st March 20X2. It is expected that additional costs of Rs. 90 lakh. Total contract value is Rs. 112 lakh. As at 31st March 20X2, XY Ltd. has billed GH Ltd. For Rs. 42 lakh as per the agreement. Assume that the work is completed to the extent of 75% by the end of Year 2.

1. Revenue to be recognized by XY Ltd. for the year ended 31st March 20X2 is
   (a) Rs. 28 lakh (b) Rs. 42 lakh
   (c) Rs. 30 lakh (d) Rs. 32 lakh
2. Total expense to be recognised in Year 1 is
   (a) Rs. 30 lakh (b) Rs. 120 lakh
   (c) Rs. 38 lakh (d) Rs. 36 lakh
3. Revenue to be recognised for year 2 is
   (a) Rs. 84 lakh (b) Rs. 42 lakh
   (c) Rs. 56 lakh (d) Rs. 28 lakh

Below information relates to Questions 4 – 5

M/s AV has presented the information for Contract No. XY123:

Total contract value	Rs. 370 lakh
Certified work completed	Rs. 320 lakh
Costs incurred to date	Rs. 360 lakh
Progress Payments received	Rs. 300 lakh
Expected future costs to be incurred	Rs. 50 lakh

4. Revenue to be recognised by M/s AV is
   (a) Rs. 320 lakh (b) Rs. 370 lakh
   (c) Rs. 360 lakh (d) Rs. 400 lakh
5. Total expense to be recognised by M/s AV is
   (a) Rs. 360 lakh (b) Rs. 400 lakh
   (c) Rs. 320 lakh (d) Rs. 360 lakh
6. LP Contractors undertakes a fixed price contract of Rs. 200 lakh. Transactions related to the contract include:
   Material purchased: Rs. 80 lakh

Unused material: Rs. 30 lakh

Labour charges: Rs. 60 lakh

Machine used for 3 years for the contract. Original cost of the machine is Rs. 100 lakh. Expected useful life is 15 years.

Estimated future costs to be incurred to complete the contract: Rs. 80 lakh. Loss on contract to be recognised is:

(a)	Rs. 40 lakh	(b)	Rs. 10 lakh
(c)	Rs. 90 lakh	(d)	Rs. 50 lakh

Thanks ....

Chapter 10

AS 9 – REVENUE RECOGNITION

CHAPTER DESIGN

1. INTRODUCTION
2. WHAT IS REVENUE?
3. SCOPE
4. REVENUE FROM SALE OF GOODS
5. REVENUE FROM RENDERING OF THE SERVICES
6. REVENUE FROM INTEREST
7. REVENUE FROM ROYALTIES
8. REVENUE FROM DIVIDEND
9. DISCLOSURE

1. INRODUCTION :

AS 9 is mandatory for all enterprises.

AS 9 deals with the bases for recognition of revenue in the statement of profit and loss of an enterprise. The Standard is concerned with the recognition of revenue arising in the course of the ordinary activities of the enterprise from

- the sale of goods
- the rendering of services
- the use by others of enterprise resources yielding interest, royalties and dividends

2. WHAT IS REVENUE ? :

Revenue is the gross inflow of cash, receivables or other consideration arising in the course of the ordinary activities of an enterprise from the sale of goods, from the rendering of services, and from the use by others of enterprise resources yielding interest, royalties and dividends. Revenue is measured by the charges made to customers or clients for goods supplied and services rendered to them and by the charges and rewards arising from the use of resources by them. In an agency relationship, the revenue is the amount of commission and not the gross inflow of cash, receivables or other consideration.

In simple words revenue is charge made to customers or clients for goods supplied and services rendered to them.

3. SCOPE :

AS 9 does not deal with the following aspects of revenue recognition to which special considerations apply:

i. Revenue arising from construction contracts;
ii. Revenue arising from hire-purchase, lease agreements;
iii. Revenue arising from government grants and other similar subsidies;
iv. Revenue of insurance companies arising from insurance contracts.

Examples of items not included within the definition of “revenue” for the purpose of AS 9 are:

i. Realised gains resulting from the disposal of, and unrealised gains resulting from the holding of, non-current assets e.g. appreciation in the value of fixed assets;
ii. Unrealised holding gains resulting from the change in value of current assets, and the natural increases in herds and agricultural and forest products;
iii. Realised or unrealised gains resulting from changes in foreign exchange rates and adjustments arising on the translation of foreign currency financial statements;

iv. Realised gains resulting from the discharge of an obligation at less than its carrying amount;

v. Unrealised gains resulting from the restatement of the carrying amount of an obligation.

4. REVENUE FROM SALE OF GOODS :

Revenue from sales or service transactions should be recognised when the requirements as to performance set out in below paragraph are satisfied, provided that at the time of performance it is not unreasonable to expect ultimate collection. If at the time of raising of any claim it is unreasonable to expect ultimate collection, revenue recognition should be postponed.

In a transaction involving the sale of goods, performance should be regarded as being achieved when the following conditions have been 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

(ii) the seller retains no effective control of the goods transferred to a degree usually associated with ownership; and

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

Revenue recognition when delivery of goods sold are subject to conditions

1. Installation and Inspection : Revenue should be recognised when :

- Goods are installed at the buyers place to his satisfaction
- Goods are inspected and accepted by the buyer

2. Sale on Approval :

Revenue should be recognised when buyer confirms his desire to buy such goods by communication

3. Guaranteed sales :

Revenue should be recognised as per the substance of the agreement of sale or after the reasonable period has expired.

4. Warranty sales :

Sales should be recognised immediately but the provision should be made to cover unexpired warranty.

5. Consignment sales :

Revenue should be recognised only when the goods are sold to the third party.

6. **Special order and shipments :**

Revenue from such sales should be recognised when the goods are identified and ready for delivery.

7. **Subscription for publication :**

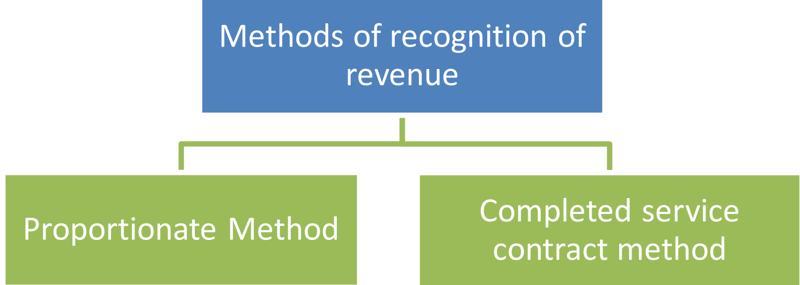
- Items delivered vary in value from period to period: Revenue should be recognised on the basis of sales value of items delivered.
- Items delivered do not vary in value from period to period: Revenue should be recognised on straight line basis over time.

8. **Instalment sales :**

Revenue of sale price excluding interest should be recognised on the date of sale. Interest should be recognised proportionately to unpaid balance.

5. REVENUE FROM RENDERING OF SERVICES :

Revenue from service transactions is usually recognised as the service is performed. There are two methods of recognition of revenue from service transaction, viz,



Proportionate Completion Method is a method of accounting which recognises revenue in the statement of profit and loss proportionately with the degree of completion of services under a contract. Here performance consists of the execution of more than one act. Revenue is recognised proportionately by reference to the performance of each act.

Completed Service Contract Method is a method of accounting which recognises revenue in the statement of profit and loss only when the rendering of services under a contract is completed or substantially completed. In this method performance consists of the execution of a single act.

Revenue recognition norms for rendering of service under special conditions

1. **Installation fees :**

It is recognised when the installation has been completed and accepted by the clients.

2. **Advertising and Insurance Agency Commission :**
   - Advertising commission is recognised when the advertisement appears before public
   - Insurance commission is recognised on the effective commencement / renewal date of the policies.

3. **Financial service commission :**
   Recognition of revenue depends upon
   - whether the service has been provided "once and for all" or is it on continuing basis.
   - The incidence of costs relating to the service
   - When the payment for the service will be received

   Generally, commission charged for arranging or granting loan and other facilities should be recognised when a loan is sanctioned and accepted by borrower.

4. **Admission fees :**
   Revenue from artistic performance, banquets and other special events should be recognised when the event takes place.

5. **Tuition fees :**
   Revenue should be recognised over the period of instruction

6. **Entrance and Membership fees :**
   Recognition depends upon the nature of service being provided against entrance and membership fees, however entrance fees are generally capitalised and membership fees should recognised on systematic and rational basis having regards to timings and nature of service provided.

6. REVENUE FROM INTEREST :

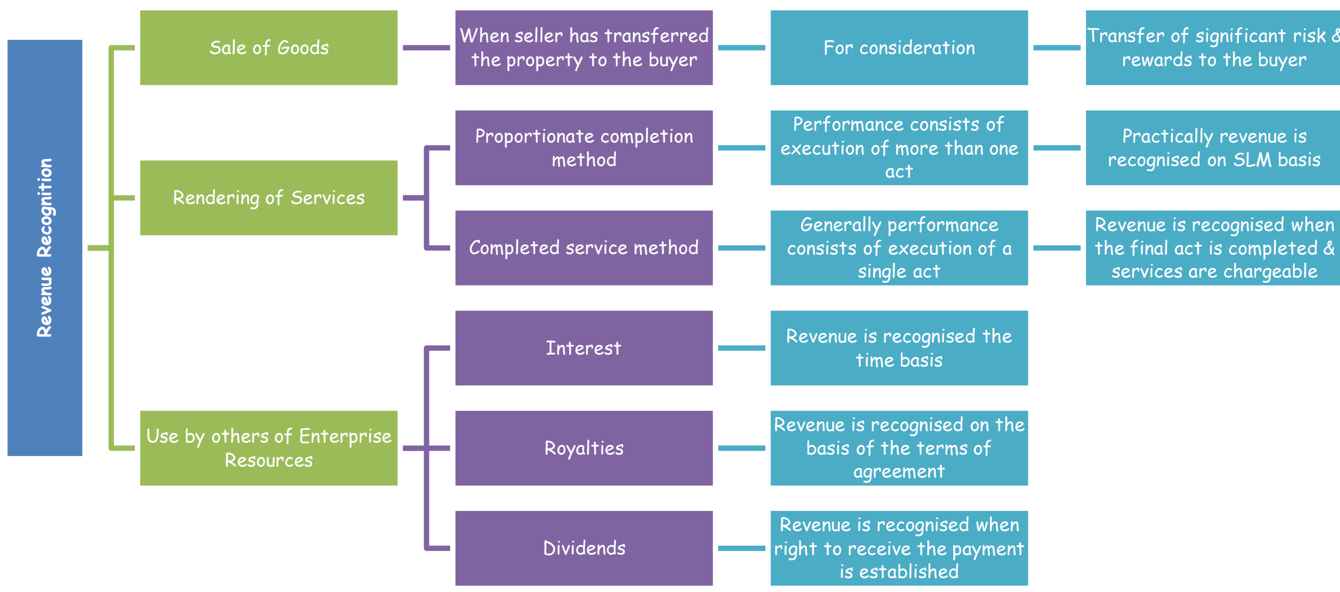
Interest : charges for the use of cash resources or amounts due to the enterprise. Revenue is recognised on a time proportion basis taking into account the amount outstanding and the rate applicable.

7. REVENUE FROM ROYALTIES :

Royalties : charges for the use of such assets as know-how, patents, trade marks and copyrights. Revenue is recognised on an accrual basis in accordance with the terms of the relevant agreement.

8. REVENUE FROM DIVIDENDS :

Dividends : rewards from the holding of investments in shares. Revenue is recognised when the owner's right to receive payment is established.



9. DISCLOSURE :

An enterprise should disclose the circumstances in which revenue recognition has been postponed pending the resolution of significant uncertainties.

PRACTICAL QUESTIONS :

Question 1:

The Board of Directors decided on 31.3.2017 to increase the sale price of certain items retrospectively from 1st January, 2017. In view of this price revision with effect from 1st January 2017, the company has to receive Rs 15 lakhs from its customers in respect of sales made from 1st January, 2017 to 31st March, 2017. Accountant cannot make up his mind whether to include Rs 15 lakhs in the sales for 2016-2017.Advise.

Question 2 : Y Ltd.

Y Ltd., used certain resources of X Ltd. In return X Ltd. received Rs 10 lakhs and Rs 15 lakhs as interest and royalties respective from Y Ltd. during the year 2016-17. You are required to state whether and on what basis these revenues can be recognised by X Ltd.

Question 3 :

A claim lodged with the Railways in March, 2015 for loss of goods of Rs 2,00,000 had been passed for payment in March, 2017 for Rs 1,50,000. No entry was passed in the books of the Company, when the claim was lodged. Advise P Co. Ltd. about the treatment of the following in the Final Statement of Accounts for the year ended 31st March, 2017.

Question 4 : Perfect Ltd.

Perfect Ltd. Manufactures machinery used in Power Plants. In response to the tenders issued by Power Plants, Perfect Ltd. Quotes its price. As per terms of contract, full price of machinery is not released by the power plants, but 10% thereof is retained and paid after one year if there is satisfactory performance of the machinery supplied. From the past experience, it is observed that Perfect Ltd. Accounts for only 90% of the invoice value as sales revenue and block the balance amount in the year of receipt to the extent of actual receipts only. Comment on the treatment done by the company.

Question 5 : Sahara Ltd.

Sahara Ltd. is in regular business with Railways and dealings with them are shown in its financial statements as ordinary activities of the business. A claim was lodged by it, with the Railways in March, 2010 for loss of goods of Rs 2,00,000. The claim had been passed for payment in March, 2013 for Rs. 1,50,000. No entry was passed in the books of the company, when the claim was lodged. Advise Sahara Ltd. about the treatment of the above in the final statement of accounts for the year ended on 31st March, 2013.

Question 6 : A Ltd.

A Ltd. Entered into a contract with B Ltd. To dispatch goods valuing Rs. 25,000 every month for 4 months upon receipt of entire payment. B Ltd accordingly made the payment of Rs. 1,00,000 and A Ltd. Requested A Ltd. Not to dispatch goods until further notice through A Ltd. Is holding the remaining goods worth Rs. 50,000 ready for dispatch. A Ltd. Accounted Rs. 50,000 as sales and transferred the balance to Advance Received against sales. Comment upon the treatment of balance amount with reference to the provisions of Accounting Standard 9

Question 7 :

A Company sells the goods with right to return. The following pattern has been observed Time frame of Return from date of purchase % Of Cumulative Sales Within 10 days 5% Between 11 days and 20 days 7% Between 21 days and 30 days 8% Between 31 days and 45 days 9% The company has made sales of Rs. 30 lakhs in the moth of February 2015 and of Rs. 36 lakhs in the month of March 2015. The total sales for the Financial year have been

Rs. 450 lakhs and the cost of sales was Rs. 360 lakhs. Determine the amount of provision to be made and Revenue to be recognized in accordance with AS-9. A year may be considered of 360 days.

Question 8 : Victory Ltd.

Victory Ltd. purchased goods on credit from Lucky Ltd. for Rs 250 crores for export. The export order was cancelled. Victory Limited decided to sell the same goods in the local market with a price discount. Lucky Limited was requested to offer a price discount of 15%. The chief Accountant of Lucky Ltd. wants to adjust the sales figure to the extent of the discount requested by Victory Ltd. Discuss whether this treatment is justified.

Question 9 : New Spice Ltd.

New Spice Ltd. sells male groaning products to various dealers situated in different states in India. It allows normal credit period of 45 days to its dealers to mace payment. Interest at the rate of 2% per month is charged on the dealers for delayed payments. The interest recovery on such overdue outstanding amounts from dealers is only 10%, due to various reasons. During the year 2014-15, the company vents to recognize only the interest received and not the balance 90% of interest receivable on overdue outstanding. Do you agree?

MCQs :

1. Which of the conditions mentioned below must be met to recognize revenue from the sale of goods?
   (i) the entity selling does not retain any continuing influence or control over the goods;
   (ii) when the goods are dispatched to the buyer;
   (iii) revenue can be measured reliably;
   (iv) the supplier is paid for the goods;
   (v) it is reasonably certain that the buyer will pay for the goods;
   (vi) the buyer has paid for the goods.
   (a) (i), (ii) and (v) (b) (ii), (iii) and (iv)
   (c) (i), (iii) and (v) (d) (i), (iv) and (v)
2. Consignment inventory is an arrangement whereby inventory is held by one party but owned by another party. Which of the following indicates that the inventory in question is a consignment inventory?
   (a) Manufacturer cannot require the dealer to return the inventory
   (b) Dealer has the right to return the inventory
   (c) Manufacture is responsible for the pricing of goods and any changes in the pricing can only be approved by the manufacturer .

(d) Manufacture is responsible for the holding the goods and any changes in the pricing can only be approved by the dealer

3. Which of the following transactions qualify as revenue for M/s AB Enterprises?

(a) Sales of Rs. 20 lakhs made under consignment sales.

(b) Sale of an old machine amounting Rs. 5 lakhs

(c) Services provided to the customer in the normal course of business. Sales recorded is Rs. 50,000.

(d) Sales of Rs. 25 lakhs made under consignment sales

4. The Accounting Club has 100 members who are required to pay an annual membership fee of Rs. 5,000 each. During the current year, all members have paid the fee. However, 5 members have paid an amount of Rs. 10,000 each. Of these, 3 members paid the current year's fee and also the previous year's dues. Remaining 2 members have paid next years' fee of Rs. 5,000 in advance.

Revenue from membership fee for the current year to be recognised will be:

(a) Rs. 5,25,000 (b) Rs. 5,10,000

(c) Rs. 5,00,000 (d) Rs. 5,15,000

5. Flix Net International offers a subscription fee model to allow the paid subscribers an annual viewing of movies, sports events and other content. It allows users to register for free and have access to limited content for one month without any charges. The customer has a right to cancel the subscription within a month's time but is required to pay for 1 year subscription fee after the free period.

XY has subscribed for free viewing on 1st March 20X1. After 1 month, he has agreed to pay the annual membership and has paid Rs. 1,200 on 31st March 20X1 for the subscription that is valid up to 31st of March 20X2.

Revenue that can be recognized by Flix Net for the year ended 31st March 20X2 is

(a) Rs. 100 (b) Rs. 1,200

(c) Nil (d) Rs. 1,100

Thanks ....

Rahul Malkan

Chapter 11

AS 10 – PROPERTY, PLANT AND EQUIPMENT

CHAPTER DESIGN

1. INTRODUCTION
2. SCOPE
3. DEFINITIONS
4. RECOGNITION
5. MEASUREMENT
   (A) INITIAL MEASUREMENT
   (B) SUBSEQUENT MEASUREMENT
6. DEPRECIATION
7. DERECOGNITION
8. DISCLOSURE

1. INTRODUCTION :

The objective of this Standard is to prescribe accounting treatment for Property, Plant and Equipment (PPE).

The principal issues in Accounting for PPE are

1. Recognition
2. Measurement
3. Depreciation
4. Derecognition

2. SCOPE :

As a general principle, AS 10 (Revised) should be applied in accounting for PPE.

Exception:

When another Accounting Standard requires or permits a different accounting treatment.

Example:

AS 191 on Leases, requires an enterprise to evaluate its recognition of an item of leased PPE on the basis of the transfer of risks and rewards. However, it may be noted that in such cases other aspects of the accounting treatment for these assets, including depreciation, are prescribed by this Standard.

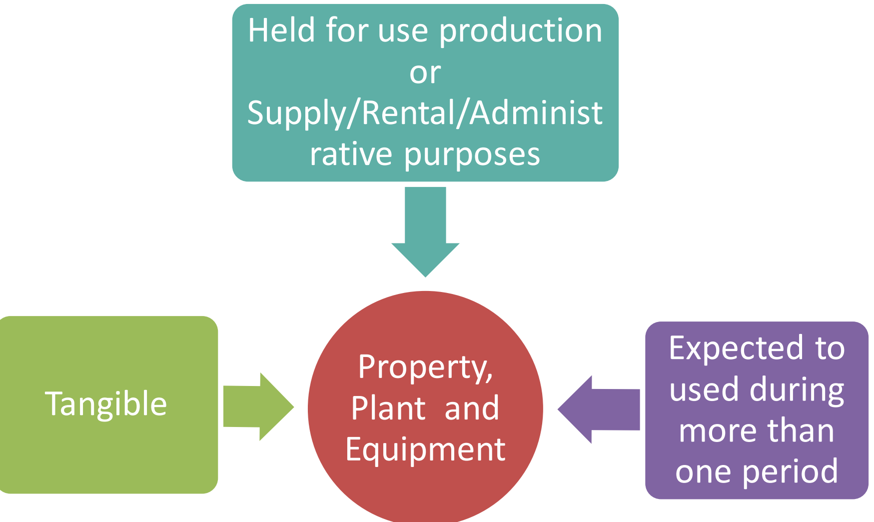
This Standard does not apply to:

1. Biological Assets (other than Bearer Plants) related to agricultural activity
2. Wasting Assets including Mineral rights, Expenditure on the exploration for and extraction of minerals, oil, natural gas and similar non-regenerative resources

Note : AS 10 (Revised) applies to Bearer Plants but it does not apply to the produce on Bearer Plants.

3. DEFINITIONS :

1. **Property, Plant and Equipment:**
   (a) are the tangible items that
   (b) are held for use in the production or supply of goods or services, for rental to others, or for administrative purposes; and
   (c) are expected to be used during more than one period



2. **Biological Asset :** Biological Asset is a living animal or plant.

E.g. Cattle, vines, trees, sheep and other plants.

An Accounting Standard on "Agriculture" is under formulation, which will, inter alia, cover accounting for livestock. Till the time, the AS on "Agriculture" is issued, accounting for livestock meeting the definition of PPE, will be covered as per AS 10 (Revised)

3. **Bearer Plant is a living plant that:**
   (a) is used in the production or supply of agricultural produce;
   (b) is expected to bear produce for more than one period; and
   (c) has a remote likelihood of being sold as agricultural produce, except for incidental scrap sales.

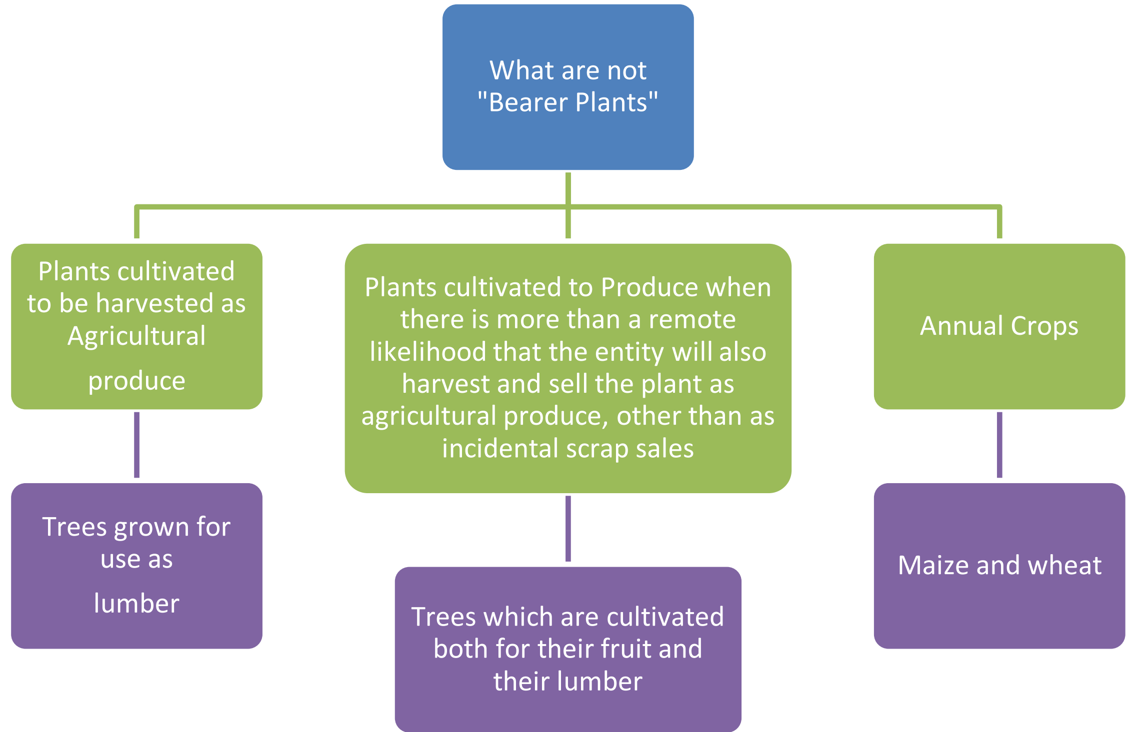
E.g. Plants such as tea bushes, grape vines, oil palms and rubber trees.

Note: AS 10 (Revised) applies to Bearer Plants but doesn't apply to the produce on Bearer Plants. The following are not Bearer Plants:

a) Plants cultivated to be harvested as Agricultural produce. E.g.: Trees grown for use as lumber.

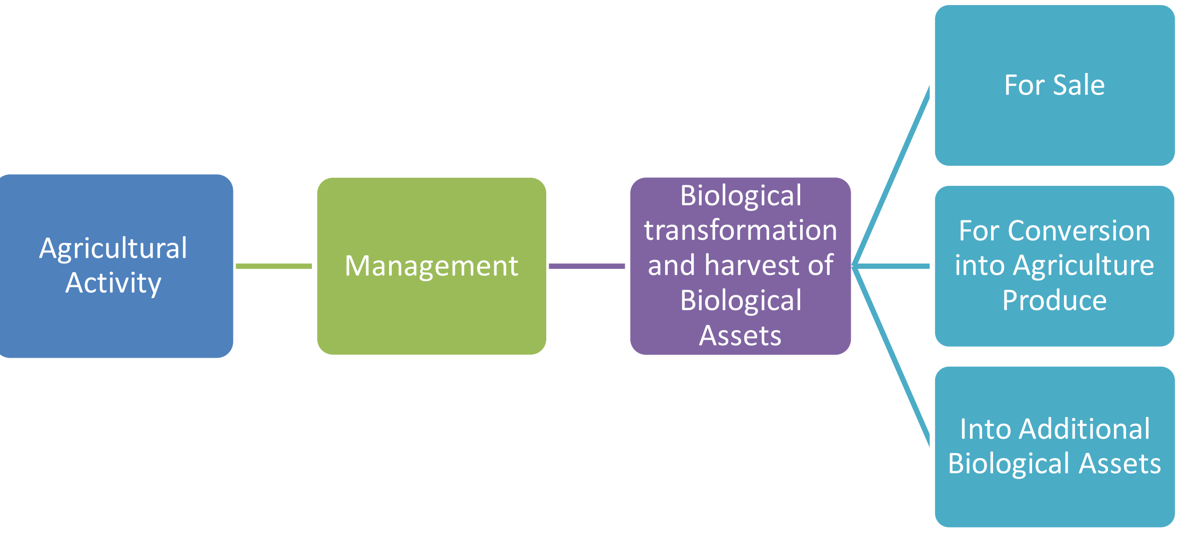
b) Plants cultivated to produce Agricultural produce when there is more than a remote likelihood that the entity will also harvest and sell the plant as agricultural produce, other than as incidental scrap sales. E.g.: Trees cultivated both for their fruit and their lumber.

c) Annual crops E.g.: Maize and wheat



4. **Agricultural Produce:** Agricultural Produce is the harvested product of Biological Assets of the enterprise.

5. **Agricultural Activity :**
   Is the management by an Enterprise of:
   - Biological transformation; and
   - Harvest of Biological Assets
     - For sale, Or
     - For conversion into Agricultural Produce, Or
     - Into additional Biological Assets



6. **Carrying amount** is the amount at which an asset is recognised after deducting any accumulated depreciation and accumulated impairment losses.

7. **Depreciable amount** is the cost of an asset, or other amount substituted for cost, less its residual value.

8. **Depreciation** is the systematic allocation of the depreciable amount of an asset over its useful life.

4. RECOGNITION :

The cost of an item of property, plant and equipment shall be recognised as an asset if, and only if:

A. it is probable that future economic benefits associated with the item will flow to the entity; and

B. the cost of the item can be measured reliably.

it is probable that future economic benefit associated with the item will flow to the entity → the cost of the item can be measured reliably.

When do we apply the above criteria for Recognition?

1. Spare Parts, Stand by Equipment and Servicing Equipment

Case I

If they meet the definition of PPE as per AS 10 (Revised):

- Recognised as PPE as per AS 10 (Revised)

Case II :

If they do not meet the definition of PPE as per AS 10 (Revised):

- Such items are classified as Inventory as per AS 2 (Revised)

2. Cost of day-to-day servicing

An enterprise does not recognise in the carrying amount of an item of PPE the costs of the day-to-day servicing of the item. Rather, these costs are recognised in the Statement of Profit and Loss as incurred.

3. Replacement of Parts of PPE :

An enterprise recognises in the carrying amount of an item of PPE the cost of replacing part of such an item when that cost is incurred if the recognition criteria are met. Note : The carrying amount of those parts that are replaced is derecognised in accordance with the de-recognition provisions of this Standard.

4. Regular Major Inspections :

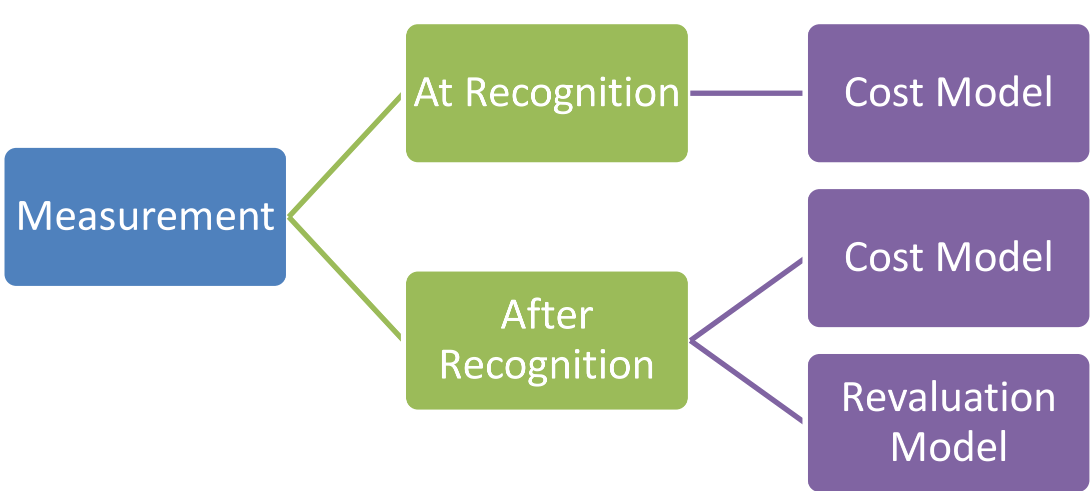
When each major inspection is performed, its cost is recognised in the carrying amount of the item of PPE as a replacement, if the recognition criteria are satisfied.

Any remaining carrying amount of the cost of the previous inspection (as distinct from physical parts) is derecognised.

Question 1 : RM

RM acquired an aircraft for Rs.1.5 crore on 1.4.2018. It has a life of 15 years. RM is required to get the aircraft inspected every 3 years to check its travel worthiness. On 1.4.2018, it carried out inspection at a cost of Rs.60,00,000. On 1.4.2021, its incurred Rs.75,00,000 as the cost of new inspection. Show treatment

5. MEASUREMENT :



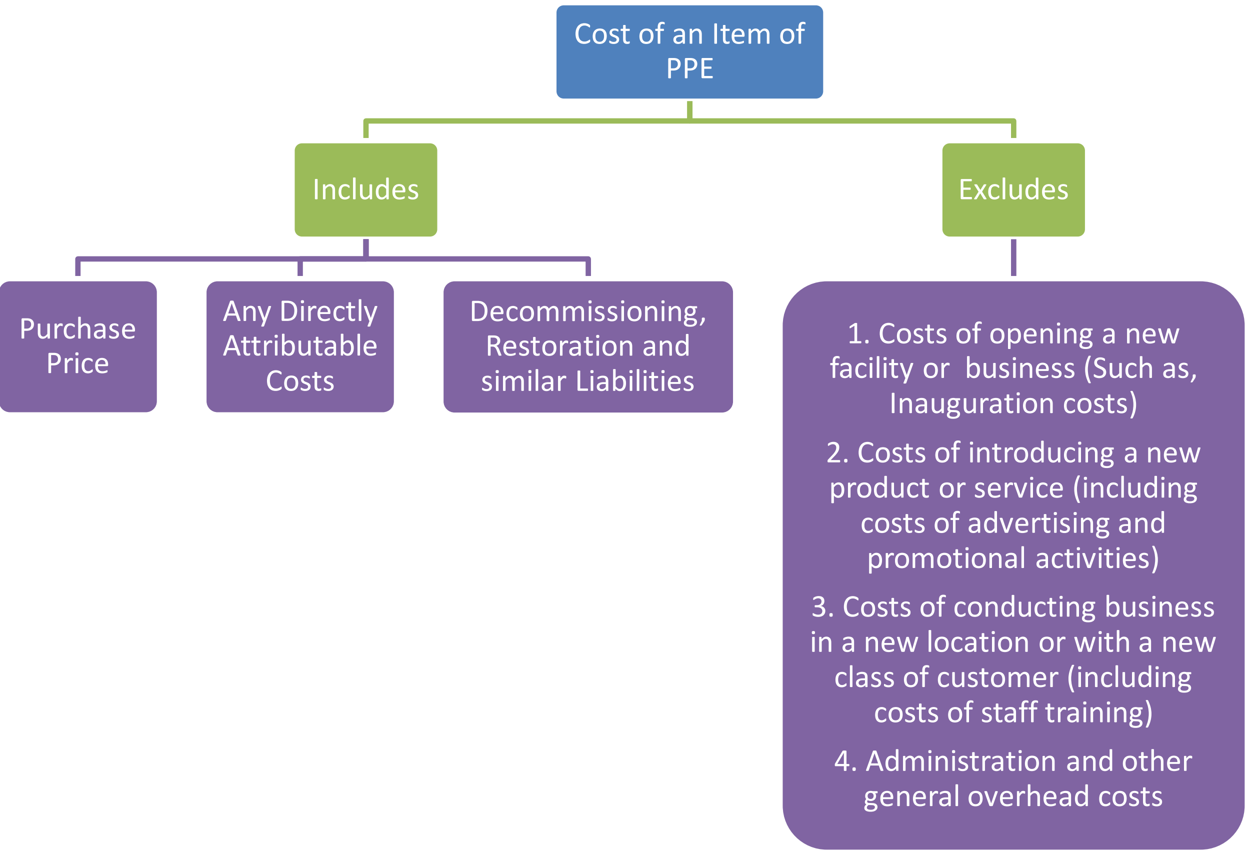
5.1 Initial Measurement :

An item of property, plant and equipment that qualifies for recognition as an asset should be initially measured at its cost.

COMPONENT OF COST :

The cost of an item of property, plant and equipment comprises:

- its purchase price, including import duties and non-refundable purchase taxes, after deducting trade discounts and rebates;
- any costs directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management; and
- the initial estimate of the costs of dismantling and removing the item and restoring the site on which it is located, the obligation for which an entity incurs either when the item is acquired or as a consequence of having used the item during a particular period for purposes other than to produce inventories during that period



Question 2 :

The purchase price of the machine is Rs.1,10,000. Other cost are as follows: Freight Rs.2000, Import duty Rs.5000. Installation Expenses Rs.1000. This are all initial cost. What will be the cost of the machinery?

Question 3 :

The purchase price of the machinery is Rs.110,000. The basic price is 1,00,000 + 10,000 Vat. The entity get the credit of VAT paid on the machinery, while calculating the tax payable on the finished goods sold. What will be the cost of machinery?

Question 4 :

An entity constructs a building for its own use. It spends Rs.50 million for material (Rs.2 million of it was lost in a fire) and Rs.5 million on wages and other direct expenses for constructing the building, it uses borrowed cost of Rs.30 million on which it pays interest of Rs.3 million upto the date of completion of construction. What is the amount to be recognised as cost construction.

Question 5 : RM Ltd

RM Ltd purchased a plant for Rs.200 million. The seller granted rebate of 0.5%. The gross price includes GST Rs.18 million for which the buyer will get tax refund. It has also incurred Rs.15 million for transport, Rs.5 million for installation and Rs.3 million for testing and professional fees. It has earned Rs.0.2 million from selling goods produced out of testing. The company borrowed Rs.100 million for financing new plant at 10%. The entire process of purchase to make it operational took 15 months. The company earned Rs.0.1 million from short term parking of money borrowed pending payment to supplier and meeting all costs. What should be initial cost of the plant ?

Question 6 : SK Ltd

SK Ltd set up fire safety devices around its factory premises. The price paid for devices is Rs.1,10, 000 (Including tax of Rs.10,000). The entity gets credit on VAT. Additional cost are Freight Rs.2000, Import Duty Rs.5000 (No refund), installation expense of Rs.1000. The initial expense of dismantling and removing was Rs.3000. After the machinery was put to use Rs.1500 was spent for maintenance. Calculate the initial cost of the asset.

Question 7 : RM mining Ltd.

RM mining Ltd. has projected site restoration expenses of Rs.1,57,04,710 after 40 years. The rate of Discount is 11%. Pass journal entry at initial recognition

Question 8 : Entity A

Entity A has an existing freehold factory property, which it intends to knock down and redevelop. During the redevelopment period the company will move its production facilities to another (temporary) site. The following incremental costs will be incurred:

1. Setup costs of Rs 5,00,000 to install machinery in the new location.
2. Rent of Rs 15,00,000
3. Removal costs of Rs 3,00,000 to transport the machinery from the old location to the temporary location. Can these costs be capitalised into the cost of the new building?

Question 9 : Entity A

Entity A, which operates a major chain of supermarkets, has acquired a new store location. The new location requires significant renovation expenditure. Management expects that the renovations will last for 3 months during which the supermarket will be closed. Management has prepared the budget for this period including expenditure related to construction and remodelling costs, salaries of staff who will be preparing the store before its opening and related utilities costs. What will be the treatment of such expenditures?

Question 10 : An amusement park

An amusement park has a 'soft' opening to the public, to trial run its attractions. Tickets are sold at a 50% discount during this period and the operating capacity is 80%. The official opening day of the amusement park is three months later. Management claim that the soft opening is a trial run necessary for the amusement park to be in the condition capable of operating in the intended manner. Accordingly, the net operating costs incurred should be capitalised. Comment.

Deferred payment beyond normal credit terms :

The cost of an item of property, plant and equipment is the cash price equivalent at the recognition date. If payment is deferred beyond normal credit terms, the difference between the cash price equivalent and the total payment is recognised as interest over the period of credit unless such interest is capitalised in accordance with Ind AS 23.

Question 11 :

The purchase price of the machinery is Rs.40,000. The company did not have enough cash, and therefore agreed to pay a year later. However they will pay Rs.45,000. What shall be the treated with reference to the above arrangement.

Question 12 :

On 1st April, 2011, an item of property is offered for sale at Rs.10 million, with payment terms being three equal instalments of Rs.33,33,333 over a two years period (payments are made on 1st April, 2011, 31st March, 2012 and 31st March, 2013). The property developer is offering a discount of 5 percent (i.e. Rs.0.5 million) if payment is made in full at the time of completion of sale. Implicit interest rate of 5.36 percent p.a. Show how the property will be recorded in accordance of Ind AS 16.

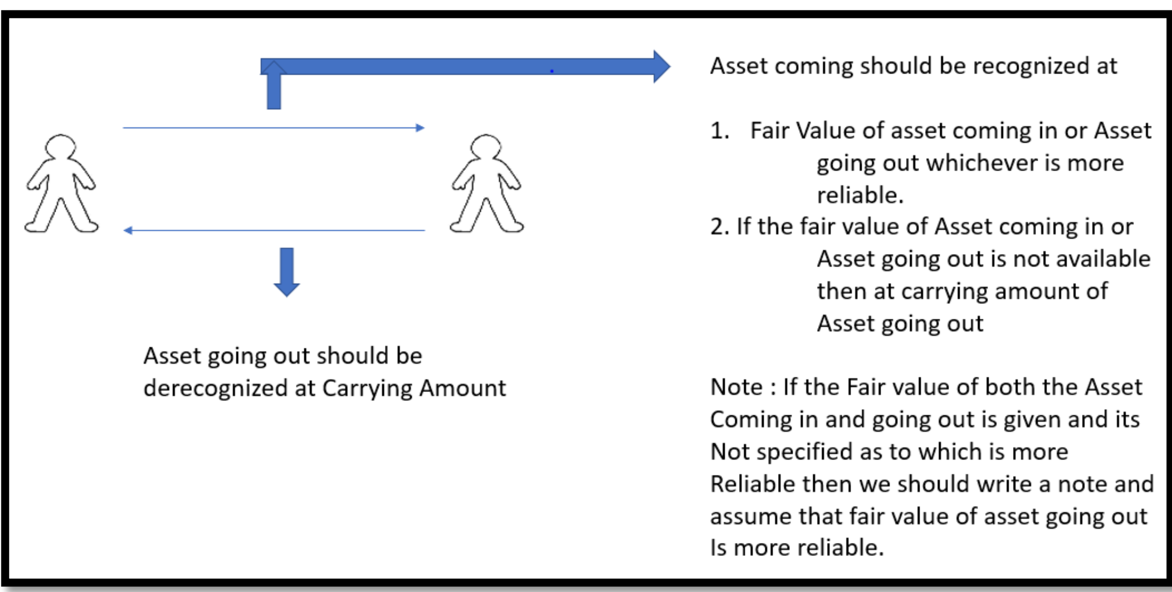
Exchange of Assets :

A. One or more items of property, plant and equipment may be acquired in exchange for a nonmonetary asset or assets, or a combination of monetary and nonmonetary assets. The cost of such an item of property, plant and equipment is measured at fair value (even if an entity cannot immediately derecognise the asset given up) unless:

1. the exchange transaction lacks commercial substance; or
2. the fair value of neither the asset received nor the asset given up is reliably measurable

B. If the acquired item is not measured at fair value, its cost is measured at the carrying amount of the asset given up.

C. If an entity is able to measure reliably the fair value of either the asset received or the asset given up, then the fair value of the asset given up is used to measure the cost of the asset received unless the fair value of the asset received is more clearly evident.



Question 13 : Entity A

Entity A exchanges surplus land with a book value of Rs 10,00,000 for cash of Rs 20,00,000 and plant and machinery valued at Rs 25,00,000. What will be the measurement cost of the assets received?

Question 14 : DM Ltd.

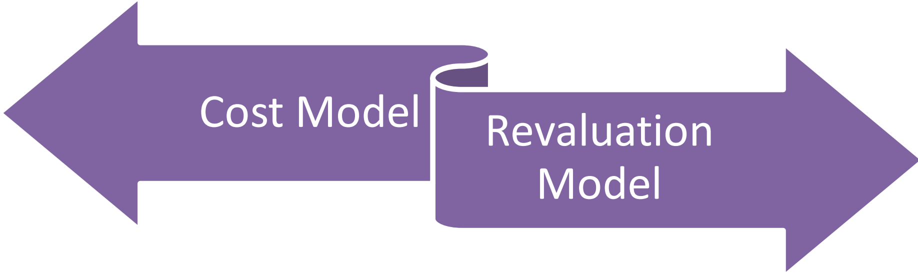
DM Ltd. purchases a Machinery in exchange of Motor Car B. Motor car B has a book Value of Rs.1,50,000. Fair Value of car given up is Rs.1,70,000. Fair value of Machine is Rs.1,80,000. Fair value of Machinery is more evidently known. Journalise.

Question 15 : Entity A

Entity A exchanges car X with a book value of Rs 13,00,000 and a fair value of Rs 13,25,000 for cash of Rs 15,000 and car Y which has a fair value of Rs 13,10,000. The transaction lacks commercial substance as the company's cash flows are not expected to change as a result of the exchange. It is in the same position as it was before the transaction. What will be the measurement cost of the assets received?

5.2 Subsequent Measurement :

An entity may choose either the cost model or the revaluation model as its accounting policy and should apply that policy to an entire class of property, plant and equipment.



Question 16 : Entity A

Entity A is a large manufacturing group. It owns a number of industrial buildings, such as factories and warehouses and office buildings in several capital cities. The industrial buildings are located in industrial zones, whereas the office buildings are in central business districts of the cities. Entity A's management want to apply the revaluation model as per AS 10 (Revised) to the subsequent measurement of the office buildings but continue to apply the historical cost model to the industrial buildings.

State whether this is acceptable under AS 10 (Revised) or not with reasons?

Question 17 : Jupiter Ltd.

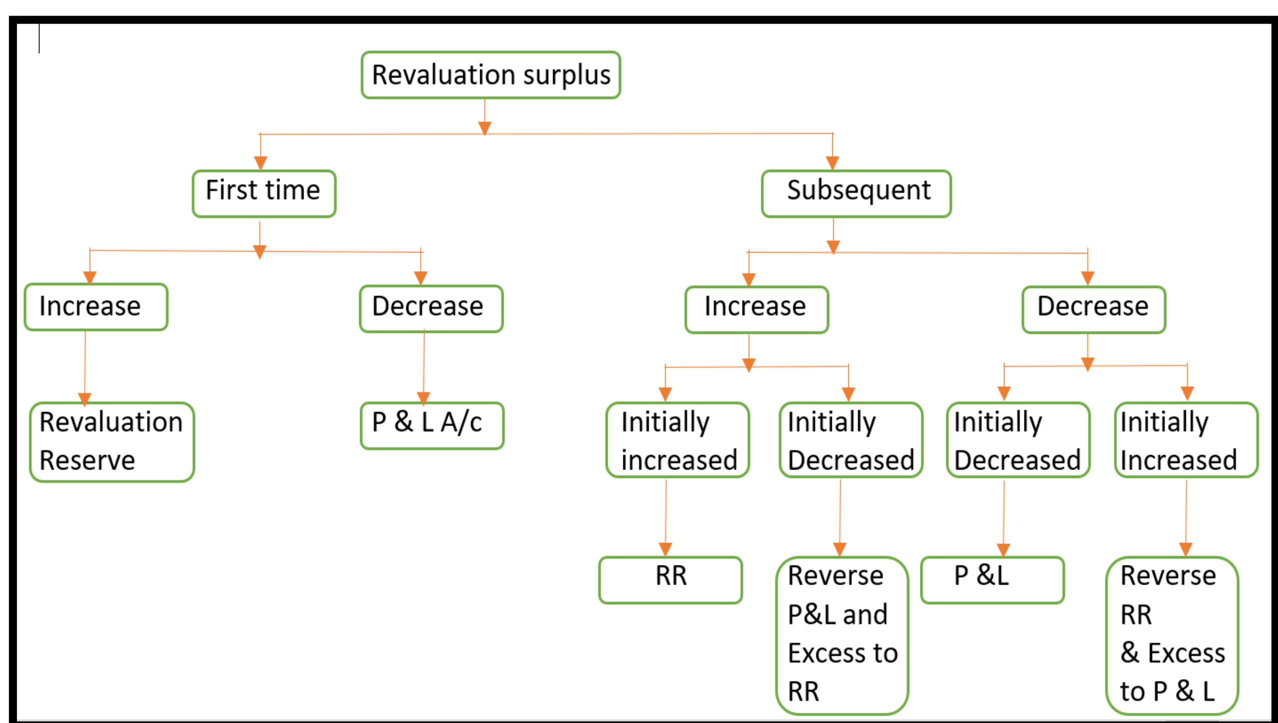
Jupiter Ltd. has an item of plant with an initial cost of Rs.100,000. At the date of revaluation accumulated depreciation amounted to Rs.55,000. The fair value of asset, by reference to transactions in similar assets, is assessed to be Rs.65,000. Find out the entries to be passed?

Frequency of revaluation

Revaluations should be made with sufficient regularity to ensure that the carrying amount does not differ materially from that which would be determined using Fair value at the Balance Sheet date.

The frequency of revaluations depends upon the changes in fair values of the items of PPE being revalued.

Revaluation – Increase or Decrease



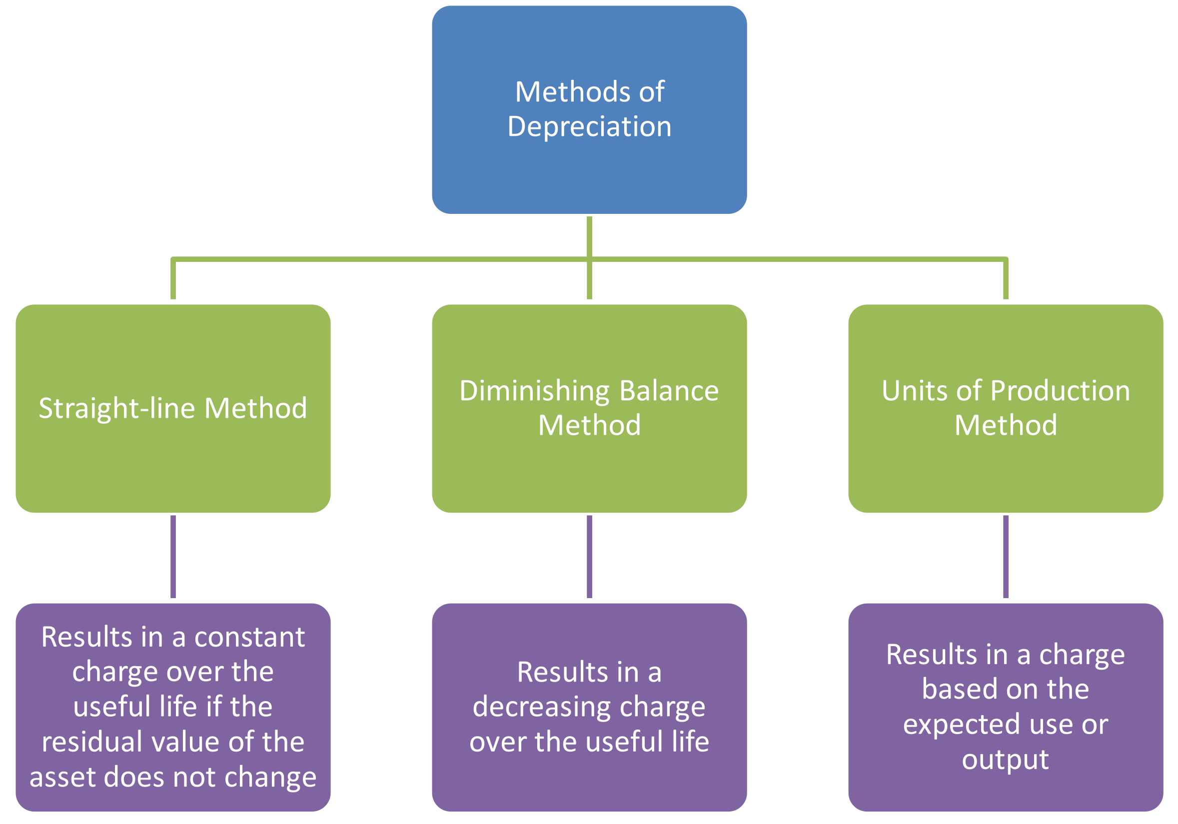
Question 18 :

An item of PPE was purchased for Rs.9,00,000 on 1st April, 2011. It is estimated to have a useful life of 10 years and is depreciated on a straight line basis. On 1st April, 2013, the asset is revalued to Rs.9,60,000. The useful life remains unchanged as ten years. Ignore impact of deferred taxes. Show the necessary treatment as per Ind AS 16.

6. DEPRECIATION :

The depreciation method used should reflect the pattern in which the future economic benefits of the asset are expected to be consumed by the enterprise. The method selected is applied consistently from period to period unless:

- There is a change in the expected pattern of consumption of those future economic benefits; Or
- That the method is changed in accordance with the statute to best reflect the way the asset is consumed.



Review of Depreciation Method:

The depreciation method applied to an asset should be reviewed at least at each financial year-end and, if there has been a significant change in the expected pattern of consumption of the future economic benefits embodied in the asset, the method should be changed to reflect the changed pattern.

Such a change should be accounted for as a change in an accounting estimate in accordance with AS 5.

Question 19 : Entity B

Entity B manufactures industrial chemicals and uses blending machines in the production process. The output of the blending machines is consistent from year to year and they can be used for different products. However, maintenance costs increase from year to year and a new generation of machines with significant improvements over existing machines is available every 5 years. Suggest the depreciation method to the management.

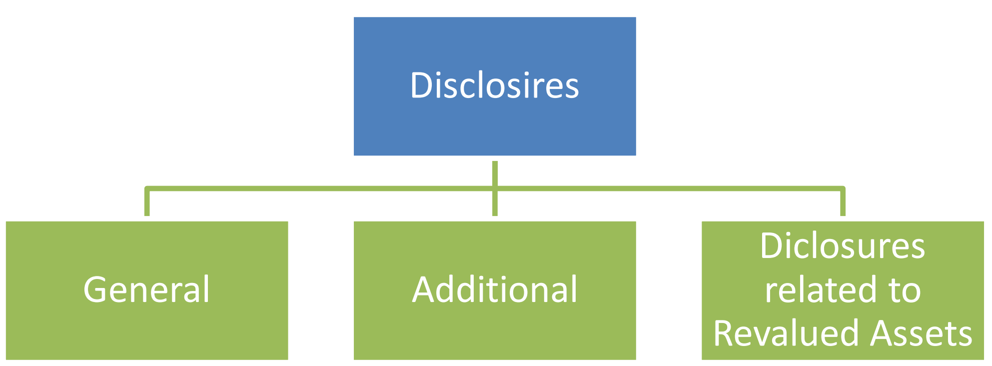
7. DERECOGNITION :

The carrying amount of an item of PPE should be derecognised:

- On disposal
  - By sale

- o By entering into a finance lease, or
- o By donation, Or
- When no future economic benefits are expected from its use or disposal

8. DISCLOSURE :



MCQs :

1. As per AS 10 (Revised) 'Property, plant and equipment', which of the following costs is not included in the carrying amount of an item of PPE
   (a) Costs of site preparation
   (b) Costs of relocating
   (c) Installation and assembly costs.
   (d) initial delivery and handling costs
2. As per AS 10 (Revised) 'Property, Plant and Equipment', an enterprise holding investment properties should value Investment property
   (a) as per fair value
   (b) under discounted cash flow model.
   (c) under cost model
   (d) under cash flow model
3. A plot of land with carrying amount of Rs. 1,00,000 was revalued to Rs. 1,50,000 at the end of Year 2. Subsequently, due to drop in market values, the land was determined to have a fair value of Rs. 1,30,000 at the end of Year 4. Assuming that the entity adopts Revaluation Model, what would be the accounting treatment of Revaluation?
   (a) Initial upward valuation of Rs. 50,000 credited to Revaluation Reserve. Subsequent downward revaluation of Rs. 20,000 debited to P/L.
   (b) Initial upward valuation of Rs. 50,000 credited to P/L. Subsequent downward revaluation of Rs. 20,000 debited to P/L.
   (c) Initial upward valuation of Rs. 50,000 credited to Revaluation Reserve. Subsequent downward revaluation of Rs. 20,000 debited to Revaluation Reserve.

(d) Initial upward valuation of Rs. 50,000 debited to P/L. Subsequent downward revaluation of Rs. 20,000 credited to P/L.

4. A plot of land with carrying amount of Rs. 1,00,000 was revalued to Rs. 90,000 at the end of Year 2. Subsequently, due to increase in market values, the land was determined to have a fair value of Rs. 1,05,000 at the end of Year 4. Assuming that the entity adopts Revaluation Model, what would be the accounting treatment of Revaluation?
   (a) Initial downward valuation of Rs. 10,000 debited to Revaluation Reserve. Subsequent upward revaluation of Rs. 15,000 credited to P/L.
   (b) Initial downward valuation of Rs. 10,000 debited to P/L. Subsequent upward revaluation of Rs. 15,000 credited to P/L.
   (c) Initial downward valuation of Rs. 10,000 debited to P/L. Subsequent upward revaluation of Rs. 10,000 credited to P/L and Rs. 5,000 credited to Revaluation Reserve.
   (d) Initial downward valuation of Rs. 10,000 credited to P/L. Subsequent upward revaluation of Rs. 10,000 debited to P/L and Rs. 5,000 debited to Revaluation Reserve.

5. On sale of an asset which was revalued upwards, what would be the treatment of Revaluation Reserve?
   (a) The Revaluation Reserve is credited to P/L since the profit on sale of such asset is now realized.
   (b) The Revaluation Reserve is credited to Retained Earnings as a movement in reserves without impacting the P/L.
   (c) No change in Revaluation Reserve since profit on sale of such asset is already impacting the P/L.
   (d) The Revaluation Reserve is reduced from the asset value to compute profit or loss.

6. A machinery was purchased having an invoice price Rs. 1,18,000 (including GST Rs. 18,000) on 1 April 20X1. The GST amount is available as input tax credit. The rate of depreciation is 10% on SLM basis. The depreciation for 20X2-X3 would be
   (a) Rs. 10,000. (b) Rs. 11,800.
   (c) Rs. 9,000. (d) Rs. 10,500.

Thanks ....

Rahul Malkan

Chapter 12

AS 11 – THE EFFECTS OF CHANGES IN FOREIGN EXCHANGE RATES

CHAPTER DESIGN

1. INTRODUCTION
2. SCOPE
3. DEFINITIONS
4. ACCOUNTING FOR FOREIGN CURRENCY TRANSACTIONS
   (A) INITIAL MEASUREMENT
   (B) SUBSEQUENT MEASUREMENT
   (C) RECOGNITION OF EXCHANGE DIFFERENCES
5. FOREIGN CURRENCY OPERATIONS
   (A) INTEGRAL OR NON-INTEGRAL OPERATIONS
   (B) INTEGRAL OPERATIONS
   (C) NON-INTEGRAL OPERATIONS
6. FORWARD EXCHANGE CONTRACT

1. INTRODUCTION :

The standard deals with the issues involved in accounting for foreign currency transactions and foreign operations i.e., to decide which exchange rate to use and how to recognise the financial effects of changes in exchange rates in the financial statements.

2. SCOPE :

This Standard should be applied:

(a) In accounting for transactions in foreign currencies.

(b) In translating the financial statements of foreign operations.

(c) This Statement also deals with accounting for foreign currency transactions in the nature of forward exchange contracts.

This Standard does not:

(a) Specify the currency in which an enterprise presents its financial statements. However, an enterprise normally uses the currency of the country in which it is domiciled. If it uses a different currency, the Standard requires disclosure of the reasons for using that currency. The Standard also requires disclosure of the reason for any change in the reporting currency.

(b) Deal with the presentation in a cash flow statement of cash flows arising from transactions in a foreign currency and the translation of cash flows of a foreign operation, which are addressed in AS 3 'Cash flow statement'.

(c) Deal with exchange differences arising from foreign currency borrowings to the extent that they are regarded as an adjustment to interest costs.

(d) Deal with the restatement of an enterprise's financial statements from its reporting currency into another currency for the convenience of users accustomed to that currency or for similar purposes.

3. DEFINITIONS :

1. **A foreign currency transaction** is a transaction which is denominated in or requires settlement in a foreign currency, including transactions arising when an enterprise either:
   (a) Buys or sells goods or services whose price is denominated in a foreign currency.
   (b) Borrows or lends funds when the amounts payable or receivable are denominated in a foreign currency.
   (c) Becomes a party to an unperformed forward exchange contract or
   (d) Otherwise acquires or disposes of assets, or incurs or settles liabilities, denominated in a foreign currency.

2. **Monetary items** are money held and assets and liabilities to be received or paid in fixed or determinable amounts of money. For example, cash, receivables and payables.
3. **Non-monetary items** are assets and liabilities other than monetary items. For example, fixed assets, inventories and investments in equity shares.
4. **Foreign operation** is a subsidiary, associate, joint venture or branch of the reporting enterprise, the activities of which are based or conducted in a country other than the country of the reporting enterprise.
5. **Integral foreign operation** is a foreign operation, the activities of which are an integral part of those of the reporting enterprise. A foreign operation that is integral to the operations of the reporting enterprise carries on its business as if it were an extension of the reporting enterprise's operations.
6. **Non-integral foreign operation** is a foreign operation that is not an integral foreign operation. When there is a change in the exchange rate between the reporting currency and the local currency, there is little or no direct effect on the present and future cash flows from operations of either the non-integral foreign operation or the reporting enterprise. The change in the exchange rate affects the reporting enterprise's net investment in the non-integral foreign operation rather than the individual monetary and non-monetary items held by the non-integral foreign operation.
   'Net investment in a non-integral foreign operation' is the reporting enterprise's share in the net assets of that operation.
7. **Forward exchange contract** means an agreement to exchange different currencies at a forward rate.
8. **Forward rate** is the specified exchange rate for exchange of two currencies at a specified future date. 'Foreign currency' is a currency other than the reporting currency of an enterprise.

4. ACCOUNTING FOR FOREIGN CURRENCY TRANSACTIONS :

4.1 Initial recognition :

ALL foreign currency transactions should be recorded at SPOT RATE i.e rate existing at the date of transaction.

4.2 Subsequent Measurement :

Subsequent measurement shall be required for any assets and liabilities in foreign currencies. All foreign currency assets and liability will have to be classified into

1. Monetary item
2. Non-monetary item

1. **Monetary items :** At closing rate (Rate existing at the date of reporting)

2. **Non-monetary items :**
   A. **Items carried over at cost :** Historical rate (Rate at which the transaction takes places) (Spot rate at the date of transaction)
   B. **Items carried over at Fair Value :** At closing rate.

4.3 Recognition of Exchange Differences :

Central Government in consultation with National Advisory Committee on Accounting Standards made an amendment to AS 11 "The Effects of Changes in Foreign Exchange Rates" in the form of Companies (Accounting Standards) Amendment Rules, 2009 and 2011.

According to the Notification, exchange differences arising on reporting of longterm foreign currency monetary items at rates different from those at which they were initially recorded during the period, or reported in previous financial statements, insofar as they relate to the acquisition of a depreciable capital asset, can be added to or deducted from the cost of the asset and should be depreciated over the balance life of the asset, and in other cases, can be accumulated in the Foreign Currency Monetary Item Translation Difference (FCMITD) Account and should be written off over the useful life of the assets (amortised over the balance period of such long term assets or liability, by recognition as income or expense in each of such periods) but not beyond 31st March, 2020.

Any difference pertaining to accounting periods which commenced on or after 7th December, 2006, previously, recognised in the profit and loss account before the exercise of the option should be reversed insofar as it relates to the acquisition of a depreciable capital asset by addition or deduction from the cost of the asset and in other cases by transfer to Foreign Currency Monetary Item Translation Difference (FCMITD) Account, and by debit or credit, as the case may be, to the general reserve.

Question 1 :

Classify the following into monetary and non-monetary items

1. Property, Plant and Equipment
2. Intangible Assets
3. Goodwill
4. Investment in Associate
5. Investment in Equity
6. Investment in Debt Security
7. Biological Assets
8. DTA
9. Inventory

10. Trade receivable
11. Bank Balance
12. Cash Balance
13. Share capital
14. Other equity
15. Provision for Employee benefits
16. Finance Lease liability
17. DTL
18. Bank and Other Loans
19. Outstanding Expenses
20. Pre-received income
21. Trade payable
22. Current Tax Liability
23. Outstanding income
24. Prepaid Expenses

Question 2 : A Ltd.

On 30th January, 20X1, A Ltd. purchased a machinery for $5,000 from USA supplier on credit basis. A's Ltd. functional currency is the Rupee. The exchange rate on the date of transaction is 1$= Rs.60. The fair value of the machinery determined on 31st March, 20X1 is $ 5,500. The exchange rate on 31st March, 20X1 is 1$= Rs.65. The payment to overseas supplier done on 31st March 20X2 and the exchange rate on 31st March 20X2 is 1$= Rs.67. The fair value of the machinery remain unchanged for the year ended on 31st March 20X2. Prepare the Journal entries for the year ended on 31st March 20X1 and year 20X2 according to Ind AS 21.

Question 3 : P Ltd.

On 1st January, 2018, P Ltd. purchased a machine for $ 2 lakhs. The functional currency of P Ltd. is Rupees. At that date the exchange rate was $1= Rs.68. P Ltd. is not required to pay for this purchase until 30th June, 2018. Rupees strengthened against the $ in the three months following purchase and by 31st March, 2018 the exchange rate was $1 = Rs.65. CFO of P Ltd. feels that these exchange fluctuations wouldn't affect the financial statements because P Ltd. has an asset and a liability denominated in rupees. Which was initially the same amount. He also feels that P Ltd. depreciates this machine over four years so the future year-end amounts won't be the same.

Examine the impact of this transaction on the financial statements of P Ltd. for the year ended 31st March, 2018 as per AS.

Question 4 : A Ltd.

Supplier, A Ltd., enters into a contract with a customer, B Ltd., on 1st January, 2018 to deliver goods in exchange for total consideration of USD 50 million and receives an upfront payment of USD 20 million on this date. The functional currency of the supplier is INR. The goods are delivered and revenue is recognised on 31st March, 2018. USD 30 million is received on 1st April, 2018 in full and final settlement of the purchase consideration.

State the date of transaction for advance consideration and recognition of revenue. Also state the amount of revenue in INR to be recognized on the date of recognition of revenue. The exchange rates on 1st January, 2018 and 31st March, 2018 are Rs.72 per USD and Rs.75 per USD respectively.

5. FOREIGN CURRENCY OPERATIONS :

5.1 Classification of Foreign Operations as Integral or Non-integral :

The method used to translate the financial statements of a foreign operation depends on the way in which it is financed and operates in relation to the reporting enterprise. For this purpose, foreign operations are classified as either 'integral foreign operations' or 'non-integral foreign operations'.

An integral foreign operation carries on its business as if it were an extension of the reporting enterprise's operations.

In contrast, a non-integral foreign operation accumulates cash and other monetary items, incurs expenses, generates income and perhaps arranges borrowings, all substantially in its local currency.

5.2 Translation of Foreign Integral Operations :

The individual items in the financial statements of the foreign operation are translated as if all its transactions had been entered into by the reporting enterprise itself. The cost and depreciation of tangible fixed assets is translated using the exchange rate at the date of purchase of the asset or, if the asset is carried at fair value or other similar valuation, using the rate that existed on the date of the valuation. The cost of inventories is translated at the exchange rates that existed when those costs were incurred. The recoverable amount or realisable value of an asset is translated using the exchange rate that existed when the recoverable amount or net realisable value was determined. For example, when the net realisable value of an item of inventory is determined in a foreign currency, that value is translated using the exchange rate at the date as at which the net realisable value is determined. The rate used is therefore usually the closing rate.

5.3 Translation of Non-Integral Foreign Operations :

The translation of the financial statements of a non-integral foreign operation is done using the following procedures:

(a) The assets and liabilities, both monetary and non-monetary, of the nonintegral foreign operation should be translated at the closing rate;

(b) Income and expense items of the non-integral foreign operation should be translated at exchange rates at the dates of the transactions; and

(c) All resulting exchange differences should be accumulated in a foreign currency translation reserve until the disposal of the net investment.

(d) For practical reasons, a rate that approximates the actual exchange rates, for example an average rate for the period is often used to translate income and expense items of a foreign operation.

(e) Any goodwill or capital reserve arising on the acquisition of a non-integral foreign operation is translated at the closing rate.

(f) A contingent liability disclosed in the financial statements of a non-integral foreign operation is translated at the closing rate for its disclosure in the financial statements of the reporting enterprise.

6. FORWARD EXCHANGE CONTRACT :

An enterprise may enter into a forward exchange contract or another financial instrument that is in substance a forward exchange contract, which is not intended for trading or speculation purposes, to establish the amount of the reporting currency required or available at the settlement date of a transaction. The premium or discount arising at the inception of such a forward exchange contract should be amortised as expense or income over the life of the contract.

Exchange differences on such a contract should be recognised in the statement of profit and loss in the reporting period in which the exchange rates change. Any profit or loss arising on cancellation or renewal of such a forward exchange contract should be recognised as income or as expense for the period.

In recording a forward exchange contract intended for trading or speculation purposes, the premium or discount on the contract is ignored and at each balance sheet date, the value of the contract is marked to its current market value and the gain or loss on the contract is recognised.

PRACTICAL QUESTIONS :

Question 5 : Kalim Ltd.

Kalim Ltd. borrowed US$ 4,50,000 on 01/01/2016, which will be repaid as on 31/07/2016. Kalim Ltd. prepares financial statement ending on 31/03/2016. Rate of exchange between reporting currency (INR) and foreign currency (USD) on different dates are as under:

01/01/2016 1 US$ = Rs.48.00

31/03/2016 1 US$ = Rs.49.00

31/07/2016 1 US$ = Rs.49.50

Question 6 : Opportunity Ltd.

Opportunity Ltd. purchased an equipment costing Rs.24,00,000 on 1.4.2015 and the same was fully financed by foreign currency loan (US Dollars) payable in four annual equal installments. Exchange rates were 1 Dollar = Rs.60.00 and Rs.62.50 as on 1.4.2015 and 31.3.2016 respectively. First installment was paid on 31.3.2016. The entire difference in foreign exchange has been capitalised. You are required to state that how these transactions would be accounted for.

Question 7 : Head Office in Kolkata

A business having the Head Office in Kolkata has a branch in UK. The following is the trial balance of Branch as at 31.03.2016:

Account Name	Amount in £	
	Dr.	Cr.
Fixed Assets (Purchased on 01.04.2013)	5,000	
Debtors	1,600	
Opening Stock	400	
Goods received from Head Office Account	6,100	
(Recorded in HO books as Rs.4,02,000)		
Sales		20,000
Purchases	10,000	
Wages	1,000	
Salaries	1,200	
Cash	3,200	
Remittances to Head Office (Recorded in HO books as Rs.1,91,000)	2,900	
Head Office Account (Recorded in HO books as Rs.4,90,000)		7,400
Creditors		4,000

- Closing stock at branch is £ 700 on 31.03.2016.
- Depreciation @ 10% p.a. is to be charged on fixed assets.
- Prepare the trial balance after been converted in Indian Rupees.
- Exchange rates of Pounds on different dates are as follow:
  01.04.2013– Rs.61; 01.04.2015– Rs.63 & 31.03.2016 – Rs.67

Question 8 : Rau Ltd.

Rau Ltd. purchased a plant for US$ 1,00,000 on 01st February 2016, payable after three months. Company entered into a forward contract for three months @ Rs.49.15 per dollar. Exchange rate per dollar on 01st Feb. was Rs.48.85. How will you recognise the profit or loss on forward contract in the books of Rau Ltd.?

Question 9 : Mr. A

Mr. A bought a forward contract for three months of US$ 1,00,000 on 1st December at 1 US$ = Rs.47.10 when exchange rate was US$ 1 = Rs.47.02. On 31st December when he closed his books exchange rate was US$ 1 = Rs.47.15. On 31st January, he decided to sell the contract at Rs.47.18 per dollar. Show how the profits from contract will be recognised in the books.

Question 10 : A Ltd.

A Ltd. purchased fixed assets costing Rs.3,000 lakhs on 1.1.2016 and the same was fully financed by foreign currency loan (U.S. Dollars) payable in three annual equal instalments. Exchange rates were 1 Dollar = Rs.40.00 and Rs.42.50 as on 1.1.2016 and 31.12.2016 respectively. First instalment was paid on 31.12.2016. The entire difference in foreign exchange has been capitalised.
You are required to state, how these transactions would be accounted for.

MCQs :

1. As per AS 11 assets and liabilities of non-integral foreign operations should be converted at ___________ rate.
   (a) Opening (b) Average
   (c) Closing (d) Transaction
2. The debit or credit balance of "Foreign Currency Monetary Item Translation Difference Account"
   (a) Is shown as "Miscellaneous Expenditure" in the Balance Sheet
   (b) Is shown under "Reserves and Surplus" as a separate line item
   (c) Is shown as "Other Non-current" in the Balance Sheet
   (d) Is shown as "Current Assets" in the Balance Sheet
3. If asset of an integral foreign operation is carried at cost, cost and depreciation of tangible fixed asset is translated at
   (a) Average exchange rate
   (b) Closing exchange rate
   (c) Exchange rate at the date of purchase of asset
   (d) Opening exchange rate

4. Which of the following can be classified as an integral foreign operation?
   (a) Branch office serving as an extension of the head office in terms of operations
   (b) Independent subsidiary of the parent company
   (c) Branch office independent of the head office in terms of operational decisions
   (d) None of the above
5. Which of the following items should be converted to closing rate for the purposes of financial reporting?
   (a) Items of Property, Plant and Equipment
   (b) Inventory
   (c) Trade Payables, Trade Receivables and Foreign Currency Borrowings
   (d) All of the above

Thanks ....

Chapter 13

AS 12 – ACCOUNTING FOR GOVERNMENT GRANTS

CHAPTER DESIGN

1. INTRODUCTION
2. SCOPE
3. GOVERNMENT GRANTS
4. RECOGNITION OF GOVERNMENT GRANT
5. ACCOUNTING FOR GOVERNMENT GRANTS
6. NON-MONETARY GRANTS
7. PRESENTATION OF GRANTS
8. REFUND OF GOVT GRANTS

1. INTRODUCTION :

AS 12 deals with accounting for government grants, its recognition criteria, measurement of non-monetary grants and presentation of grants in financial statements.

2. SCOPE :

This Standard does not deal with:

(i) The special problems arising in accounting for government grants in financial statements reflecting the effects of changing prices or in supplementary information of a similar nature.

(ii) Government assistance other than in the form of government grants.

(iii) Government participation in the ownership of the enterprise.

3. GOVERNMENT GRANTS :

Government grants are assistance by government in cash or kind to an enterprise for past or future compliance with certain conditions. They exclude those forms of government assistance which cannot reasonably have a value placed upon them and transactions with government which cannot be distinguished from the normal trading transactions of the enterprise

4. RECOGNITION OF GOVERNMENT GRANTS :

A government grant is not recognised until there is reasonable assurance that:

- the enterprise will comply with the conditions attaching to it; and
- the grant will be received.

Receipt of a grant is not of itself conclusive evidence that the conditions attaching to the grant have been or will be fulfilled.

5. ACCOUNTING FOR GOVERNMENT GRANTS :

Two broad approaches may be followed for the accounting treatment of government grants:

- the 'capital approach', under which a grant is treated as part of shareholders' funds, and
- the 'income approach', under which a grant is taken to income over one or more periods.

It is generally considered appropriate that accounting for government grant should be based on the nature of the relevant grant. Grants which have the characteristics similar to those of promoters' contribution should be treated as part of shareholders' funds. Income approach may be more appropriate in the case of other grants.

6. NON MONETARY GRANTS :

Government grants may take the form of non-monetary assets, such as land or other resources, given at concessional rates. In these circumstances, it is usual to account for such assets at their acquisition cost. Non-monetary assets given free of cost are recorded at a nominal value.

7. PRESENTATION OF GOVERNMENT GRANTS :

7.1. Presentation of Grants Related to Specific Fixed Assets :

Two methods of presentation in financial statements of grants related to specific fixed assets are regarded as acceptable alternatives.

Method I :

- The grant is shown as a deduction from the gross value of the asset concerned in arriving at its book value.

Method II :

- Grants related to depreciable assets are treated as deferred income which is recognised in the profit and loss statement on a systematic and rational basis over the useful life of the asset.

7.2 Presentation of Grants Related to Revenue :

Grants related to revenue are sometimes presented as a credit in the profit and loss statement, either separately or under a general heading such as 'Other Income'. Alternatively, they are deducted in reporting the related expense.

7.3 Presentation of Grants of the Nature of Promoters' Contribution :

Where the government grants are of the nature of promoters' contribution, i.e., they are given with reference to the total investment in an undertaking or by way of contribution towards its total capital outlay (for example, central investment subsidy scheme) and no repayment is ordinarily expected in respect thereof, the grants are treated as capital reserve which can be neither distributed as dividend nor considered as deferred income.

Question 1 : Z Ltd.

Z Ltd. purchased a fixed asset for Rs.50 lakhs, which has the estimated useful life of 5 years with the salvage value of Rs.5,00,000. On purchase of the assets government granted it a grant for Rs.10 lakhs. Pass the necessary journal entries in the books of the company for first two years if the grant amount is deducted from the value of fixed asset.

Question 2 : Z Ltd.

Z Ltd. purchased a fixed asset for Rs.50 lakhs, which has the estimated useful life of 5 years with the salvage value of Rs.5,00,000. On purchase of the assets government granted it a grant for Rs. 10 lakhs. Pass the necessary journal entries in the books of the company for first two years if the grant is treated as deferred income.

Question 3 : Santosh Ltd.

Santosh Ltd. has received a grant of Rs.8 crores from the Government for setting up a factory in a backward area. Out of this grant, the company distributed Rs.2 crores as dividend. Also, Santosh Ltd. received land free of cost from the State Government but it has not recorded it at all in the books as no money has been spent. In the light of AS 12 examine, whether the treatment of both the grants is correct.

Question 4 : Top & Top Limited

Top & Top Limited has set up its business in a designated backward area which entitles the company to receive from the Government of India a subsidy of 20% of the cost of investment. Having fulfilled all the conditions under the scheme, the company on its investment of Rs.50 crore in capital assets received Rs.10 crore from the Government in January, 2017 (accounting period being 2016-2017). The company wants to treat this receipt as an item of revenue and thereby reduce the losses on profit and loss account for the year ended 31st March, 2017.

Keeping in view the relevant Accounting Standard, discuss whether this action is justified or not.

8. REFUND OF GOVT GRANT :

- Government grants sometimes become refundable because certain conditions are not fulfilled and are treated as an extraordinary item (AS 5).
- The amount refundable in respect of a government grant related to revenue is applied first against any unamortised deferred credit remaining in respect of the grant. To the extent that the amount refundable exceeds any such deferred credit, or where no deferred credit exists, the amount is charged immediately to profit and loss statement.
- The amount refundable in respect of a government grant related to a specific fixed asset is recorded by increasing the book value of the asset or by reducing the deferred income balance, as appropriate, by the amount refundable. In the first alternative, i.e., where the book value of the asset is increased, depreciation on the revised book value is provided prospectively over the residual useful life of the asset.
- Where a grant which is in the nature of promoters' contribution becomes refundable, in part or in full, to the government on non-fulfillment of some specified conditions, the relevant amount recoverable by the government is reduced from the capital reserve.

PRACTICAL QUESTIONS :

Question 5 : Z Ltd.

Z Ltd. purchased a fixed asset for Rs.50 lakhs, which has the estimated useful life of 5 years with the salvage value of Rs.5,00,000. On purchase of the assets government granted it a grant for Rs.10 lakhs (This amount was reduced from the cost of fixed asset). Grant was considered as refundable in the end of 2nd year to the extent of Rs.7,00,000. Pass the journal entry for refund of the grant as per the first method.

Question 6 :

A fixed asset is purchased for Rs.20 lakhs. Government grant received towards it is Rs.8 lakhs. Residual Value is Rs.4 lakhs and useful life is 4 years. Assume depreciation on the basis of Straight Line method. Asset is shown in the balance sheet net of grant. After 1 year, grant becomes refundable to the extent of Rs.5 lakhs due to non-compliance with certain conditions. Pass journal entries for first two years.

Question 7 : ABC Ltd.

On 1. 4.2014, ABC Ltd. received Government grant of Rs.300 lakhs for acquisition of machinery costing Rs.1,500 lakhs. The grant was credited to the cost of the asset. The life of the machinery is 5 years. The machinery is depreciated at 20% on WDV basis. The Company had to refund the grant in May 2017 due to non-fulfillment of certain conditions. How you would deal with the refund of grant in the books of ABC Ltd. assuming that the company did not charge any depreciation for year 2017?

Question 8 : A Ltd.

A Ltd. purchased a machinery for Rs.40 lakhs. (Useful life 4 years and residual value Rs.8 lakhs) Government grant received is Rs.16 lakhs.

Show the Journal Entry to be passed at the time of refund of grant in the third year and the value of the fixed assets, if:

(1) the grant is credited to Fixed Assets A/c.

(2) the grant is credited to Deferred Grant A/c.

MCQs :

1. To encourage industrial promotion, IDCI offers subsidy worth Rs. 50 lakhs to all new industries set up in the specified industrial areas. This grant is in the nature of promoter's contribution. How such subsidy should be accounted in the books?

   (a) Credit it to capital reserve

   (b) Credit it as 'other income' in the profit and loss account in the year of commencement of commercial operations

   (c) Both (a) and (b) are permitted

(d) Credit it to general reserve

2. Government grants that are receivable as compensation for expenses or losses incurred in a previous accounting period or for the purpose of giving immediate financial support to the enterprise with no further related costs, should be
   (a) recognised and disclosed in the Statement of Profit and Loss of the period in which they are receivable as an ordinary item.
   (b) recognised and disclosed in the Statement of Profit and Loss of the period in which the losses or expenses were incurred.
   (c) recognised and disclosed in the Statement of Profit and Loss of the period in which they are receivable, as an extraordinary item if appropriate as per AS 5.
   (d) disclosed in the Statement of Profit and Loss of the period in which they are receivable, as an extraordinary item

3. Which of the following is an acceptable method of accounting presentation for a government grant relating to an asset?
   (a) Credit the grant immediately to Income statement
   (b) Show the grant as part of Capital Reserve
   (c) Reduce the grant from the cost of the asset or show it separately as a deferred income on the Liability side of the Balance Sheet.
   (d) Show the grant as part of general Reserve

4. X Ltd. has received a grant of Rs. 20 crore for purchase of a qualified machine costing Rs. 80 crore. X Ltd has a policy to recognise the grant as a deduction from the cost of the asset. The expected remaining useful life of the machine is 10 years. Assume that there is no salvage value and the depreciation method is straight-line. The amount of annual depreciation to be charged as an expense in Profit and Loss Statement will be:
   (a) Rs. 10 crore (b) Rs. 6 crore
   (c) Rs. 2 crore (d) Rs. 8 crore

5. X Ltd has received a grant of Rs. 20 crore for purchase of a qualified machine costing Rs. 80 crore. X Ltd. has a policy to recognise the grant as deferred income. The expected remaining useful life of the machine is 10 years.
   Assume that there is no salvage value and the depreciation method is straight-line. The amount of other income to be to be recognised in Profit and Loss Statement will be:
   (a) Rs. 10 crore (b) Rs. 6 crore
   (c) Rs. 2 crore (d) Rs. 8 crore

Thanks ....

Rahul Malkan

Chapter 14

AS 13 – ACCOUNTING FOR INVESTMENTS

CHAPTER DESIGN

1. INTRODUCTION
2. SCOPE
3. DEFINITIONS
4. CLASSIFICATION
5. COSTS OF INVESTMENTS
6. CARRYING AMOUNT OF INVESTMENTS
7. INVESTMENT PROPERTIES
8. DISPOSAL OF INVESTMENTS
9. RE-CLASSIFICATION OF INVESTMENTS
10. DISCLOSURE
11. ACCOUNTING FOR INVESTMENTS

1. INTRODUCTION :

The standard deals with accounting for investments in the financial statements of enterprises and related disclosure requirements. The enterprises are required to disclose the current investments (realisable in nature and intended to be held for not more than one year from the date of its acquisition) and long terms investments (other than current investments) distinctly in their financial statements

The cost of investments should include all acquisition costs (including brokerage, fees and duties) and on disposal of an investment, the difference between the carrying amount and net disposal proceeds should be charged or credited to profit and loss statement.

2. SCOPE :

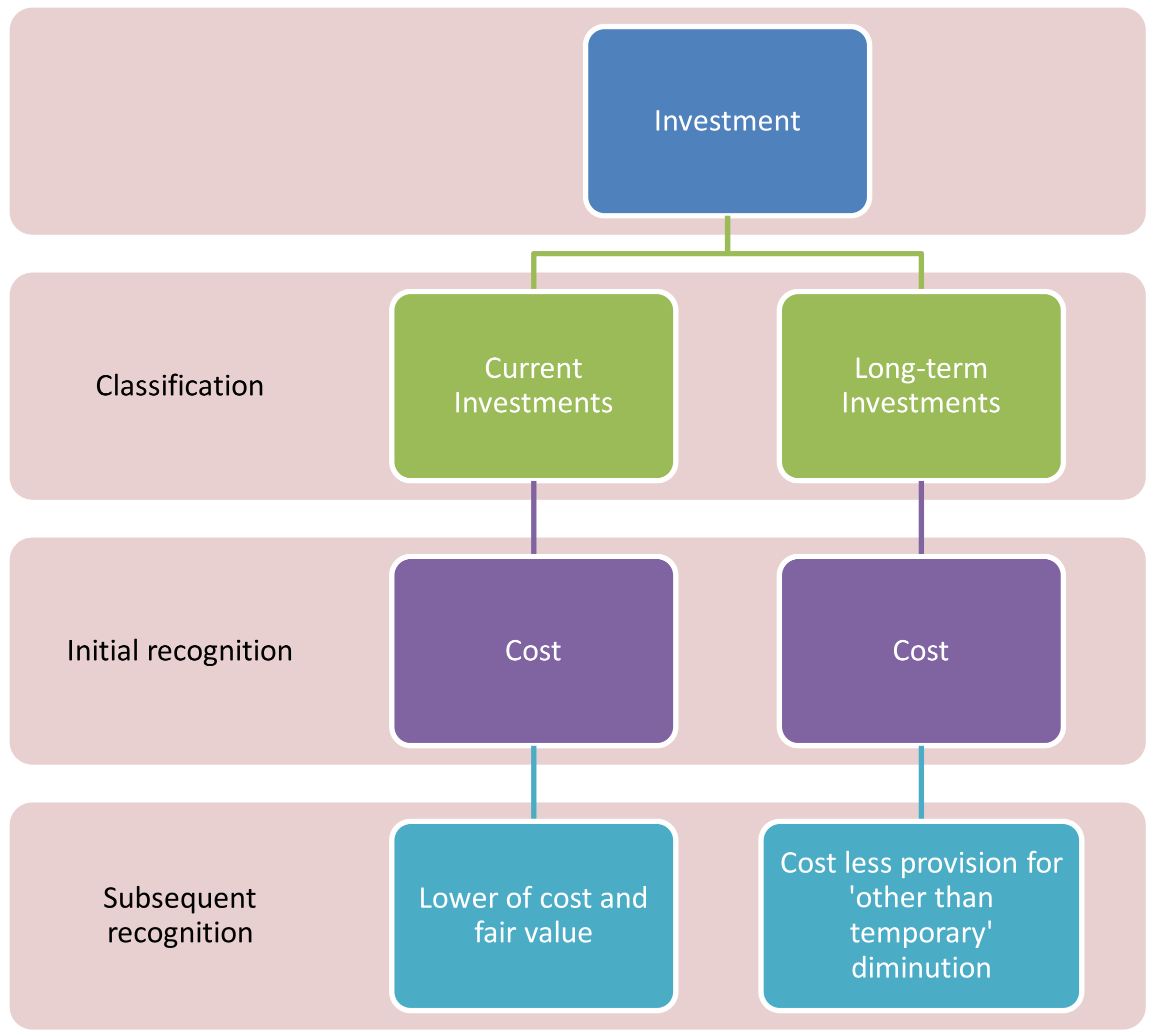
This Standard does not deal with:

a. The basis for recognition of interest, dividends and rentals earned on investments which are covered by AS 9
b. Operating or finance leases
c. Investments on retirement benefit plans and life insurance enterprises
d. Mutual funds, venture capital funds and/ or the related asset management companies, banks and public financial institutions formed under a Central or State Government Act or so declared under the Companies Act, 2013.

3. DEFINITIONS :

1. Investments are assets held by an enterprise for earning income by way of dividends, interest, and rentals, for capital appreciation, or for other benefits to the investing enterprise. Assets held as stock-in-trade (inventory) are not ‘investments’
2. Fair value is the amount for which an asset could be exchanged between a knowledgeable, willing buyer and a knowledgeable, willing seller in an arm’s length transaction. Under appropriate circumstances, market value or net realisable value provides an evidence of fair value.
3. Market value is the amount obtainable from the sale of an investment in an open market, net of expenses necessarily to be incurred on or before disposal.

4. CLASSIFICATION OF INVESTMENTS :



A current investment is an investment that is by its nature readily realisable and is intended to be held for not more than one year from the date on which such investment is made. The intention to hold for not more than one year is to be judged at the time of purchase of investment.
A long term investment is an investment other than a current investment

5. COST OF INVESTMENTS :

The cost of an investment includes acquisition charges such as brokerage, fees and duties etc.
If an investment is acquired, or partly acquired, by the issue of shares or other securities, the acquisition cost is the fair value of the securities issued or asset given up. The fair value may not necessarily be equal to the nominal or par value of the securities issued.
If an investment is acquired in exchange, or part exchange, for another asset, the acquisition cost of the investment is determined by reference to the fair value of the asset given up or the fair value of the investment acquired, whichever is more clearly evident.

6. CARRYING AMOUNT OF INVESTMENTS :

The carrying amount for current investments is the lower of cost and fair value.

Valuation of current investments on overall (or global) basis is not considered appropriate. Sometimes, the concern of an enterprise may be with the value of a category of related current investments and not with each individual investment, and accordingly the investments may be carried at the lower of cost and fair value computed category-wise (i.e. equity shares, preference shares, convertible debentures, etc.). However, the more prudent and appropriate method is to carry investments individually at the lower of cost and fair value.

Any reduction to fair value is debited to profit and loss account, however, if fair value of investment is increased subsequently, the increase in value of current investment upto the the cost of investment is credited to the profit and loss account (and excess portion, if any, is ignored).

Long term investments are usually carried at cost. The carrying amount of long term investments is therefore determined on an individual investment basis.

Where there is a decline, other than temporary, in the carrying amounts of long term valued investments, the resultant reduction in the carrying amount is charged to the profit and loss statement. The reduction in carrying amount is reversed when there is a rise in the value of the investment, or if the reasons for the reduction no longer exist.

7. INVESTMENT PROPERTY :

An investment property is an investment in land or buildings that are not intended to be occupied substantially for use by, or in the operations of, the investing enterprise.

An investment property is accounted for in accordance with cost model as prescribed in AS 10 (Revised), 'Property, Plant and Equipment'. The cost of any shares in a co-operative society or a company, the holding of which is directly related to the right to hold the investment property, is added to the carrying amount of the investment property.

8. DISPOSAL OF INVESTMENTS :

On disposal of an investment, the difference between the carrying amount and the disposal proceeds, net of expenses, is recognised in the profit and loss statement. When disposing of a part of the holding of an individual investment, the carrying amount to be allocated to that part is to be determined on the basis of the average carrying amount of the total holding of the investment.

9. RECLASSIFICATION OF INVESTMENTS :

Where long-term investments are reclassified as current investments, transfers are made at the lower of cost and carrying amount at the date of transfer. Where investments are reclassified from current to long-term, transfers are made at the lower of cost and fair value at the date of transfer

10. DISCLOSURE :

The following disclosures in financial statements in relation to investments are appropriate: -

a. The accounting policies followed for valuation of investments.

b. The amounts included in profit and loss statement for:

   i. Interest, dividends (showing separately dividends from subsidiary companies), and rentals on investments showing separately such income from long term and current investments. Gross income should be stated, the amount of income tax deducted at source being included under Advance Taxes Paid.

   ii. Profits and losses on disposal of current investments and changes in carrying amount of such investments.

   iii. Profits and losses on disposal of long term investments and changes in the carrying amount of such investments.

c. Significant restrictions on the right of ownership, realisability of investments or the remittance of income and proceeds of disposal.

d. The aggregate amount of quoted and unquoted investments, giving the aggregate market value of quoted investments.

e. Other disclosures as specifically required by the relevant statute governing the enterprise.

Question 1 :

An unquoted long term investment is carried in the books at a cost of Rs 2 lakhs. The published accounts of the unlisted company received in May, 2017 showed that the company was incurring cash losses with declining market share and the long term investment may not fetch more than Rs 20,000. How will you deal with this in preparing the financial statements of R Ltd. for the year ended 31st March, 2017?

Question 2 : X Ltd.

X Ltd. on 1-1-2017 had made an investment of Rs 600 lakhs in the equity shares of Y Ltd. of which 50% is made in the long term category and the rest as temporary investment. The realisable value of all such investment on 31-3-2017 became Rs 200 lakhs as Y Ltd. lost a case of copyright. From the given market conditions, it is apparent that the reduction in the value is not temporary in nature. How will you recognise the reduction in financial statements for the year ended on 31-3-2017?

Question 3 : M/s Innovative Garments

M/s Innovative Garments Manufacturing Company Limited invested in the shares of another company on 1st October, 2016 at a cost of Rs 2,50,000. It also earlier purchased Gold of Rs 4,00,000 and Silver of RS 2,00,000 on 1st March, 2014. Market value as on 31st March, 2017 of above investments are as follows:

	Rs.
Shares	2,25,000
Gold	6,00,000
Silver	3,50,000

How above investments will be shown in the books of accounts of M/s Innovative Garments Manufacturing Company Limited for the year ending 31st March, 2017 as per the provisions of Accounting Standard 13 "Accounting for Investments"?

Question 4 : ABC Ltd.

ABC Ltd. wants to re-classify its investments in accordance with AS 13 (Revised). Decide and state on the amount of transfer, based on the following information:

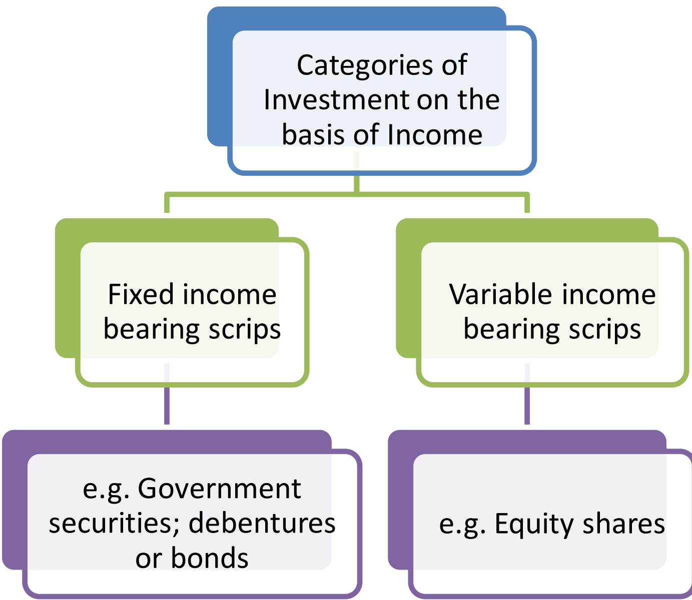
(1) A portion of current investments purchased for Rs 20 lakhs, to be reclassified as long term investment, as the company has decided to retain them. The market value as on the date of Balance Sheet was Rs 25 lakhs.

(2) Another portion of current investments purchased for Rs 15 lakhs, to be reclassified as long term investments. The market value of these investments as on the date of balance sheet was Rs 6.5 lakhs.

(3) Certain long term investments no longer considered for holding purposes, to be reclassified as current investments. The original cost of these was Rs. 18 lakhs but had been written down to Rs 12 lakhs to recognise other than temporary decline as per AS 13 (Revised).

11. ACCOUNTING FOR INVESTMENTS :

A separate Investment Account should be made for each scrip purchased. The scrips purchased may be broadly divided into two categories, viz.



Accounting for Fixed Income Securities :

Question 5 : M/s. Wye Ltd.

In 20X1, M/s. Wye Ltd. issued 12% fully paid debentures of Rs.100 each, interest being payable half yearly on 30th September and 31st March of every accounting year.
On 1st December, 20X2, M/s. Bull & Bear purchased 10,000 of these debentures at Rs.101 cum-interest price, also paying brokerage @ 1% of cum-interest amount of the purchase. On 1st March, 20X3 the firm sold all of these debentures at Rs.106 cum-interest price, again paying brokerage @ 1 % of cum-interest amount. Prepare Investment Account in the books of M/s. Bull & Bear for the period 1st December, 20X2 to 1st March, 20X3.

Question 6 : Mr. Krishna Murty

On 1.4.20X1, Mr. Krishna Murty purchased 1,000 equity shares of Rs.100 each in TELCO Ltd. @ Rs.120 each from a Broker, who charged 2% brokerage. He incurred 50 paise per Rs.100 as cost of shares transfer stamps. On 31.1.20X2, Bonus was declared in the ratio of 1: 2. Before and after the record date of bonus shares, the shares were quoted at Rs.175 per share and Rs.90 per share respectively. On 31.3.20X2, Mr. Krishna Murty sold bonus shares to a Broker, who charged 2% brokerage.
Show the Investment Account in the books of Mr. Krishna Murty, who held the shares as Current assets and closing value of investments shall be made at Cost or Market value whichever is lower.

Question 7 : Mr. X

Mr. X purchased 500 equity shares of Rs.100 each in Omega Co. Ltd. for Rs.62,500 inclusive of brokerage and stamp duty. Some years later the company resolved to capitalise its profits and to issue to the holders of equity shares, one equity bonus share for every share held by them. Prior to capitalisation, the shares of Omega Co. Ltd. were quoted at Rs.175 per share. After the capitalisation, the shares were quoted at Rs.92.50 per share. Mr. X. sold the bonus shares and received at Rs.90 per share.
Prepare the Investment Account in X's books on average cost basis.

Accounting for Variable Income Securities :

Question 8 : Mr. T. Shekharan

On 01-04-20X1, Mr. T. Shekharan purchased 5,000 equity shares of Rs.100 each in V Ltd. @ Rs.120 each from a broker, who charged 2% brokerage. He incurred 50 paisa per Rs.100 as cost of shares transfer stamps. On 31-01-20X2 bonus was declared in the ratio of 1: 2. Before and after the record date of bonus shares, the shares were quoted at Rs.175 per

share and Rs.90 per share respectively. On 31-03-20X2, Mr. T. Shekharan sold bonus shares to a broker, who charged 2% brokerage.

Show the Investment Account in the books of T. Shekharan, who held the shares as Current Assets and closing value of investments shall be made at cost or market value whichever is lower.

Question 9 : Rajat

On 1st April, 20X1, Rajat has 50,000 equity shares of P Ltd. at a book value of Rs.15 per share (nominal value Rs.10 each). He provides you the further information:

(1) On 20th June, 20X1 he purchased another 10,000 shares of P Ltd. at Rs.16 per share.

(2) On 1st August, 20X1, P Ltd. issued one equity bonus share for every six shares held by the shareholders.

(3) On 31st October, 20X1, the directors of P Ltd. announced a right issue which entitles the holders to subscribe three shares for every seven shares at Rs. 15 per share. Shareholders can transfer their rights in full or in part.

Rajat sold 1/3rd of entitlement to Umang for a consideration of Rs. 2 per share and subscribed the rest on 5th November, 20X1.

You are required to prepare Investment A/c in the books of Rajat for the year ending 31st March, 20X2.

Question 10 : Sundar

On 1.4.20X1, Sundar had 25,000 equity shares of 'X' Ltd. at a book value of Rs.15 per share (Nominal value Rs.10). On 20.6.20X1, he purchased another 5,000 shares of the company at Rs.16 per share. The directors of 'X' Ltd. announced a bonus and rights issue. No dividend was payable on these issues. The terms of the issue are as follows:

Bonus basis 1:6 (Date 16.8.20X1).

Rights basis 3:7 (Date 31.8.20X1) Price Rs.15 per share.

Due date for payment 30.9.20X1.

Shareholders were entitled to transfer their rights in full or in part. Accordingly, Sundar sold 33.33% of his entitlement to Sekhar for a consideration of Rs.2 per share.

Dividends: Dividends for the year ended 31.3.20X1 at the rate of 20% were declared by X Ltd. and received by Sundar on 31.10.20X1. Dividends for shares acquired by him on 20.6.20X1 are to be adjusted against the cost of purchase.

On 15.11.20X1, Sundar sold 25,000 equity shares at a premium of Rs.5 per share.

You are required to prepare in the books of Sundar.

(1) Investment Account

(2) Profit & Loss Account.

For your exercise, assume that the books are closed on 31.12.20X1and shares are valued at average cost.

Question 11 : Singh

On 1st January 20X1, Singh had 20,000 equity shares in X Ltd. Nominal value of the shares was Rs.10 each but their book value was Rs.16 per share. On 1st June 20X1, Singh purchased 5,000 more equity shares in the company at a premium of Rs.4 per share.

On 30th June, 20X1, the directors of X Ltd. announced a bonus and rights issue. Bonus was declared at the rate of one equity share for every five shares held and these shares were received on 2nd August, 20X1.

The terms of the rights issue were:

(a) Rights shares to be issued to the existing holders on 10th August, 20X1.

(b) Rights issue would entitle the holders to subscribe to additional equity shares in the Company at the rate of one share per every three held at Rs.15 per share-the whole sum being payable by 30th September, 20X1.

(c) Existing shareholders were entitled to transfer their rights to outsiders, either wholly or in part.

(d) Singh exercised his option under the issue for 50% of his entitlements and the balance of rights he sold to Ananth for a consideration of Rs.1.50 per share.

(e) Dividends for the year ended 31st March, 20X1, at the rate of 15% were declared by the Company and received by Singh on 20th October, 20X1.

(f) On 1st November, 20X1, Singh sold 20,000 equity shares at a premium of Rs.3 per share.

The market price of share on 31-12-20X1 was Rs.14. Show the Investment Account as it would appear in Singh's books on 31-12-20X1 and the value of shares held on that date.

Question 12 : Nidhi

The following transactions of Nidhi took place during the year ended 31st March 20X2:

1st April	Purchased Rs.12,00,000, 8% bonds at Rs.80.50 cum-interest. Interest is payable on 1st November and 1st May.
12th April	Purchased 1,00,000 equity shares of Rs.10 each in X Ltd. for Rs.40,00,000
1st May	Received half-year's interest on 8% bonds.
15th May	X Ltd. made a bonus issue of three equity shares for every two held. Nidhi sold 1,25,000 bonus shares for Rs.20 each.
1st October	Sold Rs.3,00,000, 8% bonds at Rs.81 ex-interest.
1st November	Received half-year's bond interest.
1st December	Received 18% interim dividend on equity shares (including bonus shares) in X Ltd.

Prepare the relevant investment account in the books of Nidhi for the year ended 31st March, 20X2.

Question 13 : Smart Investments

Smart Investments made the following investments in the year 20X1-X2:

12% State Government Bonds having nominal value Rs.100

Date	Particulars
01.04.20X1	Opening Balance (1200 bonds) book value of Rs.126,000
02.05.20X1	Purchased 2,000 bonds @ Rs.100 cum interest
30.09.20X1	Sold 1,500 bonds at Rs.105 ex interest

Interest on the bonds is received on 30th June and 31st Dec. each year.

Equity Shares of X Ltd.	
15.04.20X1	Purchased 5,000 equity shares @ Rs.200 on cum right basis Brokerage of 1% was paid in addition (Nominal Value of shares Rs.10)
03.06.20X1	The company announced a bonus issue of 2 shares for every 5 shares held.
16.08.20X1	The company made a rights issue of 1 share for every 7 shares held at Rs.250 per share. The entire money was payable by 31.08.20X1.
22.8.20X1	Rights to the extent of 20% was sold @ Rs.60. The remaining rights were subscribed.
02.09.20X1	Dividend @ 15% for the year ended 31.03.20X1 was received on 16.09.20X1
15.12.20X1	Sold 3,000 shares @ Rs.300. Brokerage of 1% was incurred extra.
15.01.20X2	Received interim dividend @ 10% for the year 20X1 –X2
31.03.20X2	The shares were quoted in the stock exchange @ Rs.220

Prepare Investment Accounts in the books of Smart Investments. Assume that the average cost method is followed.

Question 14 : Mr. Popli

Mr. Popli has made following transactions during the financial year 20X1-X2:

Date Particulars

01.05.20X1 Purchased 24,000 12% Bonds of Rs.100 each at Rs.84 cum-interest. Interest is payable on 30th September and 31st March every year.

15.06.20X1 Purchased 1,50,000 equity shares of Rs.10 each in Alpha Limited for Rs.25 each through a broker, who charged brokerage @ 2%.

10.07.20X1 Purchased 60,000 equity shares of Rs.10 each in Beeta Limited for Rs.44 each through a broker, who charged brokerage @2%.

14.10.20X1	Alpha Limited made a bonus issue of two shares for every three shares held.
31.10.20X1	Sold 80,000 shares in Alpha Limited for Rs.22 each.
01.01.20X2	Received 15% interim dividend on equity shares of Alpha Limited.
15.01.20X2	Beeta Limited made a right issue of one equity share for every four shares held at Rs.5 per share. Mr. Brown exercised his option for 40% of his entitlements and sold the balance rights in the market at Rs.2.25 per share.
01.03.20X2	Sold 15,000 12% Bonds at Rs.90 ex-interest.
15.03.20X2	Received 18% interim dividend on equity shares of Beeta Limited.

Interest on 12% Bonds was duly received on due dates.

Prepare separate investment account for 12% Bonds, Equity Shares of Alpha Limited and Equity Shares of Beeta Limited in the books of Mr. Brown for the year ended on 31st March, 20X2.

Question 15 : A Limited

A Limited purchased 5,000 equity shares (nominal value Rs.100 each) of Allianz Limited for Rs.105 each on 1st April, 20X1. The shares were quoted cum dividend. On 15th May, 20X1, Allianz Limited declared & paid dividend of 2% for year ended 31st March, 20X1. On 30th June, 20X1 Allianz Limited issued bonus shares in ratio of 1:5. On 1st October, 20X1 Allianz Limited issued rights share in the ratio of 1:12 @ 45 per share. A Limited subscribed to half of the rights issue and the balance was sold at Rs.5 per right entitlement. The company declared interim dividend of 1% on 30th November, 20X1. Right shares were not entitled to dividend. The company sold 3,000 shares on 31st December, 20X1 at Rs.95 per share. The company A Ltd. incurred 2% as brokerage while buying and selling shares.

You are required to prepare Investment Account in books of A Ltd for the year ended 31st March, 20X2.

PRACTICAL QUESTIONS :

Question 16 : XY Ltd.

On 1st April, 20X1, XY Ltd. has 15,000 equity shares of ABC Ltd. at a book value of Rs.15 per share (nominal value Rs.10 per share). On 1st June, 20X1, XY Ltd. acquired 5,000 equity shares of ABC Ltd. for Rs.1,00,000. ABC Ltd. announced a bonus and right issue.

(1) Bonus was declared, at the rate of one equity share for every five shares held, on 1st July 20X1.

(2) Right shares are to be issued to the existing shareholders on 1st September 20X1. The company will issue one right share for every 6 shares at 20% premium. No dividend was payable on these shares.

(3) Dividend for the year ended 31.3.20X1 were declared by ABC Ltd. @ 20%, which was received by XY Ltd. on 31st October 20X1.

XY Ltd.

(i) Took up half the right issue.

(ii) Sold the remaining rights for Rs.8 per share.

(iii) Sold half of its shareholdings on 1st January 20X2 at Rs.16.50 per share. Brokerage being 1%.

You are required to prepare Investment account of XY Ltd. for the year ended 31st March 20X2 assuming the shares are being valued at average cost.

Question 17 : Mr. Z

The following information is presented by Mr. Z (a stock broker), relating to his holding in 9% Central Government Bonds.

Opening balance (nominal value) Rs.1,20,000, Cost Rs.1,18,000 (Nominal value of each unit is Rs.100).

1.3.20X1 Purchased 200 units, ex-interest at Rs.98.

1.7.20X1 Sold 500 units, ex-interest out of original holding at Rs.100.

1.10.20X1 Purchased 150 units at Rs.98, cum interest.

1.11.20X1 Sold 300 units, ex-interest at Rs.99 out of original holdings.

Interest dates are 30th September and 31st March. Mr. Z closes his books every 31st December. Show the investment account as it would appear in his books. Mr. Z follows FIFO method.

Question 18 : Mr. Purohit

Mr. Purohit furnishes the following details relating to his holding in 8% Debentures (Rs.100 each) of P Ltd., held as Current assets:

1.4.20X1 Opening balance – Nominal value Rs.1,20,000, Cost Rs.1,18,000

1.7.20X1 100 Debentures purchased ex-interest at Rs.98

1.10.20X1 Sold 200 Debentures ex-interest at Rs.100

1.1.20X2 Purchased 50 Debentures at Rs.98 cum-interest

1.2.20X2 Sold 200 Debentures ex-interest at V 99

Due dates of interest are 30th September and 31st March.

Mr. Purohit closes his books on 31.3.20X2. Brokerage at 1% is to be paid for each transaction. Show Investment account as it would appear in his books. Assume FIFO method. Market value of 8% Debentures of P Limited on 31.3.20X2 is Rs.99.

MCQs:

1. The cost of Right shares is
   - (a) added to the cost of investments.
   - (b) subtracted from the cost of investments.
   - (c) no treatment is required.
   - (d) added to cost of investments at market value.
2. Long term investments are carried at
   - (a) fair value.
   - (b) cost less 'other than temporary' decline.
   - (c) Cost and market value whichever is less.
   - (d) Cost and market value whichever is higher.
3. Current investments are carried at
   - (a) Fair value.
   - (b) cost.
   - (c) Cost and fair value, whichever is less.
   - (d) Cost and fair value, whichever is higher.
4. A Ltd. acquired 2,000 equity shares of Omega Ltd. on cum-right basis at Rs. 75 per share. Subsequently, omega Ltd. made a right issue of 1:1 at Rs. 60 per share, which was subscribed for by A. Total cost of investments at the year-end will be Rs.
   - (a) 2,70,000.
   - (b) 1,50,000.
   - (c) 1,20,000.
   - (d) 1,70,000.
5. Cost of investment includes
   - (a) Purchase costs.
   - (b) Brokerage and Stamp duty paid.
   - (c) Both (a) and (b).
   - (d) none of the above.

Thanks ....

Rahul Malkan

Chapter 15

AS 15 – EMPLOYEE BENEFITS

CHAPTER DESIGN

1. INTRODUCTION
2. EMPLOYEE BENEFITS
3. SHORT TERM EMPLOYEE BENEFITS
4. PROFIT SHARING AND BONUS PLAN
5. POST EMPLOYMENT PLAN
6. ACCOUNTING TREATMENT
7. ACTUARIAL GAINS AND LOSSES
8. OTHER LONG TERM BENEFITS
9. TERMINATION BENEFITS

1. INTRODUCTION :

The Accounting Standard 15 - 'Employee Benefits' (AS 15), generally deals with all forms of employee benefits all forms of consideration given by an enterprise in exchange for services rendered by employees The objective of this Standard is to prescribe the accounting treatment and disclosure for employee benefits in the books of employer except employee share-based payments.

The Standard addresses only the accounting of employee benefits by employers. The Standard makes four things very clear at the outset:

1. the Standard is applicable to benefits provided to all types of employees (whether full-time, part-time, or casual staff);
2. employee benefits can be paid in cash or in kind;
3. employee benefits include benefits provided to employees and their dependents (spouses, children and others); and
4. payment can be made directly to employees, their dependent or to any other party (e.g., legal heirs, nominees, insurance companies, trust etc.).

The Standard is based on the premise that the costs associated with employees-benefits should be matched with the timing of their service. This requires assessment of the anticipated costs and their timing in future and aligning those costs over the period of their service. For example, a bonus payable to an employee for a long-term service, should ideally be spread over the period of his service and the expectations that the employee is expected to complete that service. Likewise, pension payable to an employee must be recognized as a cost during the service period itself, irrespective of the fact that the pension is payable after the service is completed.

Question 1 :

What are the kinds of employees covered in the revised AS 15 and whether a formal employer employee relationship is necessary or not, for benefits to be covered under the Standard?

Question 2 :

Whether an enterprise is required to provide for employee benefits arising from informal practices?

2. EMPLOYEE BENEFITS :

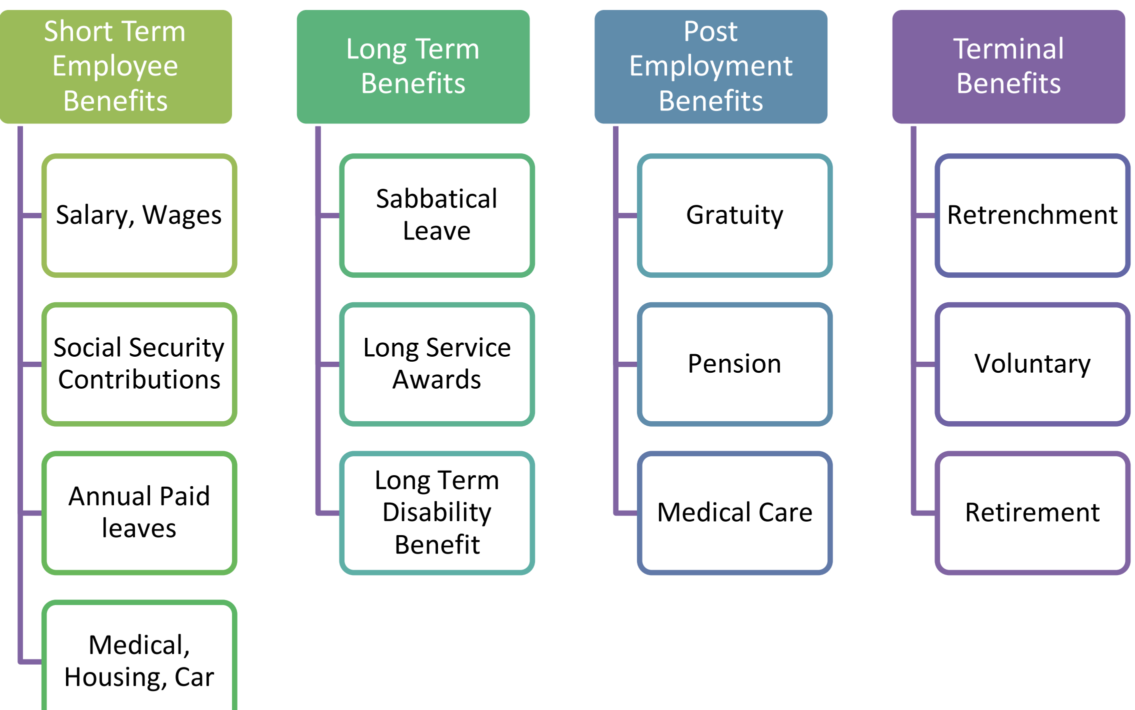
Employee benefits include:

a) Short-term employee benefits (e.g., wages, salaries, paid annual leave and sick leave, profit sharing bonuses etc. (payable within 12 months of the year-end) and non-monetary benefits for current employees.

b) Post-employment benefits (e.g., gratuity, pension, provident fund, post- employment medical care etc.).

c) long-term employee benefits (e.g., long-service leave, long-term disability benefits, bonuses not wholly payable within 12 months of the year end etc.), and

d) termination benefits (e.g. VRS payments)



3. SHORT TERM EMPLOYEE BENEFITS :

Short-term employee benefits (other than termination benefits) are payable within twelve months after the end of the period in which the service is rendered.

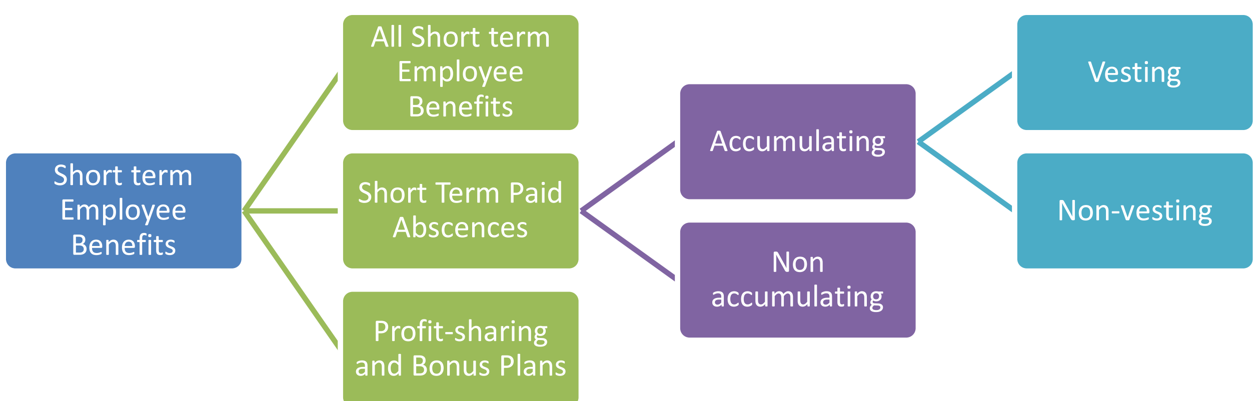
Short-term employee benefits are broadly classified into four categories:

(i) regular period benefits (e.g., wages, salaries);

(ii) short-term compensated absences (e.g., paid annual leave, maternity leave, sick leave etc.);

(iii) profit sharing and bonuses payable within twelve months after the end of the period in which employee render the related services and

(iv) non-monetary benefits (e.g., medical care, housing, cars etc.)



Question 3 : Entity XY

Entity XY is required to pay salary of Rs 2 crore for the year 20X1-X2. It actually paid a salary of Rs 1.90 crore up to 31st March 20X2, and balance in April 20X2. Determine the actual costs to be recognized in the year 20X1-X2 and any amounts to be shown through balance sheet.

Question 4 :

An enterprise has 100 employees, who are each entitled to five working days of leave for each year. Unused leave may be carried forward for one calendar year. The leave is taken first out of the current year's entitlement and then out of any balance brought forward from the previous year (a LIFO basis). At 31st December, 20X4, the average unused entitlement is two days per employee. The enterprise expects, based on past experience which is expected to continue, that 92 employees will take no more than five days of leave in 20X5 and that the remaining eight employees will take an average of six and a half days each. How many days of leave shall be accounted for as on 31st Dec, 20x4.

4. PROFIT SHARING AND BONUS PLAN :

Recognition of expenses for profit sharing and bonus plans would depend on fulfillment of conditions mentioned the Standard. The conditions are:

a) Enterprise has a present obligation to make such payments as a result of past events; and

b) Reliable estimate of the obligation can be made.

The second condition can be satisfied only when the profit sharing and bonus plans contained a formula for determining the amount of benefit. The enterprise should recognize the expected cost of profit sharing and bonus payments in the financial statements.

Question 5 :

A profit-sharing plan requires an enterprise to pay a specified proportion of its net profit for the year to employees who serve throughout the year. If no employees leave during the year, the total profit-sharing payments for the year will be 3% of net profit. The enterprise estimates that staff turnover will reduce the payments to 2.5% of net profit. Can we recognise the expense.

Question 6 :

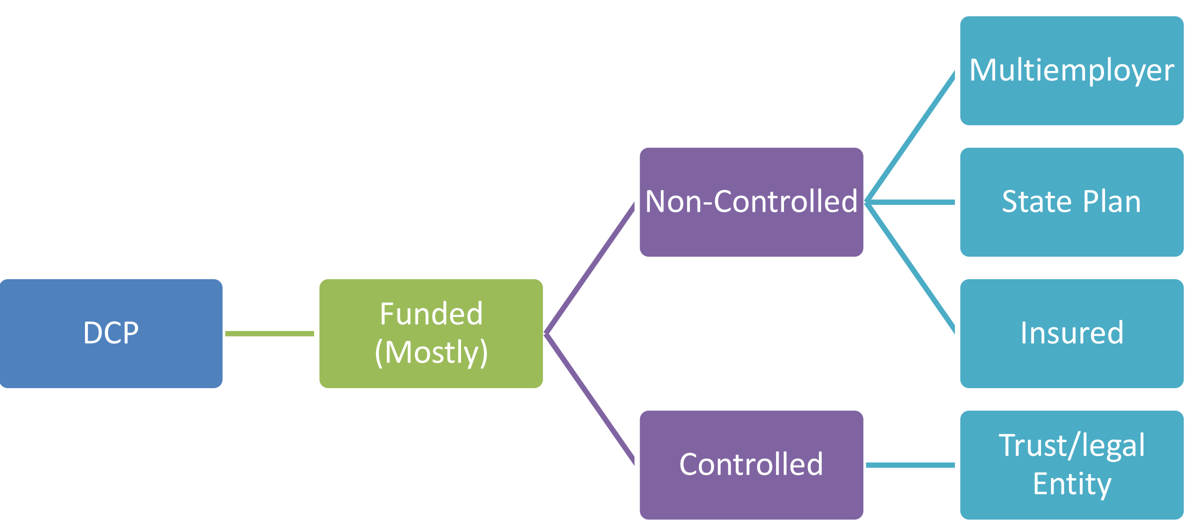
Whether an entitlement to earned leave which can be carried forward to future periods is a short -term employee benefit or a long-term employee benefit.

Question 7 :

In case an enterprise allows unutilised employee benefits, e.g., medical care, leave travel, etc., to be carried forward, whether it is required to recognise a provision in respect of carried forward benefits.

5. POST EMPLOYMENT PLAN :

Defined Contribution V/s Defined Benefits



1. Defined contribution plans (DCP) are post-employment benefit plans under which an enterprise pays fixed contributions into a separate fund and will have no obligation to pay further contributions. Under defined contribution plans, actuarial risk (that benefits will be less than expected) and investment risk (that assets invested will be insufficient to meet expected benefits) fall on the employee. A common example of Defined Contribution plans is Provident Fund.

2. Defined benefit plans are post-employment benefit plans other than defined contribution plans. In defined benefits plans, the actuarial and investment risk fall on the employer.

IS THE GRATUITY SCHEME A DEFINED CONTRIBUTION OR DEFINED BENEFIT SCHEME?

An enterprise may pay insurance premiums to fund a post-employment benefit plan. The enterprise should treat such a plan as a defined contribution plan unless the enterprise will have an obligation to either:

(a) pay the employee benefits directly when they fall due; or
(b) pay further amounts if the insurer does not pay all future employee benefits relating to employee service in the current and prior periods.

On the asset side, a question arises as to whether the funds under the scheme as certified by LIC would be treated as plan assets or reimbursement rights. The distinction is important (though both are measured on fair valuation basis) because plan assets are reduced from the defined benefit obligation and the net amount is disclosed in the balance sheet, whereas, in the case of reimbursement rights, the defined benefit obligation and the reimbursement rights are shown separately as liability and asset on the balance sheet. This would have the impact of making the balance sheet heavy both on the asset side as well as the liabilities side.

6. ACCOUNTING TREATMENT :

In the Balance Sheet of the enterprise, 'the amount recognized as a defined benefit liability should be the net total of the following amounts:

a) the present value of the defined benefit obligation at the balance sheet date
b) minus any past service cost not yet recognized;
c) minus the fair value at the balance sheet date of plan assets (if any) out of which the obligations are to be settled directly.

The recognition of expenses relating to defined benefits in the Statement of Profit and Loss is stated in Para 61 of the Standard. The Standard identifies seven components of defined employee benefit costs:

a) Current Cost
b) Interest Cost
c) the expected return on any plan assets (and on any reimbursement rights)
d) actuarial gains and losses (to the extent they are recognized)
e) past service cost (to the extent they are recognized)
f) the effect of any curtailments or settlements; and
g) the extent to which the negative net amount of defined benefit liability exceeds the amount mentioned in Para 59(b) of the Standard.

7. ACTURAL GAINS AND LOSSES :

Actuarial gains and losses comprise

- experience adjustments (the effects of difference between the previous actuarial assumptions and what has actually occurred); and
- the effects of changes in actuarial assumptions.

Actuarial gains and losses should be recognized immediately in the statement of profit and loss as income or expense.

Question 8 : Omega Limited

Omega Limited belongs to the engineering industry. The company received an actuarial valuation for the first time for its pension scheme which revealed a surplus of Rs 6 lakhs. It wants to spread the same over the next 2 years by reducing the annual contribution to Rs 2 lakhs instead of Rs 5 lakhs. The average remaining life of the employees is estimated to be 6 years. You are required to advise the company on the following items from the viewpoint of finalization of accounts, taking note of the mandatory accounting standards.

Question 9 : Zeleous Ltd.

As on 1st April, 20X1 the fair value of plan assets was Rs 1,00,000 in respect of a pension plan of Zeleous Ltd. On 30th September, 20X1 the plan paid out benefits of Rs 19,000 and received inward contributions of Rs 49,000. On 31st March, 20X2 the fair value of plan assets was Rs 1,50,000 and present value of the defined benefit obligation was Rs 1,47,920. Actuarial losses on the obligations for the year 20X1- 20X2 were Rs 600.

On 1st April, 20X1, the company made the following estimates, based on its market studies, understanding and prevailing prices.

	%
Interest & dividend income, after tax payable by the fund	9.25
Realised and unrealised gains on plan assets (after tax)	2.00
Fund administrative costs	(1.00)
Expected Rate of Return	10.25

You are required to find the expected and actual returns on plan assets.

Question 10 : Rock Star Ltd.

Rock Star Ltd. discontinues a business segment. Under the agreement with employee's union, the employees of the discontinued segment will earn no further benefit. This is a curtailment without settlement, because employees will continue to receive benefits for services rendered before discontinuance of the business segment. Curtailment reduces the gross obligation for various reasons including change in actuarial assumptions made before curtailment. If the benefits are determined based on the last pay drawn by

employees, the gross obligation reduces after the curtailment because the last pay earlier assumed is no longer valid.

Rock Star Ltd. estimates the share of unamortized service cost that relates to the part of the obligation at Rs 18 (10% of Rs 180). Calculate the gain from curtailment and liability after curtailment to be recognised in the balance sheet of Rock Star Ltd. on the basis of given information:

a) Immediately before the curtailment, gross obligation is estimated at Rs 6,000 based on current actuarial assumption.

b) The fair value of plan assets on the date is estimated at Rs 5,100.

c) The unamortized past service cost is Rs 180.

d) Curtailment reduces the obligation by Rs 600, which is 10% of the gross obligation.

Question 11 : XYZ Ltd.

An employee Roshan has joined a company XYZ Ltd. in the year 20X1. The annual emoluments of Roshan as decided is Rs 14,90,210. The company also has a policy of giving a lump sum payment of 25% of the last drawn annual salary of the employee for each completed year of service if the employee retires after completing minimum 5 years of service. The salary of the Roshan is expected to grow @ 10% per annum.

The company has inducted Roshan in the beginning of the year and it is expected that he will complete the minimum five year term before retiring. Thus he will get 5 yearly increment.

What is the amount the company should charge in its Profit and Loss account every year as cost for the Defined Benefit obligation? Also calculate the current service cost and the interest cost to be charged per year assuming a discount rate of 8%.

(P.V factor for 8% - 0.735, 0.794, 0.857, 0.926, 1)

Question 12

A company has a scheme for payment of settlement allowance to retiring employees. Under the scheme, retiring employees are entitled to reimbursement of certain travel expenses for class they are entitled to as per company rule and to a lump-sum payment to cover expenses on food and stay during the travel. Alternatively, employees can claim a lump sum amount equal to one month pay last drawn.

The company's contentions in this matter are:

i) Settlement allowance does not depend upon the length of service of employee. It is restricted to employee's eligibility under the Travel rule of the company or where option for lump-sum payment is exercised, equal to the last pay drawn.

ii) Since it is not related to the length of service of the employees, it is accounted for on claim basis.

State whether the contentions of the company are correct as per relevant Accounting Standard. Give reasons in support of your answer.

Question 13 : 'X' Ltd.

The following data apply to 'X' Ltd. defined benefit pension plan for the year ended 31.03.20X2 calculate the actual return on plan assets:

Benefits Paid	Rs 2,00,000
Employers contribution	Rs 2,80,000
Fair market value of plan assets on 31.03.20X2	Rs 11,40,000
Fair market value of plan assets as on 31.03.20X1	Rs 8,00,000

Question 14 : Anupam Ltd.

The fair value of plan assets of Anupam Ltd. was Rs 2,00,000 in respect of employee benefit pension plan as on 1st April, 20X1. On 30th September, 20X1 the plan paid out benefits of Rs 25,000 and received inward contributions of Rs 55,000. On 31st March, 20X2 the fair value of plan assets was Rs 3,00,000. On 1st April, 20X1 the company made the following estimates, based on its market studies and prevailing prices.

	%
Interest and dividend income (after tax) payable by fund	10.25
Realized gains on plan assets (after tax)	3.00
Fund administrative costs	(3.00)
Expected rate of return	10.25

Calculate the expected and actual returns on plan assets as on 31st March, 20X2, as per AS 15.

8. OTHER LONG TERM BENEFITS :

Other long-term employee benefits include, for example:

1. long-term compensated absences such as long-service or sabbatical leave
2. jubilee or other long-service benefits
3. long-term disability benefits
4. profit-sharing and bonuses payable twelve months or more after the end of the period in which the employees render the related services and
5. deferred compensation paid twelve months or more after the end of the period in which it is earned.

9. TERMINAL BENEFITS :

Termination Benefits are employee benefits payable as a result of either an enterprise's decision to terminate an employee's employment before the normal retirement date or an employee's decision to accept voluntary redundancy in exchange for those benefits (e.g., payments under VRS). Termination benefits are recognized by an enterprise as a liability and an expense only when the enterprise has

i. a detailed formal plan for the termination which is duly approved, and

ii. a reliable estimate can be made of the amount of the obligation.

Where the termination benefits fall due within twelve months after the balance sheet date, an undiscounted amount of such benefits should be recognized as liability in the balance sheet with a corresponding charge to Profit & Loss Account. However, when the termination benefits fall due more than twelve months after the balance sheet date, such benefits should be discounted using an appropriate discount rate. Where an offer has been made to encourage voluntary redundancy, the termination benefits should be measured by reference to the number of employees expected to accept the offer. Where there is uncertainty with regard to the number of employees who will accept an offer of voluntary redundancy, a contingent liability exists and should be so disclosed as per AS 29 'Provisions, Contingent Liabilities and Contingent Assets'.

MCQs :

1. Gratuity and Pension would be examples of:
   (a) Short-term employee benefits (b) Long-term employee benefits
   (c) Post-employment benefits. (d) None of the above.
2. Non-accumulating compensating absence is commonly referred to as:
   (a) Earned Leave (b) Sick Leave
   (c) Casual leave (d) All of the above
3. The plans that are established by legislation to cover all enterprises and are operated by Governments include:
   (a) Multi-Employer plans (b) State plans
   (c) Insured Benefits (d) Employee benefit plan
4. Best estimates of the variable to determine the eventual cost of post-employment benefits is referred to as:
   (a) Employer's contribution (b) Actuarial assumptions
   (c) Cost to Company (d) Employee's contribution
5. Actuarial gains / losses should be:
   (a) Recognised through reserves
   (b) Charged over the expected life of employees
   (c) Charged immediately to Profit and Loss Statement
   (d) Do not charged to Profit and Loss Statement

Thanks ....

Rahul Malkan

Chapter 16

AS 16 – BORROWING COSTS

CHAPTER DESIGN

1. INTRODUCTION
2. BORROWING COST
3. QUALIFYING ASSET
4. CAPITALIZATION OF BORROWING COST
   - (A) SPECIFIC LOANS
   - (B) GENERAL LOANS
5. PERIOD OF CAPITALIZATION
   - (A) START OF CAPITALIZATION
   - (B) SUSPENSION OF CAPITALIZATION
   - (C) CESSATION OF CAPITALIZATION
6. DISCLOSURE

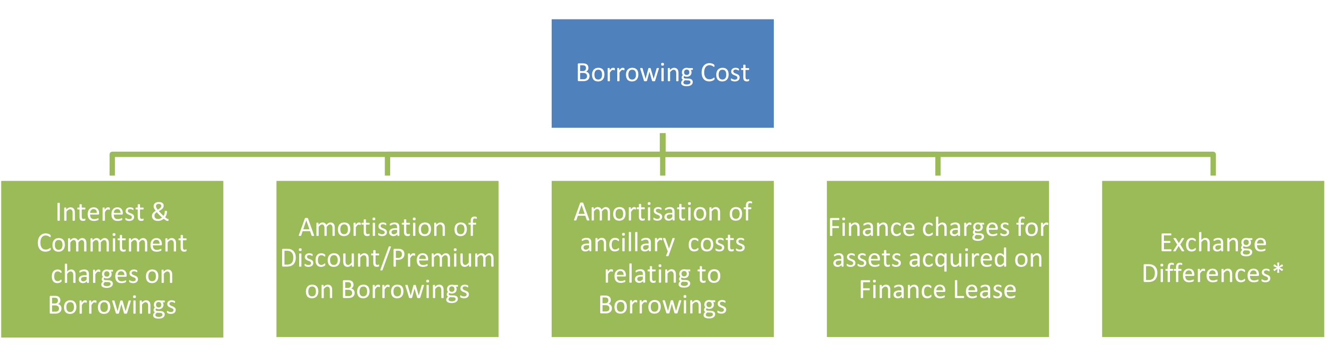
1. INTRODUCTION :

The objective of AS 16 is accounting for borrowing costs.

Borrowing cost → on qualifying Asset → should be capitalised

It does not deal with the actual or imputed cost of owners' equity, including preference share capital not classified as a liability.

2. BORROWING COST :



*To the extent they are regarded as an adjustment to interest cost

 # Exchange difference

Exchange differences arising from foreign currency borrowings to the extent that they are regarded as an adjustment to interest costs.

The adjustment should be of an amount which is equivalent to the extent to which the exchange loss does not exceed the difference between the cost of borrowing in functional currency when compared to the cost of borrowing in a foreign currency.

Question 1 :

An entity can borrow funds in its functional currency (Rs) @ 12%. It borrows $ 1,000 @ 4% on April 1, 2011 when $ 1 = Rs.40. The equivalent amount in functional currency is Rs.40,000. Interest is payable on March 31, 2012. On March 31, 2012, exchange rate is $ 1 = Rs.50. The loan is not due for repayment.

Calculate the amount of total borrowing cost.

Question 2 :

An entity can borrow funds in its functional currency (Rs) @ 12%. It borrows $ 1,000 @ 4% on April 1, 2011 when $ 1 = Rs.40. The equivalent amount in functional currency is

Rs.40,000. Interest is payable on March 31, 2012. On March 31, 2012, exchange rate is $ 1 = Rs.41. The loan is not due for repayment.
Calculate the amount of total borrowing cost.

3. QUALIFYING ASSETS :

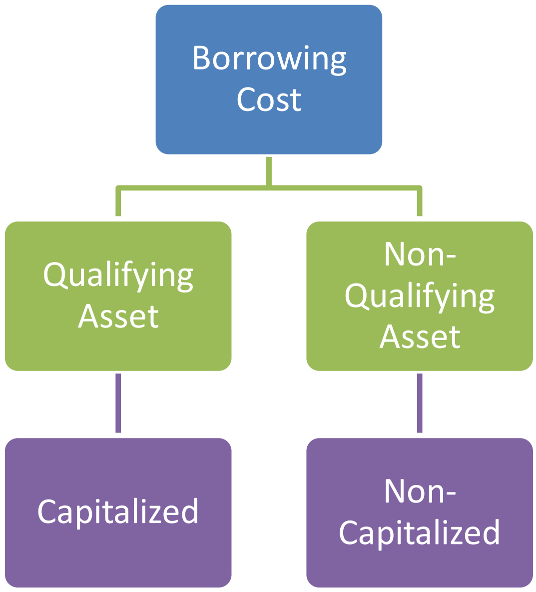
A qualifying asset is an asset that necessarily takes a substantial period of time to get ready for its intended use or sale.

Examples of qualifying assets are manufacturing plants, power generation facilities.

Note:

1. Inventories that require a substantial period of time to bring them to a saleable condition, and investment properties.
2. Other investments and those inventories that are routinely manufactured or otherwise produced in large quantities on a repetitive basis over a short period of time, are not qualifying assets.
3. Assets that are ready for their intended use or sale when acquired also are not qualifying assets.
4. substantial period of time primarily depends on the facts and circumstances of each case. It further states that, ordinarily, a period of twelve months is considered as substantial period of time unless a shorter or longer period can be justified on the basis of the facts and circumstances of the case

4. CAPITALIZATION OF BORROWING COST :



1. **Specific Borrowings :**

When an enterprise borrows funds specifically for the purpose of obtaining a particular qualifying asset, the borrowing costs that directly relate to that qualifying asset can be readily identified.

To the extent that funds are borrowed specifically for the purpose of obtaining a qualifying asset, the amount of borrowing costs eligible for capitalisation on that asset should be determined as the actual borrowing costs incurred on that borrowing during the period less any income on the temporary investment of those borrowings.

Question 3 : Alpha Ltd.

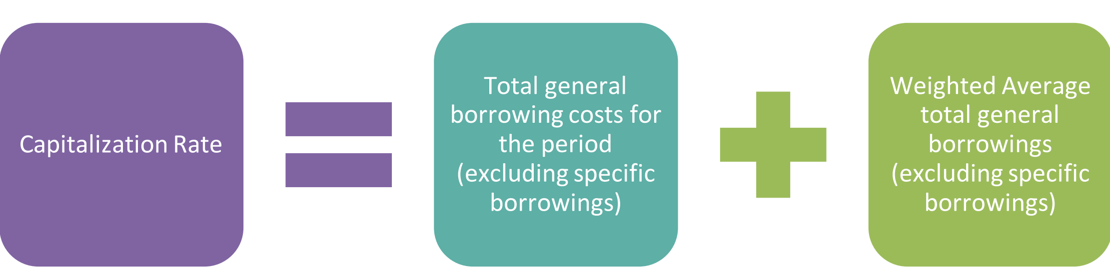
Alpha Ltd. on 1st April, 2011 borrowed 9% Rs.30,00,000 to finance the construction of two qualifying assets. Construction started on 1st April, 2011. The loan facility was availed on 1st April, 2011 and was utilized as follows with remaining funds invested temporarily at 7%.

	Factory Building	Office Building
1/4/2011	5,00,000	10,00,000
1/10/2011	5,00,000	10,00,000

Calculate the cost of the asset and the borrowing cost to be capitalized.

2. **General Borrowings :**

- When a qualifying asset is funded from a pool of general borrowings, the amount of the borrowing costs eligible for capitalisation is not so obvious. It may be difficult to identify a direct relationship between particular borrowings and a qualifying asset and to determine the borrowings that could otherwise have been avoided.
- To the extent that an entity borrows funds generally and uses them for the purpose of obtaining a qualifying asset, the entity shall determine the amount of borrowing costs eligible for capitalisation by applying a capitalisation rate to the expenditures on that asset.
- The capitalisation rate is the weighted average of the borrowing costs applicable to the borrowings of the entity that are outstanding during the period, other than borrowings made specifically for the purpose of obtaining a qualifying asset. The amount of borrowing costs that an entity capitalises during a period shall not exceed the amount of borrowing costs it incurred during that period.



Question 4 : Beta Ltd.

Beta Ltd. had the following loans in place at the end of 31st March, 2012:

Loan	01-04-2011	31-03-2012
18% Bank Loan	1000	1000
16% Term Loan	3000	3000
14% Debentures	-	2000

14% debenture was issued to fund the construction of Office building on 1st July, 2011 but the development activities has yet to be started.

On 1st April, 2011, Beta ltd began the construction of a Plant being qualifying asset using the existing borrowings. Expenditure drawn down for the construction was: Rs.500,000 on 1st April, 20X1 and Rs.2,500,000 on 1st January, 2012.

Required : Calculate the borrowing cost that can be capitalized for the plant.

Question 5 : X Limited

X Limited has a treasury department that arranges funds for all the requirements of the Company including funds for working capital and expansion programs. During the year ended March 31, 2012, the Company commenced the construction of a qualifying asset and incurred the following expenses:

Date	Amount (Rs)
July 1, 2011	2,50,000
December 1, 2011	3,00,000

The details of borrowings and interest thereon are as under:

Particulars	Average Balance	Interest (Rs.)
Long term loan @ 10%	10,00,000	1,00,000
Working Capital	5,00,000	65,000
Total	15,00,000	1,65,000

Compute the borrowing costs that need to be capitalised.

5. PERIOD OF CAPITALIZATION :

5.1 Commencement of Capitalization :

The capitalization of borrowing cost on qualifying asset should commence from "Commencement Date".

The commencement date is the date when entity first meets ALL the following conditions

1. It incurs expenditure on Asset
2. It incurs borrowing cost
3. It undertakes activities that are necessary to prepare the asset for its intended use or sale.

Question 6 : X Ltd

X Ltd is commencing a new construction project, which is to be financed by borrowing. The key dates are as follows:

(i) 15th May, 2011: Loan interest relating to the project starts to be incurred

(ii) 2nd June, 2011 : Technical site planning commences

(iii) 19th June, 2011 : Expenditure on the project started to be incurred

(iv) 18th July, 2011 : Construction work commences

Identify commencement date.

5.2. Suspension of Capitalization :

An entity is required to suspend the capitalization of borrowing cost during which there is No Active Development of Qualifying Asset.

An entity should not suspend the capitalization due to temporary delays, which are considered as regular for the development of qualifying asset.

5.3. Cessation of Capitalization :

An entity should cease capitalizing the borrowing cost when substantially all the activities necessary to prepare the qualifying asset for its intended use or sale are complete.

Note:

1. The activities are said to be completed when physical work related to asset is done, administration work might continue
2. Minor modification which are user specific should not be considered.
3. When construction of qualifying asset is undertaken in parts, we should cease the capitalization on the part which is completed only if that part is capable of independent use.

6. DISCLOSURE :

The financial statements should disclose:

a. The accounting policy adopted for borrowing costs; and

b. The amount of borrowing costs capitalised during the period.

PRACTICAL QUESTIONS :

Question 7 – X Ltd.

X Ltd. began construction of a new building on 1st January, 2016. It obtained Rs.1 lakh special loan to finance the construction of the building on 1st January, 2016 at an interest rate of 10%. The company's other outstanding two non-specific loans were:

Amount	Rate of Interest
Rs.5,00,000	11%
Rs.9,00,000	13%

The expenditures that were made on the building project were as follows:

		Rs.
January	2016	2,00,000
April	2016	2,50,000
July	2016	4,50,000
December	2016	1,20,000

Building was completed by 31st December, 2016. Following the principles prescribed in AS 16 'Borrowing Cost,' calculate the amount of interest to be capitalised and pass one Journal Entry for capitalising the cost and borrowing cost in respect of the building.

Question 8 : PRM Ltd.

PRM Ltd. obtained a loan from a bank for Rs. 50 lakhs on 30-04-2016. It was utilised as follows:

Particulars	Amount (Rs. in lakhs)
Construction of a shed	50
Purchase of a machinery	40
Working Capital	20
Advance for purchase of truck	10

Construction of shed was completed in March 2017. The machinery was installed on the date of acquisition. Delivery of truck was not received. Total interest charged by the bank for the year ending 31-03-2017 was Rs.18 lakhs. Show the treatment of interest.

Question 9 :

The company has obtained Institutional Term Loan of Rs.580 lakhs for modernisation and renovation of its Plant & Machinery. Plant & Machinery acquired under the modernisation scheme and installation completed on 31st March, 2017 amounted to Rs.406 lakhs, Rs.58 lakhs has been advanced to suppliers for additional assets and the balance loan of Rs.116 lakhs has been utilised for working capital purpose. The Accountant is on a dilemma as to how to account for the total interest of Rs.52.20 lakhs incurred during 2016-2017 on the entire Institutional Term Loan of Rs.580 lakhs.

Question 10 : Take Ltd.

Take Ltd. has borrowed Rs.30 lakhs from State Bank of India during the financial year 2016-2017. The borrowings are used to invest in shares of Give Ltd., a subsidiary company of Take Ltd., which is implementing a new project, estimated to cost Rs.50 lakhs. As on 31st March, 2017, since the said project was not complete, the directors of Take Ltd. resolved to capitalise the interest accruing on borrowings amounting to Rs.4 lakhs and add it to the cost of investments. Comment.

Question 11 : XYZ Ltd.

XYZ Ltd. , with a turnover of Rs.35 lakhs and borrowings of Rs.10 lakhs during any time in the previous year, wants to avail the exemptions available in adoption of Accounting Standards applicable to companies for the year ended 31.3.2017. Advise the management on the exemptions that are available as per the Companies (AS) Rules, 2006.

If XYZ is a partnership firm is there any other exemptions additionally available.

Question 12 : A company

A company was classified as Non-SMC in 2015-2016. In 2016-2017 it has been classified as SMC. The management desires to avail the exemption or relaxations available for SMCs in 2016-2017. However, the accountant of the company does not agree with the same. Comment.

Question 13 : Capital Cables Ltd.

Capital Cables Ltd., has a normal wastage of 4% in the production process. During the year 2016-17 the Company used 12,000 MT of raw material costing Rs. 150 per MT. At the end of the year 630 MT of wastage was in stock. The accountant wants to know how this wastage is to be treated in the books. Explain in the context of AS 2 (Revised) the treatment of normal loss and abnormal loss and also find out the amount of abnormal loss if any.

Question 14 : Mr. Mehul

Mr. Mehul gives the following information relating to items forming part of inventory as on 31-3-2017. His factory produces Product X using Raw material A.

(i) 600 units of Raw material A (purchased @ Rs.120). Replacement cost of raw material A as on 31-3-2017 is Rs.90 per unit.

(ii) 500 units of partly finished goods in the process of producing X and cost incurred till date Rs.260 per unit. These units can be finished next year by incurring additional cost of Rs.60 per unit.

(iii) 1500 units of finished Product X and total cost incurred Rs.320 per unit.

Expected selling price of Product X is Rs.300 per unit.

Determine how each item of inventory will be valued as on 31-3-2017. Also calculate the value of total inventory as on 31-3-2017.

Question 15 : Money Ltd.

Money Ltd., a non-financial company has the following entries in its Bank Account. It has sought your advice on the treatment of the same for preparing
Cash Flow Statement.

(i) Loans and Advances given to the following and interest earned on them:
  (1) to suppliers
  (2) to employees
  (3) to its subsidiaries companies
(ii) Investment made in subsidiary Smart Ltd. and dividend received
(iii) Dividend paid for the year
(iv) TDS on interest income earned on investments made
(v) TDS on interest earned on advance given to suppliers

Discuss in the context of AS 3 Cash Flow Statement.

Question 16 : ABC Ltd.

ABC Ltd. is installing a new plant at its production facility. It has incurred these costs:

1.	Cost of the plant (cost per supplier's invoice plus taxes)	Rs.25,00,000
2.	Initial delivery and handling costs	Rs.2,00,000
3.	Cost of site preparation	Rs.6,00,000
4.	Consultants used for advice on the acquisition of the plant	Rs.7,00,000
5.	Interest charges paid to supplier of plant for deferred credit	Rs.2,00,000
6.	Estimated dismantling costs to be incurred after 7 years	Rs.3,00,000
7.	Operating losses before commercial production	Rs.4,00,000

Please advise ABC Ltd. on the costs that can be capitalised in accordance with AS 10 (Revised).

Question 17 : Umesh

Explain briefly the accounting treatment needed in the following cases as per AS 11 as on 31.3.2017.

Trade receivables include amount receivable from Umesh Rs.5,00,000 recorded at the prevailing exchange rate on the date of sales, transaction recorded at US $ 1= Rs.58.50.

Long term loan taken from a U.S. Company, amounting to Rs.60,00,000. It was recorded at US $ 1 = Rs.55.60, taking exchange rate prevailing at the date of transaction.

US $ 1 = Rs.61.20 on 31.3.2017.

Question 18 : Supriya Ltd.

Supriya Ltd. received a grant of Rs.2,500 lakhs during the accounting year 2015-16 from government for welfare activities to be carried on by the company for its employees. The grant prescribed conditions for its utilisation. However, during the year 2016-17, it was found that the conditions of grants were not complied with and the grant had to be refunded to the government in full. Elucidate the current accounting treatment, with reference to the provisions of AS-12

Question 19 : Blue-chip Equity Investments Ltd.

Blue-chip Equity Investments Ltd., wants to re-classify its investments in accordance with AS 13 (Revised). State the values, at which the investments have to be reclassified in the following cases:

(i) Long term investments in Company A, costing Rs.8.5 lakhs are to be re-classified as current. The company had reduced the value of these investments to Rs.6.5 lakhs to recognise 'other than temporary' decline in value. The fair value on date of transfer is Rs.6.8 lakhs.

(ii) Long term investments in Company B, costing Rs.7 lakhs are to be re-classified as current. The fair value on date of transfer is Rs.8 lakhs and book value is Rs.7 lakhs.

(iii) Current investment in Company C, costing Rs.10 lakhs are to be re-classified as long term as the company wants to retain them. The market value on date of transfer is Rs.12 lakhs.

Question 20 : Amazing Construction Ltd.

On 1st April, 2016, Amazing Construction Ltd. obtained a loan of Rs.32 crores to be utilised as under :

(i)	Construction of sealink across two cities: (work was held up totally for a month during the year due to high water levels)	:	Rs.25 crores
(ii)	Purchase of equipments and machineries	:	Rs.3 crores
(iii)	Working capital	:	Rs.2 crores
(iv)	Purchase of vehicles	:	Rs.50,00,000
(v)	Advance for tools/cranes etc.	:	Rs.50,00,000
(vi)	Purchase of technical know-how	:	Rs.1 crores
(vii)	Total interest charged by the bank for the year en	:	Rs.80,00,000

Show the treatment of interest by Amazing Construction Ltd.

MCQs :

1. As per AS 16, all the following are qualifying assets except
   (a) Manufacturing plants and Power generation facilities
   (b) Inventories that require substantial period of time
   (c) Assets those are ready for sale.
   (d) None of the above
2. Which of the following statement is correct:
   (a) Entire exchange gain is reduced from the cost of the Qualifying asset.
   (b) Entire exchange loss is added to the cost of a Qualifying asset.
   (c) No adjustment is done for the exchange loss while computing cost of Qualifying asset.
   (d) None of the above
3. Capitalisation rate considers:
   (a) Borrowing costs on general borrowings only.
   (b) Borrowing costs on general and specific borrowings both.
   (c) Borrowing costs on specific borrowings only
   (d) None of the above
4. If the amount eligible for capitalisation in case of inventory as per AS 16 is Rs. 12,000 and cost of inventory is Rs. 40,000 and its net realizable value is Rs. 45,000; What amount can be capitalised as a part of inventory cost.
   (a) Rs. 12,000. (b) Rs. 5,000.
   (c) Rs. 7,000. (c) Rs. 10,000.
5. X Ltd is commencing a new construction project, which is to be financed by borrowing. The key dates are as follows:
   (i) 15th May, 20X1: Loan interest relating to the project starts to be incurred
   (ii) 2nd June, 20X1: Technical site planning commences
   (iii) 19th June, 20X1: Expenditure on the project started to be incurred
   (iv) 18th July, 20X1: Construction work commences

   Identify the commencement date for capitalisation under AS 16.
   (a) 15th May, 20X1. (b) 19th June, 20X1.
   (c) 18th July, 20X1. (d) 2nd June, 20X1

Thanks ....

Rahul Malkan

Chapter 17

AS 17 – SEGMENT REPORTING

CHAPTER DESIGN

1. INTRODUCTION
2. OBJECTIVE
3. SCOPE
4. BUSINESS SEGMENT
5. GEOGRAPHICAL SEGMENT
6. PRIMARY AND SECONDARY REPORTING FORMATS
7. MATRIX PRESENTATION
8. REPORTABLE SEGMENT
9. DISCLOSURES

1. INTRODUCTION :

This standard establishes principles for reporting financial information about different types of products and services an enterprise produces and different geographical areas in which it operates. The standard is more relevant for assessing risks and returns of a diversified or multi-locational enterprise which may not be determinable from the aggregated data.

2. OBJECTIVE :

Many enterprises provide groups of products and services or operate in geographical areas that are subject to differing rates of profitability, opportunities for growth, future prospects, and risks. The objective of this Standard is to establish principles for reporting financial information, about the different types of products and services an enterprise produces and the different geographical areas in which it operates. Such information helps users of financial statements:

(a) Better understand the performance of the enterprise;

(b) Better assess the risks and returns of the enterprise; and

(c) Make more informed judgements about the enterprise as a whole.

3. SCOPE :

AS 17 should be applied in presenting general purpose financial statements.

An enterprise should comply with the requirements of this Standard fully and not selectively. If a single financial report contains both consolidated financial statements and the separate financial statements of the parent, segment information need be presented only on the basis of the consolidated financial statements.

4. BUSINESS SEGMENT :

A business segment is a distinguishable component of an enterprise that is engaged in providing an individual product or service or a group of related products or services and that is subject to risks and returns that are different from those of other business segments.

Factors that should be considered in determining whether products or services are related include:

a. The nature of the products or services

b. The nature of the production processes

c. The type or class of customers for the products or services

d. The methods used to distribute the products or provide the services

e. If applicable, the nature of the regulatory environment, for example, banking, insurance, or public utilities

5. GEOGRAPHICAL SEGMENT :

A geographical segment is a distinguishable component of an enterprise that is engaged in providing products or services within a particular economic environment and that is subject to risks and returns that are different from those of components operating in other economic environments.

Factors that should be considered in identifying geographical segments include:

a. Similarity of economic and political conditions.
b. Relationships between operations in different geographical areas.
c. Proximity of operations.
d. Special risks associated with operations in a particular area.
e. Exchange control regulations and
f. The underlying currency risks.

6. PIMARY AND SECONDARY SEGMENT REPORTING FORMATS :

The dominant source and nature of risks and returns of an enterprise should govern whether its primary segment reporting format will be business segments or geographical segments.

If the risks and returns of an enterprise are affected predominantly by differences in the products and services it produces, its primary format for reporting segment information should be business segments, with secondary information reported geographically. Similarly, if the risks and returns of the enterprise are by the fact that it operates in different countries or other geographical areas, its primary format for reporting segment information should be geographical segments, with secondary information reported for groups of related products and services.

Internal organisation and management structure of an enterprise and its system of internal financial reporting to the board of directors and the chief executive officer should normally be the basis for identifying the predominant source and nature of risks and differing rates of return facing the enterprise and, therefore, for determining which reporting format is primary and which is secondary, except as provided paragraphs below:

a. If risks and returns of an enterprise are strongly affected both by differences in the products and services it produces and by differences in the geographical areas in which it operates, as evidenced by a 'matrix approach' to managing the company and to reporting internally to the board of directors and the chief executive officer, then the enterprise should use business segments as its primary segment reporting format and geographical segments as its secondary reporting forma; and
b. If internal organisational and management structure of an enterprise and its system of internal financial reporting to the board of directors and the chief executive officer are

based neither on individual products or services or groups of related products/services nor on geographical areas, it should be determined whether the risks and returns of the enterprise are related more to the products and services it produces or to the geographical areas in which it operates and accordingly, choose business segments or geographical segments as the primary segment reporting format of the enterprise, with the other as its secondary reporting format.

7. MATRIX PRESENTATION :

A 'matrix presentation' both business segments and geographical segments as primary segment reporting formats with full segment disclosures on each basis will often provide useful information if risks and returns of an enterprise are strongly affected both by differences in the products and services it produces and by differences in the geographical areas in which it operates. AS 17 does not require, but does not prohibit, a 'matrix presentation'.

8. REPOTABLE SEGMENTS :

A business segment or geographical segment should be identified as a reportable segment if:

a. Its revenue from sales to external customers and from transactions with other segments is 10% or more of the total revenue, external and internal, of all segments; or

b. Its segment result, whether profit or loss, is 10% or more of –
   (i) The combined result of all segments in profit, or
   (ii) The combined result of all segments in loss,
   (iii) Whichever is greater in absolute amount; or

c. Its segment assets are 10% or more of the total assets of all segments.

Question 1 :

The Chief Accountant of Sports Ltd. gives the following data regarding its six segments:

Particulars	M	N	O	P	Q	R	Total
Segment Assets	40	80	30	20	20	10	200
Segment Results	50	(190)	10	10	(10)	30	(100)
Segment Revenue	300	620	80	60	80	60	1,200

The Chief accountant is of the opinion that segments "M" and "N" alone should be reported. Is he justified in his view? Discuss.

9. DISCLOSURES :

Primary Reporting Format :

An enterprise should disclose the following for each reportable segment:

a. Segment revenue, classified into segment revenue from sales to external customers and segment revenue from transactions with other segments;

b. Segment result;
c. Total carrying amount of segment assets;
d. Total amount of segment liabilities;
e. Total cost incurred during the period to acquire segment assets that are expected to be used during more than one period (tangible and intangible fixed assets);
f. Total amount of expense included in the segment result for depreciation and amortisation in respect of segment assets for the period; and
g. Total amount of significant non-cash expenses, other than depreciation and amortisation in respect of segment assets that were included in segment expense and, therefore, deducted in measuring segment result.

Secondary Segment Information :

If primary format of an enterprise for reporting segment information is business segments, it should also report the following information:

a. Segment revenue from external customers by geographical area based on the geographical location of its customers, for each geographical segment whose revenue from sales to external customers is 10% or more of enterprise revenue;
b. The total carrying amount of segment assets by geographical location of assets, for each geographical segment whose segment assets are 10% or more of the total assets of all geographical segments; and
c. The total cost incurred during the period to acquire segment assets that are expected to be used during more than one period (tangible and intangible fixed assets) by geographical location of assets, for each geographical segment whose segment assets are 10% or more of the total assets of all geographical segments.

If primary format of an enterprise for reporting segment information is geographical segments (whether based on location of assets or location of customers), it should also report the following segment information for each business segment whose revenue from sales to external customers is 10% or more of enterprise revenue or whose segment assets are 10% or more of the total assets of all business segments:

a. Segment revenue from external customers;
b. The total carrying amount of segment assets; and
c. The total cost incurred during the period to acquire segment assets that are expected to be used during more than one period (tangible and intangible fixed assets).

Other Disclosures :

In measuring and reporting segment revenue from transactions with other segments, inter-segment transfers should be measured on the basis that the enterprise actually used to price

those transfers. The basis of pricing inter-segment transfers and any change therein should be disclosed in the financial statements.

Changes in accounting policies adopted for segment reporting that have a material effect on segment information should be disclosed. Such disclosure should include a description of the nature of the change, and the financial effect of the change if it is reasonably determinable.

PRACTICAL QUESTIONS :

Question 2 : M/s XYZ Ltd.

M/s XYZ Ltd. has three segments namely X, Y, Z. The total Assets of the Company are Rs 10.00 crores. Segment X has Rs 2.00 crores, segment Y has Rs 3.00 crores and segment Z has Rs 5.00 crores. Deferred tax assets included in the assets of each segments are X- Rs 0.50 crores, Y— Rs 0.40 crores and Z— Rs 0.30 crores. The accountant contends that all the three segments are reportable segments. Comment.

Question 3 : ABC Limited

ABC Limited has three segments viz. A, B and C. the total assets of the company is Rs.15 crores. The assets of Segment A is 1.85 cores, Segment B is 6.15 Crores and Segment C is Rs.7.00 Crores. Assets of each segment include deferred tax assets of Rs.0.50 Crores in A, Rs.0.40 Crores in B and Rs.0.30 Cores in C. the accountant of ABC Limited contends that all segments are reportable segments. Based on segment assets criteria. Determine the veracity of the contention of the accountant.

Question 4 : Diversifiers Ltd.

Prepare a segmental report for publication in Diversifiers Ltd. from the following details of the company's three divisions and the head office:

	RS '000
Forging Shop Division	
Sales to Bright Bar Division	4,575
Other Domestic Sales	90
Export Sales	6,135
	10,800
Bright Bar Division	
Sales to Fitting Division	
Export Sales to Rwanda	45
	300
	345
Fitting Division	

Export Sales to Maldives	
	270

Particulars	Head Office	Forging Shop Division	Bright Bar Division	Fitting Division
	Rs ('000)	Rs ('000)	Rs ('000)	Rs ('000)
Pre-tax operating result		**240**	**30**	**(12)**
Head office cost reallocated		**72**	**36**	**36**
Interest costs		**6**	**8**	**2**
Fixed assets	**75**	**300**	**60**	**180**
Net current assets	**72**	**180**	**60**	**135**
Long-term liabilities	**57**	**30**	**15**	**180**

Question 5 : AMF Ltd.

The senior Accountant of AMF Ltd. gives the following data regarding 5 segments

Particulars	P	Q	R	S	T	Total
Segment Assets	80	30	20	20	10	160
Segment Results	(190)	10	10	(10)	30	(150)
Segment Revenue	620	80	60	80	60	900

The senior accountant is of the opinion that segment 'P' alone should be reported. Is he justified in his view? Examine his opinion in the light of provision of AS 17 – Segment reporting?

MCQs :

1. As per AS 17, reportable segments are those whose total revenue from external sales and inter-segment sales is
   (a) 10% or more of the total revenue of all segments
   (b) 10% or more of the total revenue of all external segments
   (c) 12% or more of the total revenue of all segments
   (d) 12% or more of the total revenue of all external segments
2. Which of the following statements is correct?
   (a) Management has a discretion to include a segment as a reportable segment even if it passes the 10% materiality test.
   (b) Management has a discretion to include any segment as a reportable segment if it fails the 12% materiality test.
   (c) It is mandatory for the management to include the segment as a reportable segment if it passes the 10% materiality test.

(d) It is not mandatory for the management to include the segment as a reportable segment if it passes the 10% materiality test.

3. Which of the following statements is correct?
   (a) The overall test of 75% considers only external revenue to compute the threshold limit.
   (b) The overall test of 75% considers only internal revenue to compute the threshold limit.
   (c) The overall test of 75% considers both internal and external revenue to compute the threshold limit.
   (d) It is management choice whether they want to include both external and internal revenue for computing threshold limit.

4. Which of the following statements is correct?
   (a) The 10% test computed on the basis of revenue, considers both internal and external revenue to compute the threshold limit.
   (b) The 10% test computed on the basis of revenue, considers only external revenue to compute the threshold limit.
   (c) The 10% test computed on the basis of revenue, considers only internal revenue to compute the threshold limit.
   (d) It is management choice whether they want to include both external and internal revenue for computing threshold limit.

5. Which of the following statements is correct?
   (a) In case of 10% test based on profit/loss, we need to consider that any segment whose profit or loss is 10% or more than the net profit or net loss respectively of all segments taken together becomes reportable segment.
   (b) In case of 10% test based on profit/loss, we need to consider that any segment whose profit or loss is 10% or more than the net profit (after netting the losses) of all segments taken together becomes reportable segment.
   (c) In case of 10% test based on profit/loss, we need to consider that any segment whose profit or loss is 10% or more than the net profit or loss (whichever is higher in absolute figures) of all segments taken together becomes reportable segment.
   (d) In case of 10% test based on profit/loss, we need to consider that any segment whose profit or loss is 10% or more than the net profit or loss (whichever is lower in absolute figures) of all segments taken together becomes reportable segment.

Thanks ....

Rahul Malkan

Chapter 18

AS 18 – RELATED PARTY DISCLOSURES

CHAPTER DESIGN

1. INTRODUCTION
2. DEFINITIONS
3. RELATED PARTY
4. NOT RELATED PARTY
5. OTHER DEFINITIONS

1. INTRODUCTION :

AS 18 prescribes the requirements for disclosure of related party relationship and transactions between the reporting enterprise and its related parties. The requirements of the standard apply to the financial statements of each reporting enterprise as also to consolidated financial statements presented by a holding company.

2. DEFINITIONS :

1. **Related party transaction :** A transfer of resources or obligations between related parties, regardless of whether or not a price is charged.

2. **Control :**

(a) ownership, directly or indirectly, of more than one half of the voting power of an enterprise, or

(b) control of the composition of the board of directors in the case of a company or of the composition of the corresponding governing body in case of any other enterprise, or

(c) a substantial interest in voting power and the power to direct, by statute or agreement, the financial and/or operating policies of the enterprise.

For the purpose of AS 18, an enterprise is considered to **control the composition** of the board of directors of a company or governing body of an enterprise, if it has the power, without the consent or concurrence of any other person, to appoint or remove all or a majority of directors/members of the governing body of that company/enterprise. An enterprise is deemed to have the power to appoint a director/ member of the governing body, if any of the following conditions is satisfied:

(a) A person cannot be appointed as director/member of the governing body without the exercise in his favour by that enterprise of such a power as aforesaid or

(b) A person's appointment as director/member of the governing body follows necessarily from his appointment to a position held by him in that enterprise or

(c) The director/member of the governing body is nominated by that enterprise; in case that enterprise is a company, the director is nominated by that company/subsidiary thereof.

An enterprise/individual is considered to have a **substantial interest** in another enterprise if that enterprise or individual owns, directly or indirectly, 20% or more interest in the voting power of the other enterprise. Similarly, an individual is considered to have a substantial interest in an enterprise, if that individual owns, directly or indirectly, 20 per cent or more interest in the voting power of the enterprise.

3. **An Associate :** An enterprise in which an investing reporting party has significant influence and which is neither a subsidiary nor a joint venture of that party.

4. **Significant influence :** Participation in the financial and/or operating policy decisions of an enterprise, but not control of those policies.

5. **Key Management Personnel :** Those persons who have the authority and responsibility for planning, directing and controlling the activities of the reporting enterprise.

   For example, in the case of a company, the managing directors, whole time directors, manager and any person in accordance with whose directions or instructions the board of directors of the company is accustomed to act, are usually considered key management personnel.

   A non-executive director of a company should not be considered as a key management person by virtue of merely his being a director unless he has the authority and responsibility for planning, directing and controlling the activities of the reporting enterprise.
   The requirements of AS 18 should not be applied in respect of a non-executive director even if he participates in the financial and/or operating policy decision of the enterprise, unless he falls in any of the categories of 'related party relationships' discussed above.

6. **Relative :** In relation to an individual, means the spouse, son, daughter, brother, sister, father and mother who may be expected to influence, or be influenced by, that individual in his/her dealings with the reporting enterprise.

7. **Joint Venture :** a contractual arrangement whereby two or more parties undertake an economic activity which is subject to joint control.

8. **Joint Control :** the contractually agreed sharing of power to govern the financial and operating policies of an economic activity so as to obtain benefits from it.

9. **Holding Company :** a company having one or more subsidiaries.
   Subsidiary - a company :
   (a) in which another company (the holding company) holds, either by itself and/or through one or more subsidiaries, more than one-half, in nominal value of its equity share capital; or

(b) of which another company (the holding company) controls, either by itself and/or through one or more subsidiaries, the composition of its board of directors.

10. **Fellow subsidiary :** a company is considered to be a fellow subsidiary of another company if both are subsidiaries of the same holding company.

3. RELATED PARTY :

Related party - parties are considered to be related if at any time during the reporting period one party has the ability to control the other party or exercise significant influence over the other party in making financial and/or operating decisions.

AS 18 deals only with related party relationships described in (a) to (e) below:

a. Enterprises that directly, or indirectly through one or more intermediaries, control, or are controlled by, or are under common control with, the reporting enterprise (this includes holding companies, subsidiaries and fellow subsidiaries).

b. Associates and joint ventures of the reporting enterprise and the investing party or venturer in respect of which the reporting enterprise is an associate or a joint venture.

c. Individuals owning, directly or indirectly, an interest in the voting power of the reporting enterprise that gives them control or significant influence over the enterprise, and relatives of any such individual.

d. Key management personnel and relatives of such personnel and

e. Enterprises over which any person described in (c) or (d) is able to exercise significant influence. This includes enterprises owned by directors or major shareholders of the reporting enterprise and enterprises that have a member of key management in common with the reporting enterprise.

Question 1 : RM Ltd.

RM Ltd has two associates, X Ltd and Y Ltd and owns 25% of voting power of X Ltd and 30% of voting power of Y limited. Would X Limited be considered as related party to Y Ltd.

Question 2 : R Ltd.

R Ltd owns 70% of voting power of S Ltd. S Ltd in turns owns 50% of the voting interest in T Ltd. Further R Ltd also directly owns 15% of the voting interest in T Ltd. Would R Ltd deemed to have control over T Ltd or would it be only considered as exercising significant influence.

Question 3 :

Identify the related parties in the following cases as per AS 18

A Ltd. holds 51% of B Ltd.

B Ltd holds 51% of O Ltd.

Z Ltd holds 49% of O Ltd.

4. NON RELATED PARTY :

In the context of AS 18, the following are deemed not to be related parties:

a. Two companies simply because they have a director in common (unless the director is able to affect the policies of both companies in their mutual dealings).

b. A single customer, supplier, franchiser, distributor, or general agent with whom an enterprise transacts a significant volume of business merely by virtue of the resulting economic dependence and

c. The parties listed below, in the course of their normal dealings with an enterprise by virtue only of those dealings (although they may circumscribe the freedom of action of the enterprise or participate in its decision-making process):
   (i) Providers of finance
   (ii) Trade unions
   (iii) Public utilities
   (iv) Government departments and government agencies including government sponsored bodies

   Related party disclosure requirements as laid down in AS 18 do not apply in circumstances where providing such disclosures would conflict with the reporting enterprise's duties of confidentiality as specifically required in terms of a statute or by any regulator or similar competent authority.

5. OTHER DEFINITIONS :

Name of the related party and nature of the related party relationship where control exists should be disclosed irrespective of whether or not there have been transactions between the related parties.

This is to enable users of financial statements to form a view about the effects of related party relationships on the enterprise.

If there have been transactions between related parties, during the existence of a related party relationship, the reporting enterprise should disclose the following:

(i) The name of the transacting related party;

(ii) A description of the relationship between the parties;

(iii) A description of the nature of transactions;

(iv) Volume of the transactions either as an amount or as an appropriate proportion;

(v) Any other elements of the related party transactions necessary for an understanding of the financial statements;

(vi) The amounts or appropriate proportions of outstanding items pertaining to related parties at the balance sheet date and provisions for doubtful debts due from such parties at that date;

(vii) Amounts written off or written back in the period in respect of debts due from or to related parties.

Items of a similar nature may be disclosed in aggregate by type of related party except when separate disclosure is necessary for an understanding of the effects of related party transactions on the financial statements of the reporting enterprise.

PRACTICAL QUESTIONS :

Question 4 : Narmada Ltd.

Narmada Ltd. sold goods for Rs 90 lakhs to Ganga Ltd. during financial year ended 31-3-2017. The Managing Director of Narmada Ltd. own 100% of Ganga Ltd. The sales were made to Ganga Ltd. at normal selling prices followed by Narmada Ltd. The Chief accountant of Narmada Ltd contends that these sales need not require a different treatment from the other sales made by the company and hence no disclosure is necessary as per the accounting standard. Is the Chief Accountant correct?

Question 5 : X Limited

X Limited is a wholly owned subsidiary of Z Limited and a 50% co- venturer in joint venture XY. Whether transactions between joint venture XY and Z would require disclosures?

MCQs :

1. According to AS-18 Related Party Disclosures, which ONE of the following is not a related party of Skyline Limited?
   (a) A shareholder of Skyline Limited owning 30% of the ordinary share capital
   (b) An entity providing banking facilities to Skyline Limited in the normal course of business
   (c) An associate of Skyline Limited
   (d) Key management personnel of Skyline Limited

2. Are the following statements in relation to related parties true or false, according to AS-18 Related Party Disclosures?
   (A) A party is related to another entity that it is jointly controlled by.
   (B) A party is related to another entity that it controls.

Statement (A) Statement (B)

(a)	False	False
(b)	False	True
(c)	True	False
(d)	True	True

3. Which of the following is not a related party as envisaged by AS-18 Related Party Disclosures?
   (a) A director of the entity
   (b) The parent company of the entity
   (c) A shareholder of the entity that holds 1% stake in the entity
   (d) The spouse of the managing director of the entity
4. According to AS-18 Related Party Disclosures, related party transaction is a transfer of resources or obligations between related parties – provided a price is charged for such transfer.
   (a) True (b) False
5. According to AS-18 Related Party Disclosures, parties are considered to be related, if and only if at the end of the reporting period - one party has the ability to control the other party or exercise significant influence over the other party in making financial and/or operating decisions.
   (a) True (b) False

Thanks ....

Chapter 19

AS 19 – LEASES

CHAPTER DESIGN

1. INTRODUCTION
2. APPLICABILITY OF AS 19
3. DEFINITIONS
4. TYPES OF LEASES
5. INDICATORS OF FINANCE LEASE
6. ACCOUNTING IN BOOKS OF LESSEE
   (A) FINANCE LEASE
   (B) OPERATING LEASE
7. ACCOUNTING IN BOOKS OF LESSOR
   (A) FINANCE LEASE
   (B) OPERATING LEASE
   (C) MANUFACTURER OR DEALER LESSOR
8. SALE AND LEASE BACK

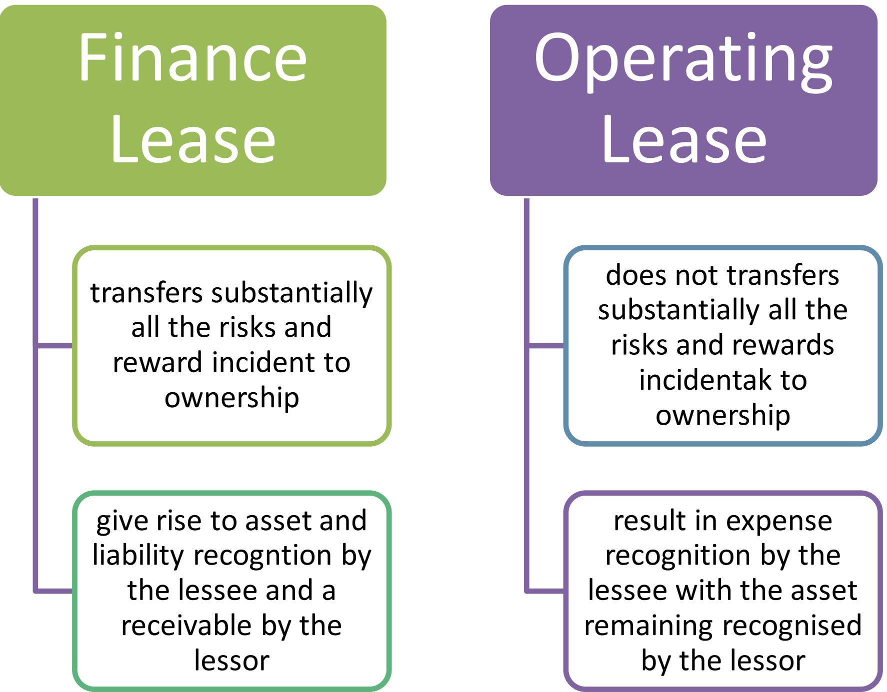
1. INTRODUCTION :

The objective of this Standard is to prescribe for lessees and lessors :

(i) the appropriate accounting policies to be used and

(ii) disclosures applicable to leases

Leases are required to be classified as



2. APPLICABILTY :

The standard applies to all leases other than:

(a) lease agreements to explore for or use of natural resources, such as oil, gas, timber metals and other mineral rights; and

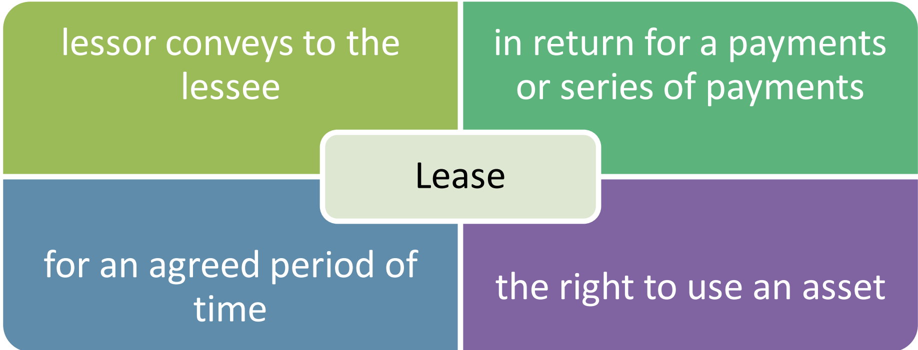
(b) licensing agreements for items such as motion picture films, video recordings, plays, manuscripts, patents and copyrights; and

(c) lease agreements to use lands

3. DEFINITIONS :

1. <u>LEASE :</u>

A *Lease* is an agreement whereby the Lessor *(legal owner of an asset)* conveys to the Lessee (another party) in return for a payment or series of periodic payments (Lease rents), the right to use an asset for an agreed period of time.

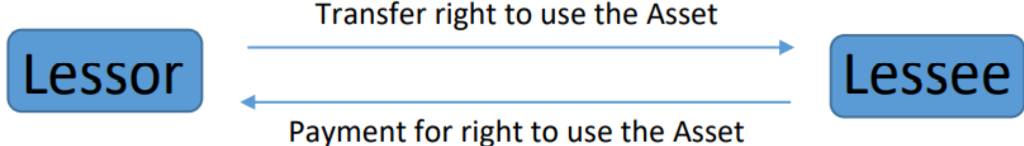


2. LESSOR :

Lessor is a party who gives the asset on lease and gets lease rent

3. LESSEE :

Lessee is one who takes the asset on lease and pays rent periodically or as per agreed terms



Question 1 : Moon & Sun legal Consultants Limited

Moon & Sun legal Consultants Limited has signed an agreement with a client for rendering consultancy services on monthly basis for 15 days per month for 2 years at a fees of Rs 1 million per annum. Is this agreement tantamount to a lease?

4. NON-CANCELLABLE LEASE :

A **non-cancellable lease** is a lease that is cancellable only:

(a) upon the occurrence of some remote contingency; or

(b) with the permission of the lessor; or

(c) if the lessee enters into a new lease for the same or an equivalent asset with the same lessor; or

(d) upon payment by the lessee of an additional amount such that, at inception, continuation of the lease is reasonably certain.

5. LEASE TERM :

The **lease term** is the non-cancellable period for which the lessee has agreed to take on lease the asset together with any further periods for which the lessee has the option to

continue the lease of the asset, with or without further payment, which option at the inception of the lease it is reasonably certain that the lessee will exercise.

Lease Term = Primary Lease term + Secondary Lease Term

6. INCEPTION OF LEASE :

The inception of the lease is the earlier of the date of the lease agreement and the date of commitment by the parties to the principal provisions of the lease. As at this date:

a) a lease is classified as either an operating or a finance lease; and

b) in the case of a finance lease, the amounts to be recognised at the commencement of the lease term are determined.

7. COMMENCEMENT OF LEASE :

The commencement of the lease term is the date from which the lessee is entitled to exercise its right to use the leased asset. It is the date of initial recognition of the lease (ie the recognition of the assets, liabilities, income or expenses resulting from the lease, as appropriate)

Example :

Inception of the Lease and Commencement of the lease A lessee may sign an agreement to lease a car on 31st March, 2018 but does not take delivery of the car until 30th June, 2018. Lease classification is made at the inception of the lease i.e. on 31st March, 2018. The recognition of the related assets, liabilities, income and expense in the financial statements will not take place until 30th June, 2018. Commencement of the lease will be on 30th June, 2018.

8. MINIMUM LEASE RENTALS :

Minimum lease payments are the payments over the lease term that the lessee is or can be required to make, excluding contingent rent, costs for services and taxes to be paid by and reimbursed to the lessor, together with:

a) for a lessee, any amounts guaranteed by
   - (i) the lessee or
   - (ii) by a party related to the lessee;

b) for a lessor, any residual value guaranteed to the lessor by:
   - (i) the lessee;
   - (ii) a party related to the lessee; or
   - (iii) a third party unrelated to the lessor that is financially capable of discharging the obligations under the guarantee

Note : However, if the lessee has an option to purchase the asset at a price that is expected to be sufficiently lower than fair value at the date the option becomes exercisable for it to be reasonably certain, at the inception of the lease, that the option will be exercised, the minimum lease payments comprise the minimum payments payable over the lease term to the expected date of exercise of this purchase option and the payment required to exercise it.

9. RESIDUAL VALUE :

Residual value of a leased asset is the estimated fair value of the asset at the end of the lease term.

10. ECONOMIC LIFE :

Economic life is either:

(a) the period over which an asset is expected to be economically usable by one or more users; or

(b) the number of production or similar units expected to be obtained from the asset by one or more users.

11. GUARANTEED RESIDUAL VALUE :

(a) in the case of the lessee, that part of the residual value which is guaranteed by the lessee or by a party on behalf of the lessee (the amount of the guarantee being the maximum amount that could, in any event, become payable); and

(b) in the case of the lessor, that part of the residual value which is guaranteed by or on behalf of the lessee, or by an independent third party who is financially capable of discharging the obligations under the guarantee.

12. UNGUARANTEED RESIDUAL VALUE :

Unguaranteed residual value of a leased asset is the amount by which the residual value of the asset exceeds its guaranteed residual value.

13. FAIR VALUE :

Fair value is the amount for which an asset could be exchanged or a liability settled between knowledgeable, willing parties in an arm's length transaction

Question 2 : A Ltd.

Calculate minimum lease payments for A Ltd. who took an asset on a 5 years lease from B Ltd. using the following information:

Payments over the lease term	Rs 1,000 per month
Contingent rent	Rs 20,000
Cost for services given by B Ltd.	Rs 40,000
Taxes to be reimbursed to B Ltd.	Rs 15,000
Residual value guaranteed by A Ltd.	Rs 5,000
Fair value of asset after 5 years	Rs 6,000

Also, A Ltd. has an option to purchase the asset after a period of 5 years at Rs 2,000. It is reasonably certain that A Ltd. will exercise the option.

Required Calculation Minimum Lease Payments.

14. GROSS INVESTMENT IN LEASE :

Gross investment in the lease is the aggregate of:

(a) the minimum lease payments receivable by the lessor under a finance lease, and

(b) any unguaranteed residual value accruing to the lessor.

15. NET INVESTMENT IN LEASE :

Net investment in the lease is the gross investment in the lease discounted at the interest rate implicit in the lease.

16. UNEARNED FINANCE LEASE :

Unearned finance income is the difference between:

(a) the gross investment in the lease, and

(b) the net investment in the lease.

Gross Investment → Less → Net Investment

Question 3 : X Ltd.

X Ltd. gave an asset on a finance lease to Y Ltd. Y Ltd. has to pay Rs 10,000 per annum for 5 years. Unguaranteed residual value accruing to X Ltd. is Rs 5,000. Interest rate implicit in the lease is 15%. Calculate MLP, gross investment, net investment and unearned finance income.

17. INITIAL DIRECT COST:

Initial direct costs are incremental costs that are directly attributable to negotiating and arranging a lease, except for such costs incurred by manufacturer or dealer lessors.

18. INTEREST RATE IMPLICIT TO LEASE :

The interest rate implicit in the lease is the discount rate that, at the inception of the lease, causes the aggregate present value of

a. the minimum lease payments and
b. the unguaranteed residual value to be equal to the sum of
   (i) the fair value of the leased asset and
   (ii) any initial direct costs of the lessor.

Question 4

Fair value of asset	Rs 90,000
Initial direct costs to the lessor	Rs 10,000
Annual lease payments (at year end)	Rs 25,000 for 6 years
Unguaranteed residual value at the end of 6 years	Rs 5,000

Calculate the rate implicit to the lease

19. INCREMENTAL BORROWING COST :

The lessee's incremental borrowing rate of interest is the rate of interest the lessee would have to pay on a similar lease or, if that is not determinable, the rate that, at the inception of the lease, the lessee would incur to borrow over a similar term, and with a similar security, the funds necessary to purchase the asset.

20. CONTINGENT RENT :

Contingent rent is that portion of the lease payments that is not fixed in amount but is based on the future amount of a factor that changes other than with the passage of time

(e.g. percentage of future sales, amount of future use, future price indices, future market rates of interest).

Question 5 : A car

A car is leased under a three year contract. The lease rentals during the three years are fixed provided the mileage does not exceed a maximum amount during that period. Any mileage incurred above the maximum is subject to an additional charge. How the minimum lease rentals should be calculated.

4. LEASE CLASSIFICATION :

A lease is classified as a finance lease if it transfers substantially all the risks and rewards incidental to ownership. A lease is classified as an operating lease if it does not transfer substantially all the risks and rewards incidental to ownership.

The classification of leases adopted in this Standard is based on the extent to which risks and rewards incidental to ownership of a leased asset lie with the lessor or the lessee

CHARACTERISTICS OF FINANCE LEASE :

Whether a lease is a finance lease or an operating lease depends on the substance of the transaction rather than the form of the contract.

(a) The lease transfers ownership of the asset to the lessee by the end of the lease term;

(b) The lessee has the option to purchase the asset at a price which is expected to be sufficiently lower than the fair value at the date the option becomes exercisable such that, at the inception of the lease, it is reasonably certain that the option will be exercised;

(c) The lease term is for the major part of the economic life of the asset even if title is not transferred;

(d) At the inception of the lease, present value of the minimum lease payments amounts to at least substantially all of the fair value of the leased asset; and

(e) The leased asset is of a specialized nature such that only the lessee can use it without major modifications being made.

5. INDICATORS OF FINANCE LEASE :

Additional Indicators of situations which individually or in combination could also lead to a lease being classified as a finance lease are:

(a) If the lessee can cancel the lease and the lessor’s losses associated with the cancellation are borne by the lessee;

(b) If gains or losses from the fluctuations in the residual value accrue to the lessee (for example if the lessor agrees to allow rent rebate equaling most of the disposal value of leased asset at the end of the lease); and

(c) If the lessee can continue the lease for a secondary period at a rent, which is substantially lower than market rent.

Question 7 : Sun Ltd.

On 1st April, 2011, Sun Ltd entered, as lessee, into a five-year non-cancellable lease of an equipment that has an economic life of ten years, at the end of which it is expected to have no value. At the inception of the lease, the fair value (cash cost) of the Equipment is Rs 1,00,000. On 31st March, for each of the first four years of the lease term the lessee is required to pay the lessor Rs 23,000. At the end of the lease term ownership of the Equipment passes to the lessee upon payment of the final lease payment of Rs 23,539. The interest rate implicit in the lease is 5 per cent per year, which approximates the lessee's incremental borrowing rate.

6. ACCOUNTING IN THE BOOKS OF LESSEE :

6.1 FINANCE LEASE :

1. Recognise finance lease as Asset and liabilities
   - leased asset as an asset and
   - obligation to pay future rentals as a liability.
2. At amount equal to lower of
   - fair value of the leased asset
   - the present value of the MLP.
3. The discount rate to be used in calculating the present value of the minimum lease payments is the interest rate implicit in the lease, if this is practicable to determine; if not, the lessee's incremental borrowing rate shall be used.
4. Any initial direct costs of the lessee are added to the amount recognised as an asset. The costs identified as directly attributable to activities performed by the lessee for a finance lease are added to the amount recognised as an asset.
5. It is not appropriate for the liabilities for leased assets to be presented in the financial statements as a deduction from the leased assets. If for the presentation of liabilities in the balance sheet a distinction is made between current and noncurrent liabilities, the same distinction is made for lease liabilities.
6. Any contingent Rent should be charged to Profit and Loss A/c.
7. Minimum lease payments are apportioned between the finance charge and the reduction of the outstanding liability.
8. The finance charge is allocated to each period during the lease term so as to produce a constant periodic rate of interest on the remaining balance of the liability. Contingent rents are recognised as expenses in the periods in which they are incurred.

9. Depreciation should be charged as per the Accounting Policy of the company
10. A lessee is also required to recognise any impairment of a leased asset. To determine whether a leased asset has become impaired, an entity applies Ind AS 36, Impairment of Assets.

Question 8 :

Annual lease rents	= RS 50,000 at the end of each year.
Lease period	= 5 years;
Guaranteed residual value	= Rs 25,000
Unguaranteed residual value (UGR)	= RS 15,000
Fair Value at the inception (beginning) of lease	= Rs 2,00,000
Interest rate implicit on lease is	=12.6%

Account the above lease in the books of the lessor.

Question 9 : S.K. Ltd.

S. Square Private Limited has taken machinery on finance lease from S.K. Ltd. The information is as under:

Lease term	= 4 years
Fair value at inception of lease	= Rs 20,00,000
Lease rent	= Rs 6,25,000 p.a. at the end of year
Guaranteed residual value	= Rs 1,25,000
Expected residual value	= Rs 3,75,000
Implicit interest rate	= 15%

Discounted rates for 1st year, 2nd year, 3rd year and 4th year are 0.8696, 0.7561, 0.6575 and 0.5718 respectively.

Calculate the value of the lease liability as per AS-19 and disclose impact of this on Balance sheet and Profit & loss account at the end of year 1

Question 10 : X Ltd.

X Ltd. Leased an Asset to RM Ltd from 1/1/2010 for the period of 3 years. The fair Value of the Machinery is Rs. 2,35,500. Calculate the interest rate implicit to the Lease. Lease Rentals are 100000 at the year end and GRV is 17000. Pass the journal entries in the books of RM Ltd. For year 1. Depreciation is charged @ 20% SLM.

Question 11 :

On 1st April, 2000, Venus ltd began to lease a property that was used in the production process. The lease was for 4 years and annual rental (payable in advance on 1st April each year) was Rs 20,00,000. The rate of interest implicit in this lease was 9% p.a. and the

present value of the minimum lease payments was very close to the fair value of the property at the inception of the lease, which was estimated at Rs 71,00,000.

Required: Explain the accounting treatment for the above property lease and produce appropriate extracts from the financial statements of Venus ltd for the year ended 31st March, 2012.

Question 12 : Sam Ltd.

Sam Ltd. Leased an Asset to Curran Ltd on the following terms

Fair Value of Asset	20,00,000
Life 5 years Lease Rentals	5,00,000 P.A
Guaranteed Residual Value	1,00,000
Estimated Residual Value	2,00,000
IRR	15%
Depreciation	10% SLM

Pass the journal entries in the books of Curran Ltd. for year 1 and also ascertain unearned Finance Income.

Question 13 :

Consider the following information

1.	Life	10 years
2.	Lease Rentals	Rs 60,000 P.A
3.	Other services	Rs 5,000 P.A
4.	IRR	10%
5.	PVIFA (10%, 10)	6.145

Find A. Lease liability at the inception of the lease by lessee assuming that fair value of lease is similar to PV of MLP B. Also give treatment of Rs. 5,000 payable.

Question 14 : RM Ltd.

RM Ltd took a machine on lease on the following terms

Annual Lease Rentals	Rs. 50,000
Lease period	13 years
IRR	15%

RM has an option of buying the Machinery at Rs. 75,000 at the end of the lease period which RM is reasonably certain to buy.

Find out the amount in which the finance lease be recognised in the books of RM Ltd.

6.2 OPERATING LEASE :

Lease payments (excluding costs for services such as insurance and maintenance) under an operating lease shall be recognised as an expense on a straight-line basis, even if the payments are not on that basis, over the lease term unless either:

a) another systematic basis is more representative of the time pattern of the user's benefit even if the payments to the lessors are not on that basis; or

b) the payments to the lessor are structured to increase in line with expected general inflation to compensate for the lessor's expected inflationary cost increases. If payments to the lessor vary because of factors other than general inflation, then this condition is not met.

Question 15 : X Ltd.

X Ltd gives a Machinery to Y Ltd. The Lease period is for 3 years. The life of the asset is 10 years. Lease Rental is 10,000 P.A. Pass the necessary journal entries.

Question 16 : XY Ltd.

XY Ltd gives a Machinery to YZ Ltd. The Lease period is for 3 years. The life of the asset is 10 years. Lease Rentals are 10,000, 20,000 and 30,000 respectively for 3 years. Pass the necessary journal entries.

Question 17 : XYZ Ltd.

XYZ Ltd gives a Machinery to ZYX Ltd. The Lease period is for 3 years. The life of the asset is 10 years. Lease Rent will be 10,000 for the first year. Lease rent shall increase by 10% every year to offset the inflation.

7. ACCOUNTING IN THE BOOKS OF LESSOR :

7.1 FINANCE LEASE :

1. Lessors are present Lease as a receivable at an amount equal to the net investment in the lease. (PV of Gross Investment in Lease).
2. Net Investment in Lease is Gross Investment in lease Less Unearned Finance Income.
3. For finance leases other than those involving manufacturer or dealer lessors, initial direct costs are included in the initial measurement of the finance lease receivable and reduce the amount of income recognised over the lease term.
4. No Depreciation is charged / No impairment of Asset / The receivables are subject to review for impairment

Question 18 :

A Ltd. has initiated a Lease for 3 years for machine costing 1,50,000 useful life 4 years. At the end of Lease asset would be reverted back to A Ltd. UGRV = 20,000 IRR = 10%

Find :

A. Annual Lease Rentals

B. Gross Investment in the Lease

C. Net Investment in the Lease

D. Unearned Finance Income

E. Journal entries from the point of view of A Ltd.

7.2 MANUFACTURER ALSO PROVIDING LEASING ACTIVITY :

At times inorder to increase the sales the manufacturer may also provide leasing agreement (Financing facility).

In such cases, AS 19 specifies

1. Profit on sale should be charged to Profit and Loss A/c
2. Finance Income should be spread over the period of the lease.

The following points should be considered

1. The sale value should be the lower of a. Fair value b. PV of MLP arrived at by applying commercial rate of interest.
2. Profit = Sales Revenue – Cost of Sales
3. An Initial Direct Cost should be charged to Profit and Loss. They are more like selling and distribution Expense.
4. Cost of sales = Cost /Carrying Amount – PV of unguaranteed Residual Value.

Question 19 : RM

RM is the manufacturer of Industrial Pumps. It offer them for outright sales as well as lease arrangement.

Normal Selling Price	Rs 20,00,000
Lease Rentals	Rs. 6,00,000 P.A Lease term 5 years (it covers the useful life of the asset)
Cost of Sale	Rs. 16,00,000
Residual Value	Nil
IRR	15.24%

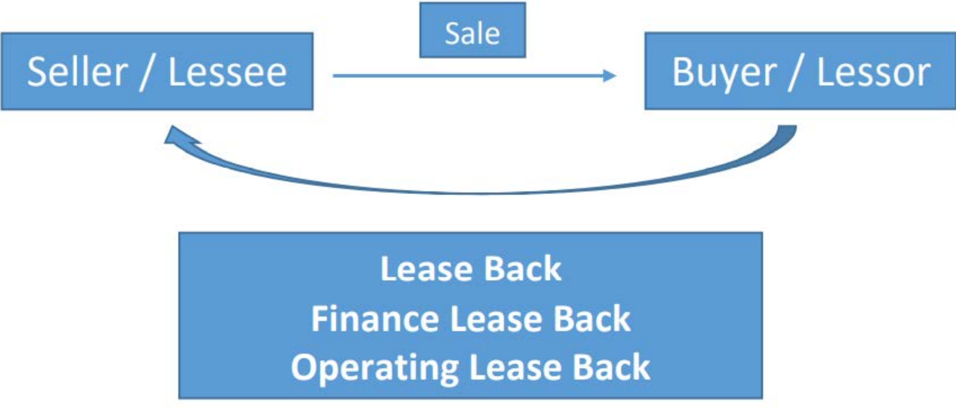
How should the total profit be distinguished between normal profit and finance income?

7.3 OPERATING LEASE :

1. Lessors are required to present assets subject to operating leases in their balance sheet according to the nature of the asset.
2. Lease income from operating leases (excluding amounts for services such as insurance and maintenance) shall be recognised in income on a straight-line basis (even if the receipts are not on such a basis) over the lease term, unless either:
   a) another systematic basis is more representative of the time pattern in which use benefit derived from the leased asset is diminished, even if the payments to the lessors are not on that basis; or
   b) the payments to the lessor are structured to increase in line with expected general inflation to compensate for the lessor's expected inflationary cost increases. If payments to the lessor vary according to factors other than inflation, then this condition is not met.
3. The depreciation policy for depreciable leased assets shall be consistent with the lessor's normal depreciation policy for similar assets, and depreciation shall be calculated in accordance with Ind AS 16 and Ind AS 38.
4. To determine whether a leased asset has become impaired, an entity applies Ind AS 36.
5. Costs, including depreciation, incurred in earning the lease income are recognised as an expense.
6. Initial direct costs incurred by lessors in negotiating and arranging an operating lease shall be added to the carrying amount of the leased asset and recognised as an expense over the lease term on the same basis as the lease income.

8. SALE AND LEASE BACK :

A sale and leaseback transaction involves the sale of an asset and the leasing back of the same asset. The lease payment and the sale price are usually interdependent because they are negotiated as a package. The accounting treatment of a sale and leaseback transaction depends upon the type of lease involved.



The point to be discussed is about the sale, i.e how should the profit be recognised. The lease should be accounted as per rules we have discussed above. Yes but the recognition of the profit depends of the nature of Lease back i.e if it is Finance Lease or Its an Operating Lease.

FINANCE LEASEBACK :

The excess or deficiency of sales proceeds over the carrying amount should be deferred and amortised over the lease term in proportion to the depreciation of the leased asset.

Question 20 : Santa

On 1st Jan 2011, Santa sold equipment for Rs 614460. The carrying amount of the equipment on the date was Rs. 1,00,000. The sale was part of the package under which banta Ltd. leased the asset to santa ltd for 10 years term. The economic life of asset is estimated at 10 years. The minimum lease rents payable by the lessee has been fixed at Rs. 1,00,000 payable annually beginning 31st December, 2011. The incremental borrowing interest rate of santa ltd. is estimated at 10% P.A. Calculate the net effect on the profit and loss in the books of santa Ltd.

OPERATING LEASEBACK :

If a sale and leaseback transaction results in an operating lease, it is necessary to determine the fair value of the asset and compare this with the contract sale price. Because the sale and lease transactions are connected, the sale may have been arranged at other than fair value, with the impact of any difference being recognised in the rentals payable.

Case 1: Sale price = Fair Value

Profit or loss should be recognised immediately.

Case 2: Sale Price < Fair Value

Profit and loss should be recognised immediately. However if the loss is compensated by future lease payments at below market price, it should be deferred and amortised in proportion to the lease payments over the period for which the asset is expected to be used.

Case 3: Sale Price > Fair Value

The excess over fair value should be deferred and amortised over the period for which the asset is expected to be used.

Question 21 : A Ltd.

A Ltd. sold machinery having WDV of Rs 40 lakhs to B Ltd. forRs 50 lakhs and the same machinery was leased back by B Ltd. to A Ltd. The lease back is operating lease.

Comment if –

(a) Sale price of Rs 50 lakhs is equal to fair value.

(b) Fair value is Rs 60 lakhs.

(c) Fair value is Rs 45 lakhs and sale price is Rs 38 lakhs.

(d) Fair value is Rs 40 lakhs and sale price is Rs 50 lakhs.

(e) Fair value is Rs 46 lakhs and sale price is Rs 50 lakhs

(f) Fair value is Rs 35 lakhs and sale price is Rs 39 lakhs.

Question 22 :

X Ltd. sold JCB Machine having WDV of Rs 50 Lakhs to Y Ltd. for Rs 60 Lakhs and the same JCB was leased back by Y Ltd. to X Ltd. The lease is operating lease. Comment according to relevant Ind AS if:

(a) Sale price of Rs 60 Lakhs is equal to fair value.

(b) Fair value is Rs 50 Lakhs and sale price is Rs 45 Lakhs.

(c) Fair value is Rs 55 Lakhs and sale price Rs 62 Lakhs.

(d) Fair value is Rs 45 Lakhs and sale price is Rs 48 Lakhs.

MCQs :

1. A Ltd. sold machinery having WDV of Rs. 40 lakhs to B Ltd. for Rs. 50 lakhs (Fair value Rs. 50 lakhs) and same machinery was leased back by B Ltd. to A Ltd. The lease back is in nature of operating lease. The treatment will be
   (a) A Ltd. should amortise the profit of Rs. 10 lakhs over lease term.
   (b) A Ltd. should recognise the profit of Rs. 10 lakhs immediately.
   (c) A Ltd. should defer the profit of Rs. 10 lakhs.
   (d) B Ltd. should recognise the profit of Rs. 10 lakhs immediately.
2. In case of an operating lease – identify which statement is correct:
   (a) The lessor continues to show the leased asset in its books of accounts.
   (b) The lessor de-recognises the asset from its Balance Sheet.
   (c) The lessor discontinues to claim depreciation in its books.
   (d) The lessee recognises the asset in its Balance Sheet.
3. In case of finance lease, if the asset is returned back to the lessor at the end of the lease term - the lessee always claims depreciation based on which of the following:
   (a) Useful life.
   (b) Lease term.
   (c) Useful life or lease term whichever is less.

(d) Useful life or lease term whichever is higher.

4. AS 19 lays down 5 deterministic conditions to classify the lease as a finance lease. To classify the lease as an operating lease – which statement is correct?
   (a) Any 1 condition fails.
   (b) Majority of the 5 conditions fail.
   (c) All 5 conditions fail.
   (d) Any 2 conditions fails.

5. The basis of classification of a lease is:
   (a) Control Test.
   (b) Risk and reward Test.
   (c) Both control test and risk and reward test.
   (d) Only reward Test

Thanks ....

Chapter 20

AS 20 – EARNINGS PER SHARE

CHAPTER DESIGN

1. INTRODUCTION
2. BASIC EARNING PER SHARE
   A. NUMERATOR = PROFITS ATTRIBUTED TO EQUITY SHAREHOLDERS
   B. DENOMINATOR = WEIGHTED AVERAGE NUMBER OF SHARES OUTSTANDING (WANOES)
      (I) FRESH ISSUE / BUY BACK
      (II) PARTLY PAID UP SHARES
      (III) BONUS ISSUE / SHARE SPLIT / SHARE CONSOLIDATION
      (IV) RIGHT ISSUE
3. DILUTED EARNINGS PER SHARE
   A. NUMERATOR = PROFIT ATTRIBUTED TO EQUITY SHAREHOLDERS
   B. DENOMINATOR = WEIGHTED AVERAGE NUMBER OF SHARES OUTSTANDING (WANOES)
4. RESTATEMENT
5. PRESENTATION
6. DISCLOSURE

1. INTRODUCTION :

Earnings per share (EPS) is a financial ratio indicating the amount of profit or loss for the period attributable to each equity share and AS 20 gives computational methodology for determination and presentation of basic and diluted earnings per share.

The objective of AS 20 is to describe principles for determination and presentation of earnings per share which will improve comparison of performance among different enterprises for the same period and among different accounting periods for the same enterprise.

This Accounting Standard is mandatory for all companies. However, disclosure of diluted earnings per share (both including and excluding extraordinary items) is not mandatory for SMCs. Such companies are however encouraged to make these disclosures.

In consolidated financial statements, the information required by AS 20 should be presented on the basis of consolidated information.

2. BASIC EARNINGS PER SHARE :

Basic earnings per share is calculated as = $\frac{\text{Net profit (loss) attributable to equity shareholders}}{\text{Weighted average number of equity shares outstanding during the period}}$

A. Numerator = Profits attributed to Equity Shareholders :

1. All items of income and expense which are recognized in a period, including tax expense and extraordinary items, are included in the determination of the net profit or loss for the period unless AS 5 requires or permits otherwise.
2. The amount of preference dividends and any attributable tax thereto for the period is deducted from the net profit for the period
3. The amount of preference dividends for the period that is deducted from the net profit for the period is:
   a. The amount of any preference dividends on non-cumulative preference shares provided for in respect of the period; and
   b. The full amount of the required preference dividends for cumulative preference shares for the period, whether or not the dividends have been provided for. The amount of preference dividends for the period does not include the amount of any preference dividends for cumulative preference shares paid or declared during the current period in respect of previous periods.

4. If an enterprise has more than one class of equity shares, net profit or loss for the period is apportioned over the different classes of shares in accordance with their dividend rights.

B. Denominator = Weighted Average Number of Shares Outstanding (WANOES)

The number of shares used in the denominator for basic EPS should be the weighted average number of equity shares outstanding during the period.

(i) Fresh Issue / Buy Back

Question 1 :

Calculate Weighted Number of shares

Date	Particulars	Issue	Buy Back	Balance
1st Jan	Balance at the beginning of the year	-	-	1800
31st May	Issue of shares for cash	600	-	2400
1st Nov	Buy Back of shares	-	300	2100

In most cases, shares are included in the weighted average number of shares from the date the consideration is receivable, for example:

a. Equity shares issued in exchange for cash are included when cash is receivable;

b. Equity shares issued as a result of the conversion of a debt instrument to equity shares are included as of the date of conversion;

c. Equity shares issued in lieu of interest or principal on other financial instruments are included as of the date interest ceases to accrue;

d. Equity shares issued in exchange for the settlement of a liability of the enterprise are included as of the date the settlement becomes effective;

e. Equity shares issued as consideration for the acquisition of an asset other than cash are included as of the date on which the acquisition is recognised; and

f. Equity shares issued for the rendering of services to the enterprise are included as the services are rendered.

(ii) Partly Paid up shares :

Partly paid equity shares are treated as a fraction of an equity share to the extent that they were entitled to participate in dividends relative to a fully paid equity share during the reporting period.

Question 2 :

Date	Particulars	No. of shares	Face Value	Paid up Value
1st Jan	Balance at the beginning of the year	1800	10	10
31st Oct	Issue of shares	600	10	5

Where an enterprise has equity shares of **different nominal values** but with the same dividend rights, the number of equity shares is calculated by converting all such equity shares into equivalent number of shares of the same nominal value.

(iii) Bonus issue, Share split and Right Issue:

Equity shares may be issued, or the number of shares outstanding may be reduced, without a corresponding change in resources. Examples include:

a. A bonus issue;
b. A bonus element in any other issue, for example a bonus element in a rights issue to existing shareholders;
c. A share split; and
d. A reverse share split (consolidation of shares).

(a) Bonus / Share split / Share consolidation :

In case of a **bonus issue or a share split,** equity shares are issued to existing shareholders for no additional consideration. Therefore, the number of equity shares outstanding is increased without an increase in resources.

The number of equity shares outstanding before the event is adjusted for the proportionate change in the number of equity shares outstanding as if the event had occurred at the beginning of the earliest period reported means along with the impact to current year adjustment, it will also impact the calculation of EPS of last year retrospectively.

Question 3 :

Net profit for the year 2020	Rs 18,00,000
Net profit for the year 2021	Rs 60,00,000
No. of equity shares outstanding until 30th September 2021	20,00,000

Bonus issue 1st October 2021 was 2 equity shares for each equity share outstanding at 30th September, 2021

Calculate Basic Earnings Per Share.

(b) Right Issue :

In a **rights issue**, the exercise price is often less than the fair value of the shares. Therefore, a rights issue usually includes a bonus element. So we are required to split the right issue into bonus and fresh issue.

Right issue = Bonus issue + Fresh Issue

To split the right issue we are required to calculate adjustment factor:

$$\text{Adjustment factor} = \frac{\text{Fair value per share immediately prior to the exercise of rights}}{\text{Theoretical ex-rights fair value per share}}$$

The theoretical ex-rights fair value per share is calculated by adding the aggregate fair value of the shares immediately prior to the exercise of the rights to the proceeds from the exercise of the rights, and dividing by the number of shares outstanding after the exercise of the rights.

Question 4 :

Net profit for the year 2020	Rs 11,00,000
Net profit for the year 2021	Rs 15,00,000
No. of shares outstanding prior to rights issue	5,00,000 shares
Rights issue price	Rs 15.00
Last date to exercise rights	1st March 2021

Rights issue is one new share for each five outstanding (i.e. 1,00,000 new shares)

Fair value of one equity share immediately prior to exercise of rights on 1st March 2021 was Rs 21.00. Compute Basic Earnings Per Share.

3. DILUTED EARNINGS PER SHARE :

In calculating diluted earnings per share, effect is given to all dilutive potential equity shares that were outstanding during the period

A. Profits available for Equity share holders :

The net profit for the period attributable to equity shares is:

i. Increased by the amount of dividends recognised in the period in respect of the dilutive potential equity shares as adjusted for any attributable change in tax expense for the period;

ii. Increased by the amount of interest recognised in the period in respect of the dilutive potential equity shares as adjusted for any attributable change in tax expense for the period; and

iii. Adjusted for the after-tax amount of any other changes in expenses or income that would result from the conversion of the dilutive potential equity shares.

B. Weighted Average Number of shares :

The weighted average number of equity shares outstanding during the period is increased by the weighted average number of additional equity shares which would have been outstanding assuming the conversion of all dilutive potential equity shares.

Question 5 :

Net profit for the current year	Rs 1,00,00,000
No. of equity shares outstanding	50,00,000
Basic earnings per share	Rs 2.00
No. of 12% convertible debentures of Rs 100 each	1,00,000
Each debenture is convertible into 10 equity shares	
Interest expense for the current year	Rs 12,00,000
Tax relating to interest expense (30%)	Rs 3,60,000

Question 6 :

Net profit for the year 2021	RS 12,00,000
Weighted average number of equity shares outstanding during the year 2021	5,00,000 shares
Average fair value of one equity share during the year 2021	Rs 20.00
Weighted average number of shares under option during the year 2021	1,00,000 shares
Exercise price for shares under option during the year 2021	RS 15.00

4. RESTATEMENT :

If the number of equity or potential equity shares outstanding increases as a result of a bonus issue or share split or decreases as a result of a reverse share split (consolidation of shares), the calculation of basic and diluted earnings per share should be adjusted for all the periods presented. If these changes occur after the
balance sheet date but before the date on which the financial statements are approved by the board of directors, the per share calculations for those financial statements and any prior period financial statements presented should be based on the new number of shares. When per share calculations reflect such changes in the number of shares, that fact should be disclosed.

5. PRESENTATION :

An enterprise should present basic and diluted earnings per share on the face of the statement of profit and loss for each class of equity shares that has a different right to share in the net profit for the period. An enterprise should present basic and diluted earnings per share with equal prominence for all periods presented. AS 20 requires an enterprise to present basic and diluted earnings per share, even if the amounts disclosed are negative (a loss per share).

6. DISCLOSURE :

An enterprise should disclose the following:

a. Where the statement of profit and loss includes extraordinary items (as defined is AS 5), basic and diluted EPS computed on the basis of earnings excluding extraordinary items (net of tax expense);

b. The amounts used as the numerators in calculating basic and diluted earnings per share, and a reconciliation of those amounts to the net profit or loss for the period;

c. The weighted average number of equity shares used as the denominator in calculating basic and diluted earnings per share, and a reconciliation of these denominators to each other; and

d. The nominal value of shares along with the earnings per share figures.

If an enterprise discloses, in addition to basic and diluted earnings per share, per share amounts using a reported component of net profit other than net profit or loss for the period attributable to equity shareholders, such amounts should be calculated using the weighted average number of equity shares determined in accordance with AS 20. If a component of net profit is used which is not reported as a line item in the statement of profit and loss, a reconciliation should be provided between the component used and a line item which is reported in the statement of profit and loss. Basic and diluted per share amounts should be disclosed with equal prominence.

PRACTICAL QUESTIONS :

Question 7 :

Calculate WANOES from the following information.

Date	Particulars	Issue	Buy Back	Balance
1st April, 2020	Balance at the beginning of the year	-	-	3,60,000
31st August, 2020	Issue of shares for cash	1,20,000	-	4,80,000
1st Feb, 2021	Buy Back of shares	-	60,000	4,20,000

Question 8 :

Net profit for year 2019-20	Rs 3,60,000
Net profit for year 2020 -21	Rs 12,00,000
No of equity shares outstanding till 31st Dec 20	4,00,000

Bonus was issued on 1st Jan, 2021. 2 equity shares were issued for each equity share outstanding on 31st Dec, 2010. Calculate Basic EPS from the following information as per AS 20.

Question 9 : RM Ltd.

RM Ltd. Issues Rs 2,00,000, 10% convertible debentures were issued which are convertible into 8000 equity shares. Net profit for the current year is Rs 1,00,000. WANOES outstanding for the current year is 50,000 and tax rate is 40%. Calculate basic EPS and Diluted EPS.

Question 10 : RS Ltd.

In 2020, RS Ltd, reported net income of Rs 2,00,000 and had 20,000 equity shares during the entire year, RM Ltd. also had outstanding during all of 2010 the following convertible securities

1. 6% convertible preference shares of Rs 100 face value, 1000 shares, each share is convertible into 15 equity shares.
2. Convertible debentures, 15%, Rs 1,00,000, Rs 1000 debentures, convertible into 10 shares.

Assume tax rate of 40%.

Calculate Basic EPS and Diluted EPS.

Question 11 : MR Ltd.

MR Ltd supplied the following information. You are required to compute the basic earnings per share.

Net profit	: Accounting year 2019	: Rs 20,00,000
	: Accounting year 2020	: Rs 30,00,000
No of shares prior to right issue	: 10,00,000 shares	
Right issue	: One share for every 4 shares outstanding	
Right issue price	: Rs 20	
Date for exercise of right issue	: 31/3/2020	
Fair value of share immediately prior to right issue		: Rs 25

Question 12 :

From the following information given below for a company, you are required to compute the Basic and Diluted EPS for the accounting year 2020-21 and the adjusted EPS for the year 2019-20. Assuming that the company is a listed company in India.

Net profit for year ended 31st March 2020 Rs 75,50,000

Net profit for year ended 31st March 2021 Rs 1,00,25,000
No of equity shares as on 1st April 2020 50,00,250
Bonus issue on 1st Jan 2020 1 share for every 2 shares held
No of 12% convertible debentures of Rs 100 each issued
On 1st jan 2015 1,00,000
Conversion ratio of debentures 10 shares per debentures
Tax rate 30%

Question 13 : Atmanirbhar Ltd.

From the following information given by Atmanirbhar Ltd. Calculate basic EPS and Diluted EPS as per AS 20.

	Rs
Net profit for the current year	2,50,00,000
No of equity shares outstanding	50,00,000
No of 12% convertible debentures of Rs 100 each	50,000
Each debenture is convertible into 8 equity shares	
Interest expenses for the current year	6,00,000
Tax savings relating to interest expenses (30%)	1,80,000

Question 14 : Q Ltd.

Following information is supplied by Q Ltd.
Number of shares outstanding prior to right issue – 2,50,000 shares
Right issue – two shares for every 5 shares outstanding
Right issue price – Rs 98 per share
Fair value of one equity share immediately prior to exercise of right on 30/6/2020 is Rs.102.
Net profit to equity shareholders
2019 – 2020 – Rs 50,00,000
2020 – 2021 – Rs 75,00,000
You are required to calculate the basic earnings per share as per AS – 20.

Question 15 : Nish Ltd.

The following information is given to us by Nish Ltd.
Number of shares outstanding : 5,00,000
Right issue : 2 for 5
Fair value before right : Rs 34
Right issue price : Rs 20
Calculate :

1. Theoretical ex-right fair value
2. Adjustment factor.

MCQs :

1. AB Company Ltd. had 1,00,000 shares of common stock outstanding on January 1. Additional 50,000 shares were issued on July 1, and 25,000 shares were reacquired on September 1. The weighted average number of shares outstanding during the year on Dec. 31 is
   (a) 1,40,000 shares (b) 1,25,000 shares
   (c) 1,16,667 shares (d) 1,20,000 shares
2. As per AS 20, potential equity shares should be treated as dilutive when, and only when, their conversion to equity shares would
   (a) Decrease net profit per share from continuing ordinary operations.
   (b) Increase net profit per share from continuing ordinary operations.
   (c) Make no change in net profit per share from continuing ordinary operations.
   (d) Decrease net loss per share from continuing ordinary operations.
3. As per AS 20, equity shares which are issuable upon the satisfaction of certain conditions resulting from contractual arrangements are
   (a) Dilutive potential equity shares (b) Contingently issuable shares
   (c) Contractual issued shares (d) Potential equity shares
4. In case potential equity shares have been cancelled during the year, they should be:
   (a) Ignored for computation of Diluted EPS.
   (b) Considered from the beginning of the year till the date they are cancelled.
   (c) The company needs to make an accounting policy and can follow the treatment in (a) or (b) as it decides.
   (d) Considered for computation of diluted EPS only if the impact of such potential equity shares would be material.
5. Partly paid up equity shares are:
   (a) Always considered as a part of Basic EPS.
   (b) Always considered as a part of Diluted EPS.
   (c) Depending upon the entitlement of dividend to the shareholder, it will be considered as a part of Basic or Diluted EPS as the case may be.
   (d) Considered as part of Basic/ Diluted EPS depending on the accounting policy of the company.

Thanks ....

Chapter 21

AS 22 – ACCOUNTING FOR TAXES ON INCOME

CHAPTER DESIGN

1. INTRODUCTION
2. OBJECTIVE
3. DEFINITIONS
4. RECOGNITIONS AND MEASUREMENT
   - (A) CURRENT TAX
   - (B) DEFERRED TAX
5. DISCLOSURES
6. RELEVANT EXPLANATIONS TO AS 22

1. INTRODUCTION :

This standard prescribes the accounting treatment of taxes on income and follows the concept of matching expenses against revenue for the period. The concept of matching is more peculiar in cases of income taxes since in a number of cases, the taxable income may be significantly different from the income reported in the financial statements due to the difference in treatment of certain items under taxation laws and the way it is reflected in accounts.

Question 1 :

Asset costing Rs. 1,00,000 was purchased on 1/1/2019. Depreciation @ 20% was charged as per SLM. However for Tax calculation 100 % is allowed for tax purpose. Assume PBDT of Rs. 2,00,000 for year 1 and year 2. Show how would AS 22 change the way taxes are accounted.

2. OBJECTIVE :

Matching of such taxes against revenue for a period poses special problems arising from the fact that in a number of cases, taxable income may be significantly different from the accounting income. This divergence between taxable income and accounting income arises due to two main reasons.

Firstly, there are differences between items of revenue and expenses as appearing in the statement of profit and loss and the items which are considered as revenue, expenses or deductions for tax purposes, known as Permanent Difference.

Secondly, there are differences between the amount in respect of a particular item of revenue or expense as recognised in the statement of profit and loss and the corresponding amount which is recognised for the computation of taxable income, known as Timing Difference.

3. DEFINTIIONS :

1. **Accounting income (loss)** is the net profit or loss for a period, as reported in the statement of profit and loss, before deducting income-tax expense or adding income tax saving.

2. **Taxable income (tax loss)** is the amount of the income (loss) for a period, determined in accordance with the tax laws, based upon which income-tax payable (recoverable) is determined.

3. **Tax expense (tax saving)** is the aggregate of current tax and deferred tax charged or credited to the statement of profit and loss for the period.

4. **Current tax** is the amount of income tax determined to be payable (recoverable) in respect of the taxable income (tax loss) for a period.

5. **Deferred tax** is the tax effect of timing differences. The differences between taxable income and accounting income can be classified into permanent differences and timing differences.
   - **(A)** **Timing differences** are the differences between taxable income and accounting income for a period that originate in one period and are capable of reversal in one or more subsequent periods.
   - **(B)** **Permanent differences** are the differences between taxable income and accounting income for a period that originate in one period and do not reverse subsequently.

4. RECOGNITION AND MEASUREMENTS :

1. **Recognition :**

   As per this Accounting Standard the income tax expense should be treated just like any other expenses on accrual basis irrespective of the timing of payment of tax. Tax expenses for the period should be recognised for the year which consist of current tax and deferred tax.

2. **Measurement :**
   - A. Current tax should be measured at the amount expected to be paid to (recovered from) the taxation authorities, using the applicable tax rates and tax laws.
   - B. Deferred tax assets and liabilities are usually measured using the tax rates and tax laws that have been enacted by the balance sheet date.
   - C. Difference in Accounting Profit and Tax Profit: We all know the profit as per accounts can be different from taxable profit. The reasons for difference between two profits are
     - **(i)** **Timing differences** are the differences between taxable income and accounting income for a period that originate in one period and are capable of reversal in one or more subsequent periods.
     - **(ii)** **Permanent differences** are the differences between taxable income and accounting income for a period that originate in one period and do not reverse subsequently.

   Note : Deferred Tax Asset / Deferred Tax liability is not created because of permanent difference, its created only because of timing difference .

Deferred Tax Liability is recognised for timing difference that will result in taxable amounts in future years. In simple words we are paying less tax now and are required to pay more in future

DTL = Pay less now and Pay more in future

Question 2 : RM Ltd.

RM Ltd prepares its annual accounts on 31st March. On 1st April, 2018, it purchases a machine at a cost of Rs 1,50,000. The machine has useful life of 3 years will zero expected scrap value. It is allowed to charge 100% depreciation as per tax and for accounts its decides to depreciate the asset by using SLM for the period of 3 years. It earned profit before depreciation and tax for Rs 2,00,000 each year and tax rate is 30%. Calculate current tax and deferred tax.

Deferred tax Asset is recognised for timing difference that will result deductible amounts in future years. In simple words we are paying more tax now and are required to pay less in future.

DTA = Pay more now and Pay less in future.

Question 3 : MR Ltd.

MR Ltd prepares its annual accounts on 31st March. It suffered a loss of Rs 1,00,000 in the year 2019 and made the profit of Rs 50,000 and Rs 60,000 in year 2020 and 2021. The loss can be carried for 8 years and tax rate is 40%. MR is virtually certain at the end of 2019 that company would generate sufficient taxable income in future years. Calculate the current tax and the deferred tax for the year 2019, 2020 and 2021.

Recognising DTA :

While recognising the tax effect of timing differences, consideration of prudence cannot be ignored. Therefore, deferred tax assets are recognised and carried forward only to the extent that there is a reasonable certainty of their realisation. This reasonable level of certainty would normally be achieved by examining the past record of the enterprise and by making realistic estimates of profits for the future. Where an enterprise has unabsorbed depreciation or carry forward of losses under tax laws, deferred tax assets should be recognised only to the extent that there is virtual certainty supported by convincing evidence that sufficient future taxable income will be available against which such deferred tax assets can be realised.

Re-assessment of Unrecognised Deferred Tax Assets :

At each balance sheet date, an enterprise re-assesses unrecognised deferred tax assets. The enterprise recognises previously unrecognised deferred tax assets to the extent that it has become reasonably certain or virtually certain, as the case may be, that sufficient future taxable income will be available against which such deferred tax assets can be realised.

Review of Deferred Tax Assets :

The carrying amount of deferred tax assets should be reviewed at each balance sheet date. An enterprise should write-down the carrying amount of a deferred tax asset to the extent that it is no longer reasonably certain or virtually certain, as the case may be, that sufficient future taxable income will be available against which deferred tax asset can be realised. Any such write-down may be reversed to the extent that it becomes reasonably certain or virtually certain, as the case may be, that sufficient future taxable income will be available.

5. DICSLOSURES :

Statement of profit and loss:

Under AS 22, there is no specific requirement to disclose current tax and deferred tax in the statement of profit and loss. However, considering the requirements under the Companies Act, 2013, the amount of income tax and other taxes on profits should be disclosed.
AS 22 does not require any reconciliation between accounting profit and the tax expense.

Balance sheet :

The break-up of deferred tax assets and deferred tax liabilities into major components of the respective balance should be disclosed in the notes to accounts.
Deferred tax assets and liabilities should be distinguished from assets and liabilities representing current tax for the period. Deferred tax assets and liabilities should be disclosed under a separate heading in the balance sheet of the enterprise, separately from current assets and current liabilities.
The nature of the evidence supporting the recognition of deferred tax assets should be disclosed, if an enterprise has unabsorbed depreciation or carry forward of losses under tax laws.
An enterprise should offset assets and liabilities representing current tax if the enterprise:

a. Has a legally enforceable right to set off the recognised amounts and
b. Intends to settle the asset and the liability on a net basis.

An enterprise should offset deferred tax assets and deferred tax liabilities if:

a. The enterprise has a legally enforceable right to set off assets against liabilities representing current tax; and

b. The deferred tax assets and the deferred tax liabilities relate to taxes on income levied by the same governing taxation laws.

6. RELEVANT EXPLANATIONS TO AS 22 :

Accounting for Taxes on Income in the situations of Tax Holiday under sections 80-IA and 80-IB of the Income Tax Act, 1961

The deferred tax in respect of timing differences which reverse during the tax holiday period should not be recognised to the extent the enterprise's gross total income is subject to the deduction during the tax holiday period as per the requirements of the Act. Deferred tax in respect of timing differences which reverse after the tax holiday period should be recognised in the year in which the timing differences originate. However, recognition of deferred tax assets should be subject to the consideration of prudence as laid down in AS 22.

For the above purposes, the timing differences which originate first should be considered to reverse first.

Accounting for Taxes on Income in the situations of Tax Holiday under sections 10A and 10B of the Income Tax Act, 1961

The deferred tax in respect of timing differences which originate during the tax holiday period and reverse during the tax holiday period, should not be recognised to the extent deduction from the total income of an enterprise is allowed during the tax holiday period as per the provisions of sections 10A and 10B of the Act. Deferred tax in respect of timing differences which originate during the tax holiday period but reverse after the tax holiday period should be recognised in the year in which the timing differences originate. However, recognition of deferred tax assets should be subject to the consideration of prudence as laid down in AS 22.

For the above purposes, the timing differences which originate first should be considered to reverse first.

Accounting for Taxes on Income in the context of section 115JB of the Income Tax Act, 1961

The payment of tax under section 115JB of the Act is a current tax for the period. In a period in which a company pays tax under section 115JB of the Act, the deferred tax assets and liabilities in respect of timing differences arising during the period, tax effect of which is required to be recognised under AS 22, should be measured using the regular tax rates and not the tax rate under section 115JB of the Act. In case an enterprise expects that the timing differences arising in the current period would reverse in a period in which it may pay tax under section 115JB of the Act, the deferred tax assets and liabilities in respect of timing differences arising during the current period, tax effect of which is required to be recognised under AS 22, should be measured using the regular tax rates and not the tax rate under section 115JB of the Act.

PRACTICAL QUESTIONS :

Question 4 : Rama Ltd.

Rama Ltd Provided the following information

	Rs .
Depreciation as per accounting records	2,00,000
Depreciation as per income tax records	5,00,000
Unamortised preliminary expenses as per tax record	30,000

There is adequate evidence of future profit sufficiency. How much deferred tax asset/liability should be recognised as transition adjustment? Tax rate 50%.

Question 5 : A Ltd.

From the following details of A Ltd. for the year ended 31-03-2017, calculate the deferred tax asset/ liability as per AS 22 and amount of tax to be debited to the Profit and Loss Account for the year.

	Rs .
Accounting Profit	6,00,000
Book Profit as per MAT	3,50,000
Profit as per Income Tax Act	60,000
Tax rate	20%
MAT rate	7.5%

Question 6 : Ultra Ltd.

Ultra Ltd. has provided the following information.

Depreciation as per accounting records = Rs 4,00,000

Depreciation as per tax records = Rs 10,00,000

Unamortised preliminary expenses as per tax record = Rs 30,000

There is adequate evidence of future profit sufficiency. How much deferred tax asset/liability should be recognised as transition adjustment when the tax rate is 50%?

Question 7 : XYZ

XYZ is an export oriented unit and was enjoying tax holiday upto 31.3.2016. No provision for deferred tax liability was made in accounts for the year ended 31.3.2016. While finalising the accounts for the year ended 31.3.2017, the Accountant says that the entire deferred tax liability upto 31.3.2016 and current year deferred tax liability should be routed through Profit and Loss Account as the relevant Accounting Standard has already become mandatory from 1.4.2001. Do you agree?

Question 8 : PQR Ltd.

PQR Ltd.'s accounting year ends on 31st March. The company made a loss of Rs. 2,00,000 for the year ending 31.3.2015. For the years ending 31.3.2016 and 31.3.2017, it made profits of Rs. 1,00,000 and Rs. 1,20,000 respectively. It is assumed that the loss of a year can be carried forward for eight years and tax rate is 40%. By the end of 31.3.2015, the company feels that there will be sufficient taxable income in the future years against which carry forward loss can be set off. There is no difference between taxable income and accounting income except that the carry forward loss is allowed in the years ending 2016 and 2017 for tax purposes. Prepare a statement of Profit and Loss for the years ending 2015, 2016 and 2017.

Question 9 : Omega Limited

Omega Limited is working on different projects which are likely to be completed within 3 years period. It recognises revenue from these contracts on percentage of completion method for financial statements during 2014-2015, 2015-2016 and 2016-2017 for Rs. 11,00,000, Rs. 16,00,000 and Rs. 21,00,000 respectively. However, for Income-tax purpose, it has adopted the completed contract method under which it has recognised revenue of Rs. 7,00,000, Rs. 18,00,000 and Rs. 23,00,000 for the years 2014-2015, 2015-2016 and 2016-2017 respectively. Income-tax rate is 35%. Compute the amount of deferred tax asset/liability for the years 2014-2015, 2015-2016 and 2016-2017.

Question 10 : RM Ltd.

RM Ltd Provided the following information

	Rs .
Depreciation as per accounting records	2,50,000
Depreciation as per income tax records	5,50,000
Unamortised preliminary expenses as per tax record	40,000

There is adequate evidence of future profit sufficiency. How much deferred tax asset/liability should be recognised as transition adjustment? Tax rate 50%.

Question 11 : Nish Ltd.

From the following details of Nish Ltd. for the year ended 31-03-2019, calculate the deferred tax asset/ liability as per AS 22 and amount of tax to be debited to the Profit and Loss Account for the year.

	Rs
Accounting Profit	9,00,000
Book Profit as per MAT	5,25,000
Profit as per Income Tax Act	700
Tax rate	30%
MAT rate	7.5%

MCQs :

1. As per AS 22 on 'Accounting for Taxes on Income', tax expense is:
   - (a) Current tax + deferred tax charged to profit and loss account
   - (b) Current tax-deferred tax credited to profit and loss account
   - (c) Either (a) or (b)
   - (d) Deferred tax charged to profit and loss account
2. G Ltd. has provided the following information:
   Depreciation as per accounting records = Rs. 2,00,000
   Depreciation as per tax records = Rs. 5,00,000
   There is adequate evidence of future profit sufficiency.
   How much deferred tax asset/liability should be recognized as transition adjustment when the tax rate is 50%?
   - (a) Deferred Tax asset = Rs. 2,70,000.
   - (b) Deferred Tax asset = Rs. 1,35,000.
   - (c) Deferred Tax Liability = Rs. 2,70,000
   - (d) Deferred Tax Liability = Rs. 1,35,000.
3. State which of the followings statements are correct:
   - (1) There are no pre-conditions required to recognize deferred tax liability,
   - (2) Deferred tax asset under all circumstances can only be created if and only if there is reasonable certainty that future taxable income will arise.
   - (a) Both are correct.
   - (b) Only (1) is correct.
   - (c) Only (2) is correct.
   - (d) None of the statements are correct.
4. Which of the following statement are incorrect:
   - (a) Only timing differences result in creation of deferred tax.
   - (b) Permanent differences do not result in recognition of deferred tax.
   - (c) The tax rate used for measurement of deferred tax is substantively enacted tax rate.
   - (d) The entity has to recognize deferred tax liability/asset arising out of timing difference. There are no conditions which are required to evaluated for their recognition.

Thanks ....

Chapter 22

AS 23 – ACCOUNTING FOR INVESTMENTS IN ASSOCIATES IN CONSOLIDATED FINANCIAL STATEMENTS

CHAPTER DESIGN

1. INTRODUCTION
2. DEFINITIONS
3. EQUITY METHOD
4. WHY IS EQUITY METHOD OF ACCOUNTING ADOPTED FOR INVESTMENT IN ASSOCIATES?

1. INTRODUCTION :

AS 23, came into effect in respect of accounting periods commenced on or after 1-4-2002. AS 23 describes the principles and procedures for recognizing investments in associates (in which the investor has significant influence, but not a subsidiary or joint venture of investor) in the consolidated financial statements of the investor. An investor which presents consolidated financial statements should account for investments in associates as per equity method in accordance with this standard but in its separate financial statements, AS 13 will be applicable.

2. DEFINITIONS :

1. A subsidiary is an enterprise that is controlled by another enterprise (known as the parent).
2. A parent is an enterprise that has one or more subsidiaries.
3. A group is a parent and all its subsidiaries.
4. The equity method is a method of accounting whereby the investment is initially recorded at cost, identifying any goodwill/capital reserve arising at the time of acquisition. The carrying amount of the investment is adjusted thereafter for the post acquisition change in the investor's share of net assets of the investee. The consolidated statement of profit and loss reflects the investor's share of the results of the operations of the investee.
5. Equity is the residual interest in the assets of an enterprise after deducting all its liabilities.
6. Consolidated financial statements are the financial statements of a group presented as those of a single enterprise. An associate is an enterprise in which the investor has significant influence and which is neither a subsidiary nor a joint venture of the investor.
7. Significant influence is the power to participate in the financial and/or operating policy decisions of the investee but not control over those policies.

As a general rule, significant influence is presumed to exist when an investor holds, directly or indirectly through subsidiaries, 20% or more of the voting power of the investee.

As a general rule, significant influence is presumed to exist when an investor holds, directly or indirectly through subsidiaries, 20% or more of the voting power of the investee.

If the investor holds, directly or indirectly through subsidiaries, less than 20% of the voting power of the investee, it is presumed that the investor does not have significant influence, unless such influence can be clearly demonstrated. The presence of one or more of the indicators as above may indicate that an investor has significant influence over a less than 20% owned corporate investee.

3. EQUITY METHOD

The equity method is a method of accounting whereby the investment is initially recorded at cost, identifying any goodwill/capital reserve arising at the time of acquisition. The carrying amount of the investment is adjusted thereafter for the post acquisition change in the investor's share of

net assets of the investee. The consolidated statement of profit and loss reflects the investor's share of the results of operations of the investee.

Goodwill/capital reserve arising on the acquisition of an associate by an investor should be included in the carrying amount of investment in the associate but should be disclosed separately.

From the definition, following broad conclusions can be drawn:

a. In CFS, investment is to be recorded at cost.

b. Any surplus or deficit in cost and net asset to be recorded as goodwill or capital reserve.

c. Distributions received from an investee reduce the carrying amount of the investment.

d. Any subsequent change in share in net asset is adjusted in cost of investment and goodwill/capital reserve.

e. Consolidated Profit & Loss shows the investor's share in the results of operations of the investee.

Question 1 : A Ltd.

A Ltd. acquire 45% of B Ltd. shares on April 01, 20X1, the price paid was Rs 15,00,000. Following are the extracts of balance sheet of B Ltd. as of 1 April 20X1:

Paid up Equity Share Capital	Rs 10,00,000
Securities Premium	Rs 1,00,000
Reserves and Surplus	Rs 5,00,000

B Ltd. has reported net profits of Rs 3,00,000 and paid dividends of Rs 1,00,000 for the year ended 31 March 20X2. Calculate the amount at which the investment in B Ltd. should be shown in the consolidated balance sheet of A Ltd. as on March 31, 20X2.

Question 2 : AB Ltd.

AB Ltd. holds 22% share of BA Ltd. on 1st April of the year and following are the relevant information as available on the date are Cost of Investment Rs 33,000 and Total Equity on the date of acquisition Rs 2,00,000. How will the above case be presented in Balance sheet.

Question 3 : AC Ltd.

AC Ltd. holds 22% share of BC Ltd. on 1st April of the year and following are the relevant information as available on the date are Cost of Investment Rs 55,000 and Total Equity on the date of acquisition Rs 2,00,000. How will the above case be presented in Balance sheet.

Question 4 : AD Ltd.

AD Ltd. acquired 10% stake of BD Ltd. on April 01 and further 15% on October 01 during the same year. Other information is as follow:

Cost of Investment for 10% Rs 1,00,000 and for 15% Rs 1,45,000

Net asset on April 01 Rs 8,50,000 and on October 01 Rs 10,00,000.

How will the following case be Accounted for.

Question 5 : ABC Ltd.

ABC Ltd. acquired 10% stake of BBC Ltd. on April 01 and further 15% on October 01 of the same year. Other information is as follow:

Cost of Investment for 10% Rs 1,00,000 and for 15% Rs 1,55,000

Net asset on April 01 Rs 8,50,000 and on October 01 Rs 10,00,000.

How will the following be accounted for ?

Question 6 : X Ltd.

X Ltd. acquired 25% stake of Y Ltd. on April 01 and further 5% on October 01 of the same year. Other information is as follow:

Cost of Investment for 25% Rs 1,50,000 and for 5% Rs 20,000

Net asset on April 01 Rs 5,00,000.

Profit for the year Rs 90,000 earned in the ratio 2:1 respectively.

How will the following be accounted for ?

Question 7 : AK Ltd.

AK Ltd. acquired 40% share in BK Ltd. on April 01, 20X1 for Rs 10 lacs. On that date B Ltd. had 1,00,000 equity shares of Rs 10 each fully paid and accumulated profits of Rs 2,00,000. During the year 20X1-20X2, B Ltd. suffered a loss of Rs 10,00,000; during 20X2-20X3 loss of Rs 12,50,000 and during 20X3-20X4 again a loss of Rs 5,00,000. Show the extract of consolidated balance sheet of A Ltd. on all the four dates recording the above events.

Question 8 : Bright Ltd.

Bright Ltd. acquired 30% of East India Ltd. shares for Rs 2,00,000 on 01-06-20X1. By such an acquisition Bright can exercise significant influence over East India Ltd. During the financial year ending on 31-03-20X1 East India earned profits Rs 80,000 and declared a dividend of Rs 50,000 on 12-08-20X1. East India reported earnings of Rs 3,00,000 for the financial year ending on 31-03-20X2 (assume profits to accrue evenly) and declared dividends of Rs 60,000 on 12-06-20X2.

Calculate the carrying amount of investment in:

(i) Separate financial statements of Bright Ltd. as on 31-03-20X2;

(ii) Consolidated financial statements of Bright Ltd.; as on 31-03-20X2;

(iii) What will be the carrying amount as on 30-06-20X2 in consolidated financial statements?

Question 9 : A Ltd.

A Ltd. acquired 25% of shares in B Ltd. as on 31.3.20X1 for Rs 3 lakhs. The Balance Sheet of B Ltd. as on 31.3.20X1 is given below:

	Rs.
Share Capital	5,00,000
Reserves and Surplus	5,00,000
	10,00,000
Fixed Assets	5,00,000
Investments	2,00,000
Current Assets	3,00,000
	10,00,000

During the year ended 31.3.20X2 the following are the additional information available:

(i) A Ltd. received dividend from B Ltd., for the year ended 31.3.20X1 at 40% from the Reserves.

(ii) B Ltd., made a profit after tax of Rs 7 lakhs for the year ended 31.3.20X2.

(iii) B Ltd., declared a dividend @ 50% for the year ended 31.3.20X2 on 30.4.20X2.

A Ltd. is preparing Consolidated Financial Statements in accordance with AS 21 for its various subsidiaries. Calculate:

(i) Goodwill if any on acquisition of B Ltd.'s shares.

(ii) How A Ltd., will reflect the value of investment in B Ltd., in the Consolidated Financial Statements?

(iii) How the dividend received from B Ltd. will be shown in the Consolidated Financial Statements?

4. WHY IS EQUITY METHOD OF ACCOUNTING ADOPTED FOR INVESTMENT IN ASSOCIATES?

Investments in associates cannot be treated as a normal investment under AS 13. The intent of investing to such an extent (i.e.; 20% or more but less than 50% of equity) in an associate is an expression of the fact that the investor is not merely interested in the dividend distribution, but also is interested in the participation of decision-making process in the associate.

Thus, recognition of income on the basis of distributions received may not be an adequate measure of the income earned by an investor on an investment in an associate because the distributions received may bear little relationship to the performance of the associate. As the investor has significant influence over the associate, the investor has a measure of responsibility for the associate's performance and, as a result, the return on its investment. The investor accounts for this stewardship by extending the scope of its consolidated financial statements to include its share of results of such an associate and so provides an analysis of earnings and investment from which more useful ratios can be calculated. As a result, application of the equity

method in consolidated financial statements provides more informative reporting of the net assets and net income of the investor.

MCQ'S

1. Identity which of the statements are correct
   An enterprise can influence the significant economic decision making by many ways like:
   (i) Representation on the board of directors or governing body of the investee.
   (ii) Participation in policy-making processes.
   (iii) Interchange of managerial personnel.
   (iv) Provision of essential technical information.
   (a) Statement (i) and (ii) are correct.
   (b) Statement (i), (ii) and (iii) are correct.
   (c) Statement (i), (ii), (iii) and (iv) are correct.
   (d) Statement (ii) and (iii) are correct.
2. A Ltd. is holding 90% share in B Ltd. and 10% shares in C Ltd., and B Ltd. is holding 11% shares in C Ltd.
   Identity which of the statements are incorrect.
   (i) In this case, A Ltd. is parent of B Ltd.
   (ii) As far as the relationship between A Ltd. and C Ltd. is concerned; A Ltd has a total of direct and indirect holding of (10% + 90% of 11%) 19.9 % in C Ltd.
   (iii) C Ltd. is an associate of A Ltd.
   (a) Statement (ii) is incorrect.
   (b) Statement (iii) is incorrect.
   (c) Statement (ii) and (iii) both are incorrect.
   (d) All statements are incorrect.
3. A Ltd. acquired 10% stake of B Ltd. on April 01 and further 15% on October 01 of the same year. Other information is as follows:
   Cost of Investment for 10% Rs 1,00,000 and for 15% Rs 1,55,000 Net asset on April 01 Rs 8,50,000 and on October 01 Rs 10,00,000.
   What is the amount of goodwill or capital reserve arising on significant influence?
   (a) Goodwill = Rs 10,000. (b) Goodwill = Rs 20,000.
   (c) Capital Reserve = Rs 10,000.
4. Capital Reserve = Rs 20,000. 4. A Ltd. acquired 10% stake of B Ltd. On April 01 and further 15% on October 01 during the same year. Other information is as follow:
   Cost of Investment for 10% Rs 1,00,000 and for 15% Rs 1,45,000
   Net asset on April 01 Rs 8,50,000 and on October 01 Rs 10,00,000.
   What is the amount of goodwill or capital reserve arising on significant influence?
   (a) Goodwill = Rs 10,000. (b) Goodwill = Rs 20,000.

(c) Capital Reserve = Rs 10,000. (d) Capital Reserve = Rs 20,000.

5. Identity which of the statements are correct.

(i) In case an associate has made a provision for proposed dividend (i.e. dividend declared after the reporting period but it pertains to that reporting year) in its financial statements, the investor's share of the results of operations of the associate should be computed without taking into consideration the proposed dividend.

(ii) In case an associate has made a provision for proposed dividend (i.e. dividend declared after the reporting period but it pertains to that reporting year) in its financial statements, the investor's share of the results of operations of the associate should be computed after taking into consideration the proposed dividend.

(iii) The potential equity shares of the investee held by the investor should not be taken into account for determining the voting power of the investor.

(iv) The potential equity shares of the investee held by the investor should be taken into account for determining the voting power of the investor.

(a) Statement (i) and (iii). (b) Statement (ii) and (iv).

(c) Statement (i) only. (d) Statement (iii) only.

Thanks ....

Chapter 23

AS 24 – DISCONTINUING OPERATIONS

CHAPTER DESIGN

1. INTRODUCTION
2. DISCONTINUING OPERATIONS
3. INITIAL DISCLOSURE EVENT
4. RECOGNITION AND MEASUREMENT
5. PRESENTATION AND DISCLOSURE
   (A) INITIAL DISCLOSURE
   (B) DISCLOSURE OTHER THAN INITIAL DISCLOSURE
   (C) OTHER DISCLOSURES
6. UPDATING THE DISCLOSURE
7. SEPARATE DISCLOSURE FOR EACH DISCONTINUING OPERATION
8. PRESENTATION OF THE REQUIRED DISCLOSURES
9. RESTATEMENT OF PRIOR PERIODS

1. INTRODUCTION :

Imagine that a large company selling several products in the market decides to discontinue the sale of one of its key product as it plans to sell that portion of its business to another entity. Ideally, this information should be disclosed to primary stakeholders as they would take economic decisions based on the performance of the remaining portion of the business that is expected to be continued by the company in future. Therefore, the presentation requirements of such discontinuing operations becomes relevant and the aspects of AS 24 need to be understood. AS 24 is applicable to all discontinuing operations.

2. DISCONTINUING OPERATIONS :

A discontinuing operation is a component of an enterprise:

(a) That the enterprise, pursuant to a single plan, is:

- (i) Disposing of substantially in its entirety, such as by selling the component in a single transaction or by demerger or spin-off of ownership of the component to the enterprise's shareholders; or
- (ii) Disposing of piecemeal, such as by selling off the component's assets and settling its liabilities individually; or
- (iii) Terminating through abandonment; and

(b) That represents a separate major line of business or geographical area of operations.

(c) That can be distinguished operationally and for financial reporting purposes.

Question 1 : Co. XY

Co. XY runs a famous chain of restaurants. It decides to sell its stake in one of the restaurant. This restaurant contributes around 5% of total revenue to the entire business. XY does not intend to sell any other restaurant as part of its strategy. Does sale of above stake be defined as discontinuing operations.

Question 2 : Group MN

Group MN operates in various industries including Hotels, Airlines and Software through its subsidiaries. It has decided to sell its Airline business to be able to concentrate on other verticals. As a result, it has started to sell its aircrafts and paying off the associated liabilities. During the year, it has sold off 5 aircrafts out of the fleet of 50 aircrafts so far as part of the sale. The Airline business constitutes 25% of total group revenue. Does the above plan qualify to be defined as discontinuing operations

Question 3 : GH

GH, a large car manufacturing company, decides to discontinue its manufacturing operations relating to the diesel cars production. It plans to restructure the business by

revamping its existing operations, and starting new manufacturing process for manufacture and sale of electric vehicles. Does this qualify for discontinuing operations

3. INITIAL DISCLOSURE EVENT :

With respect to a discontinuing operation, the initial disclosure event is the occurrence of one of the following, whichever occurs earlier:

a) The enterprise has entered into a binding sale agreement for substantially all of the assets attributable to the discontinuing operation; or

b) The enterprise's board of directors or similar governing body has both
   a. approved a detailed, formal plan for the discontinuance and
   b. made an announcement of the plan.

A detailed, formal plan for the discontinuance normally includes:

- identification of the major assets to be disposed of;
- the expected method of disposal;
- the period expected to be required for completion of the disposal;
- the principal locations affected;
- the location, function, and approximate number or employees who will be compensated for terminating their services; and
- the estimated proceeds or salvage to be realised by disposal.

An enterprise's board of directors or similar governing body is considered to have made the announcement of a detailed, formal plan for discontinuance, if it has announced the main features of the plan to those affected by it, such as, lenders, stock exchanges, trade payables, trade unions, etc. in a sufficiently specific manner so as to make the enterprise demonstrably committed to the discontinuance.

4. RECOGNITION AND MEASUREMENT :

For recognising and measuring the effect of discontinuing operations, this AS does not provide any guidelines, but for the purpose the relevant Accounting Standards should be referred.

5. PRESENTATION AND DISCLOSURE :

5.1. Initial Disclosure :

An enterprise should include the following information relating to a discontinuing operation in its financial statements beginning with the financial statements for the period in which the initial disclosure event occurs:

a) A description of the discontinuing operation(s);

b) The business or geographical segment(s) in which it is reported as per AS 17

c) The date and nature of the initial disclosure event;

d) The date or period in which the discontinuance is expected to be completed

e) if known or determinable;

f) The carrying amounts, as of the balance sheet date, of the total assets to be disposed of and the total liabilities to be settled;

g) The amounts of revenue and expenses in respect of the ordinary activities attributable to the discontinuing operation during the current financial reporting period;

h) The amount of pre-tax profit or loss from ordinary activities attributable to the discontinuing operation during the current financial reporting period, and the income tax expense related thereto;

i) The amounts of net cash flows attributable to the operating, investing, and financing activities of the discontinuing operation during the current financial reporting period;

5.2. Disclosures Other Than Initial Disclosures Note :

All the disclosures above should be presented in the notes to the financial statements except for amounts pertaining to pre-tax profit/loss of the discontinuing operation and the income tax expense thereon (second last bullet above) which should be shown on the face of the statement of profit and loss.

5.3. Other disclosures :

When an enterprise disposes of assets or settles liabilities attributable to a discontinuing operation or enters into binding agreements for the sale of such assets or the settlement of such liabilities, it should include, in its financial statements, the following information when the events occur:

a) For any gain or loss that is recognised on the disposal of assets or settlement of liabilities attributable to the discontinuing operation, (i) the amount of the pre-tax gain or loss and (ii) income tax expense relating to the gain or loss and

b) The net selling price or range of prices (which is after deducting expected disposal costs) of those net assets for which the enterprise has entered into one or more binding sale agreements, the expected timing of receipt of those cash flows and the carrying amount of those net assets on the balance sheet date.

6. UPDATING THE DISCLOSURES :

In addition to these disclosures, an enterprise should include, in its financial statements, for periods subsequent to the one in which the initial disclosure event occurs, a description of any

significant changes in the amount or timing of cash flows relating to the assets to be disposed or liabilities to be settled and the events causing those changes.

The disclosures should continue in financial statements for periods up to and including the period in which the discontinuance is completed. Discontinuance is completed when the plan is substantially completed or abandoned, though full payments from the buyer(s) may not yet have been received.

If an enterprise abandons or withdraws from a plan that was previously reported as a discontinuing operation, that fact, reasons therefore and its effect should be disclosed.

7. SEPARATE DISCLOSURE FOR EACH DISCONTINUING OPERATION :

Any disclosures required by AS 24 should be presented separately for each discontinuing operation.

8. PRESENTATION OF THE REQUIRED DISCLOSURE :

The above disclosures should be presented in the notes to the financial statements except the following which should be shown on the face of the statement of profit and loss:

a) The amount of pre-tax profit or loss from ordinary activities attributable to the discontinuing operation during the current financial reporting period, and the income tax expense related thereto; and

b) The amount of the pre-tax gain or loss recognised on the disposal of assets or settlement of liabilities attributable to the discontinuing operation.

9. RESTATEMENT OF PRIOR PERIODS :

Comparative information for prior periods that is presented in financial statements prepared after the initial disclosure event should be restated to segregate assets, liabilities, revenue, expenses, and cash flows of continuing and discontinuing operations in a manner similar to that mentioned above.

10. DISCLOSURE IN INTERIM FINANCIAL REPORTS :

Disclosures in an interim financial report in respect of a discontinuing operation should be made in accordance with AS 25, 'Interim Financial Reporting', including:

A) Any significant activities or events since the end of the most recent annual reporting period relating to a discontinuing operation and

B) Any significant changes in the amount or timing of cash flows relating to the assets to be disposed or liabilities to be settled.

Question 4 : Rohini Limited

Rohini Limited is in the business of manufacture of passenger cars and commercial vehicles. The Company is working on a strategic plan to close the production of passenger cars and to produce only commercial vehicles over the coming 5 years. However, no specific plans have been drawn up for sale of neither the division nor its assets. As part of its prospective plan it will reduce the production of passenger cars by 20% annually. It also plans to establish another new factory for the manufacture of commercial vehicles and transfer surplus employees in a phased manner.

You are required to comment:

1. If mere gradual phasing out in itself can be considered as a 'discontinuing operation' within the meaning of AS-24.
2. If the Company passes a resolution to sell some of the assets in the passenger car division and also to transfer few other assets of the passenger car division to the new factory, does this trigger the application of AS-24?
3. Would your answer to (ii) above be different if the Company resolves to sell the assets of the passenger car division in a phased but time bound manner?

MCQs

1. AB decided to dispose of its Clothing division as part of its long-term strategy.
   (A) Date of Board approval - 1st March 20X1;
   (B) Date of formal announcement made to affected parties - 15th March 20X1.
   (C) Date of Binding Sale agreement – 1st July 20X1;
   (D) Reporting date – 31st March 20X1
   The date of initial disclosure event would be:
   (a) 1st March 20X1 (b) 15th March 20X1
   (c) 31st March 20X1 (d) 31st July 20X1
2. To qualify as a component that can be distinguished operationally and for financial reporting purposes, the condition(s) to be met is (are):
   (a) The operating assets and liabilities of the component can be directly attributed to it.
   (b) Its revenue can be directly attributed to it.
   (c) At least a majority of its operating expenses can be directly attributed to it.
   (d) All of the above
3. Identify which of the following statements is incorrect?
   (a) A discontinuing operation is a component of an enterprise that represents a separate major line of business or geographical area of operations.
   (b) A discontinuing operation is a component of an enterprise that can be distinguished operationally and for financial reporting purposes.

(c) A discontinuing operation is a component of an enterprise that may or may not be distinguished operationally and for financial reporting purposes.

(d) A discontinuing operation may be disposed of in its entirety or piecemeal, but always pursuant to an overall plan to discontinue the entire component.

4. Identify the incorrect statement

(a) Discontinuing operations are infrequent events, but this does not mean that all infrequent events are discontinuing operations.

(b) The fact that a disposal of a component of an enterprise is classified as a discontinuing operation under AS 24 would always raise a question regarding the enterprise's ability to continue as a going concern.

(c) For recognising and measuring the effect of discontinuing operations, AS 24 does not provide any guidelines, but for the purpose the relevant Accounting Standards should be referred.

(d) An enterprise shall include a description of the discontinuing operation, in its financial statements beginning with the financial statements for the period in which the initial disclosure event occurs.

Thanks ....

Rahul Malkan

Chapter 24

AS 26 – INTANGIBLE ASSETS

CHAPTER DESIGN

1. INTRODUCTION
2. SCOPE
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5. INITIAL MEASUREMENT
   - (A) SEPARATE ACQUISITION
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   - (D) EXCHANGE OF ASSETS
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   - (F) INTERNALLY GENERATED INTANGIBLE ASSETS
     - (I) RESEARCH PHASE
     - (II) DEVELOPMENT PHASE
6. SUBSEQUENT MEASUREMENT
7. AMORTIZATION OF INTANGIBLE ASSET
   - (A) PERIOD
   - (B) METHOD
   - (C) RESIDUAL VALUE
8. IMPAIRMENT OF INTANGIBLE ASSETS
9. RETIREMENT AND DISPOSAL
10. DISCLOSURES

1. INTRODUCTION :

The objective of AS 26 is to prescribe the accounting treatment for intangible assets that are not dealt with specifically in another Accounting Standard. AS 26 requires an enterprise to recognise an intangible asset if, and only if, certain criteria are met. AS 26 also specifies how to measure the carrying amount of intangible assets and requires certain disclosures about intangible assets.

2. SCOPE :

AS 26 should be applied by all enterprises in accounting for intangible assets, except:

a. Intangible assets that are covered by another Accounting Standard
   For example, AS 26 does not apply to:
   (a) intangible assets held by an enterprise for sale in the ordinary course of business (AS 2 and AS 7)
   (b) deferred tax assets (AS 22)
   (c) leases that fall within the scope of AS 19
   (d) goodwill arising on an amalgamation (AS 14 (Revised)) and goodwill arising on consolidation (AS 21 (Revised))
b. Financial assets.
c. Mineral rights and expenditure on the exploration for, or development and extraction of, minerals, oil, natural gas and similar non-regenerative resources and
d. Intangible assets arising in insurance enterprises from contracts with policyholders.

However, AS 26 applies to other intangible assets used (such as computer software), and other expenditure (such as start-up costs), in extractive industries or by insurance enterprises.

AS 26 also applies to:

(i) expenditure on advertising, training, start - up cost
(ii) Research and development activities
(iii) Right under licensing agreements for items such as motion picture films, video recordings, plays, manuscripts
(iv) Patents, copyrights and trademarks
(v) goodwill

3. DEFINITIONS :

1. An asset :

An Asset is a resource:

a. Controlled by an enterprise as a result of past events and
b. From which future economic benefits are expected to flow to the enterprise.

2. **Monetary assets :**

Monetary Assets are money held and assets to be received in fixed or determinable amounts of money.

3. **Non-monetary Assets :**

Non – monetary assets are assets other than monetary assets.

4. **Amortisation :**

Amortization is the systematic allocation of the depreciable amount of an intangible asset over its useful life.

5. **Depreciable amount :**

Depreciable Amount is the cost of an asset less its residual value.

6. **Useful life :**

Useful life is either:

(a) the period of time over which an asset is expected to be used by the enterprise; or

(b) the number of production or similar units expected to be obtained from the asset by the enterprise.

7. **Fair value :**

Fair Value of an asset is the amount for which that asset could be exchanged between knowledgeable, willing parties in an arm's length transaction.

8. **An impairment loss :**

An impairment loss is the amount by which the carrying amount of an asset exceeds its recoverable amount.

9. **Carrying amount :**

Carrying amount is the amount at which an asset is recognised in the balance sheet, net of any accumulated amortisation and accumulated impairment losses thereon.

10. **A financial asset :**

A Financial asset is any asset that is:

a) Cash,

b) A contractual right to receive cash or another financial asset from another enterprise,

c) A contractual right to exchange financial instruments with another enterprise under conditions that are potentially favourable or

d) An ownership interest in another enterprise.

11. Intangible Assets :

An intangible asset is

- an identifiable
- non-monetary asset
- without physical substance
- held for use in the production or supply of goods or services, for rental to others, or for administrative purposes.

12. Identifiability :

- The definition of an intangible asset requires that an intangible asset be identifiable. To be identifiable, it is necessary that the intangible asset is clearly distinguished from goodwill.
- An intangible asset can be clearly distinguished from goodwill if the asset is separable. An asset is separable if the enterprise could rent, sell, exchange or distribute the specific future economic benefits attributable to the asset without also disposing of future economic benefits that flow from other assets used in the same revenue earning activity.
- Though Separability is not a necessary condition for identifiability. If an asset generates future economic benefits only in combination with other assets, the asset is identifiable if the enterprise can identify the future economic benefits that will flow from the asset.

Question 1 : Sun Ltd.

Sun Ltd has an expertise in consulting business. In past years, company has gained a market share for its services of 30 percent and considers recognizing it as an intangible asset. Is the action by company is justified?

4. RECOGNITION :

The recognition of an item as an intangible asset requires

a. It is probable that the future economic benefits that are attributable to the asset will flow to the enterprise; and

b. The cost of the asset can be measured reliably.

c. that the item meets the definition of an intangible asset

Question 2 : Company XYZ Ltd.

Company XYZ Ltd. has provided training to its staff on various new topics like GST, Ind AS etc. to ensure the compliance as per the required law. Can the company recognise such cost of staff training as intangible asset?

5. INITIAL MEASUREMENT :

An intangible asset should be measured initially at cost.

An Intangible Assets can be acquired by any of the following ways

(a) Separate Acquisition
(b) Acquisition as the part of Amalgamation
(c) Acquisition by the way of Govt. Grant
(d) Exchange of Asset
(e) Internally generated Goodwill
(f) Internally generated intangible Assets

(a) Separate Acquisition :

If an intangible asset is acquired separately, the cost of the intangible asset can usually be measured reliably. This is particularly so when the purchase consideration is in the form of cash or other monetary assets.

The cost of an intangible asset comprises its purchase price, including any import duties and other taxes (other than those subsequently recoverable by the enterprise from the taxing authorities), and any directly attributable expenditure on making the asset ready for its intended use. Directly attributable expenditure includes, for example, professional fees for legal services. Any trade discounts and rebates are deducted in arriving at the cost.

If an intangible asset is acquired in exchange for shares or other securities of the reporting enterprise, the asset is recorded at its fair value, or the fair value of the securities issued, whichever is more clearly evident.

Question 3 : Jupiter Ltd.

Jupiter Ltd. Acquires new energy efficient technology that will significantly reduce its energy costs for manufacturing

1. Costs of new solar technology – 10,00,000
2. Trade discount provided – (1,00,000)
3. Training course for staff in new technology – 50,000
4. Initial testing of new technology – 35,000
5. Losses incurred while other parts of plant shut down during testing and training – 25,000

Calculate the amount of Intangible Asset.

(b) Acquisition as the part of Amalgamation :

An intangible asset acquired in an amalgamation in the nature of purchase is accounted for in accordance with AS 14 (Revised). In accordance with AS 26:

a) A transferee recognises an intangible asset that meets the recognition criteria, even if that intangible asset had not been recognised in the financial statements of the transferor and

b) If the cost (i.e. fair value) of an intangible asset acquired as part of an amalgamation in the nature of purchase cannot be measured reliably, that asset is not recognised as a separate intangible asset but is included in goodwill.

Hence, judgement is required to determine whether the cost (i.e. fair value) of an intangible asset acquired in an amalgamation can be measured with sufficient reliability for the purpose of separate recognition

Question 4 : RM Ltd.

RM Ltd purchased Nish Ltd on 1/1/2020. Net Assets of Nish Ltd amounted to Rs 1,80,000. The total consideration paid by RM Ltd amounted to Rs 2,00,000. Calculate the amount of goodwill to be recognised by RM Ltd. RM Ltd spent additional amount of Rs 20,000 on expenditures designed to maintain goodwill. On 31st December, RM estimated that the benefit period of goodwill was 20 years. Calculate the amount of goodwill to be amortise and also calculate the carrying amount of goodwill after amortization.

(c) Acquisition by the way of Govt. grant. :

Intangible asset acquired free of charge, or for nominal consideration, by way of government grant is recognised at a nominal value or at the acquisition cost, as appropriate; any expenditure that is directly attributable to making the asset ready for its intended use is also included in the cost of the asset.

(d) Exchange of Assets :

A. The cost of such an item of intangible is measured at fair value (even if an entity cannot immediately derecognise the asset given up) unless:
   1. the exchange transaction lacks commercial substance; or
   2. the fair value of neither the asset received nor the asset given up is reliably measurable

B. If the acquired item is not measured at fair value, its cost is measured at the carrying amount of the asset given up.

Question 5 : Sun Ltd.

Sun Ltd. acquired a software from Earth Ltd. in exchange for a telecommunication license. The telecommunication license is carried at Rs.5,00,000 in the books of Sun Ltd. The Software is carried at Rs.10,000 in the books of the Earth Ltd which is not the fair value. Advise journal entries in the following situations in the books of Sun Ltd and Earth Ltd:-

1) Fair value of software is Rs.5,20,000 and fair value of telecommunication license is Rs.5,00,000.
2) Fair Value of Software is not measureable. However similar Telecommunication license is transacted by another company at Rs.4,90,000.
3) Neither Fair Value of Software nor Telecommunication license could be reliably measured.

(e) <u>Internally generated goodwill :</u>

Internally generated goodwill is not recognised as an asset because it is not an identifiable resource controlled by the enterprise that can be measured reliably at cost.

(f) <u>Internally generated Intangible Assets :</u>

To assess whether an internally generated intangible asset meets the criteria for recognition, an enterprise classifies the generation of the asset into

- ➢ Research Phase &
- ➢ Development Phase

If an enterprise cannot distinguish the research phase from the development phase of an internal project to create an intangible asset, the enterprise treats the expenditure on that project as if it were incurred in the research phase only.

<u>Research Phase :</u>

Research is original and planned investigation undertaken with the prospect of gaining new scientific or technical knowledge and understanding.

No intangible asset arising from research or from the research phase should be recognised. Expenditure on research or on the research phase should be recognised as an expense when it is incurred.

<u>Development phase :</u>

An intangible asset arising from development (or from the development phase of an internal project) should be recognised if, and only if, an enterprise can demonstrate all of the following:

a. The technical feasibility of completing the intangible asset so that it will be available for use or sale.
b. Its intention to complete the intangible asset and use or sell it.
c. Its ability to use or sell the intangible asset.
d. How the intangible asset will generate probable future economic benefits. Among other things, the enterprise should demonstrate the existence of a market for the output of the intangible asset or the intangible asset itself or, if it is to be used internally, the usefulness of the intangible asset.
e. The availability of adequate technical, financial and other resources to complete the development and to use or sell the intangible asset and
f. Its ability to measure the expenditure attributable to the intangible asset during its development reliably.

Question 6 : An enterprise

An enterprise is developing a new production process. During the year 2021, expenditure incurred was Rs 10 lacs, of which RS 9 lacs was incurred before 1 December 2021 and 1 lac was incurred between 1 December 2021 and 31 December 2021. The enterprise is able to demonstrate that, at 1 December 2021, the production process met the criteria for recognition as an intangible asset. The recoverable amount of the know-how embodied in the process (including future cash outflows to complete the process before it is available for use) is estimated to be Rs 5 lacs.

During the year 2022, expenditure incurred is Rs 20 lacs. At the end of 2022, the recoverable amount of the know-how embodied in the process (including future cash outflows to complete the process before it is available for use) is estimated to be Rs 19 lacs.

Question 7 : The company

The company had spent RS 45 lakhs for publicity and research expenses on one of its new consumer product, which was marketed in the accounting year 2015-2016, but proved to be a failure. State, how you will deal with the following matters in the accounts of U Ltd. for the year ended 31st March, 2016.

Subsequent Expenditure

Subsequent expenditure on an intangible asset after its purchase or its completion should be recognised 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. The 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.

Subsequent expenditure on brands, mastheads, publishing titles, customer lists and items similar in substance is always recognised as an expense to avoid the recognition of internally generated goodwill.

6. SUBSEQUENT MEASUREMENT :

After initial recognition, an intangible asset should be carried at its cost less any accumulated amortisation and any accumulated impairment losses.

7. AMOTTIZATION OF INTANGIBLE ASSETS :

The depreciable amount of an intangible asset should be allocated on a systematic basis over the best estimate of its useful life.

AMORTIZATION PERIOD :

Amortisation should commence when the asset is available for use.

Estimates of the useful life of an intangible asset generally become less reliable as the length of the useful life increases. AS 26 adopts a presumption that the useful life of intangible assets is unlikely to exceed ten years.

In some cases, there may be persuasive evidence that the useful life of an intangible asset will be a specific period longer than ten years. In these cases, the presumption that the useful life generally does not exceed ten years is rebutted and the enterprise:

a. Amortises the intangible asset over the best estimate of its useful life.
b. Estimates the recoverable amount of the intangible asset at least annually in order to identify any impairment loss and
c. Discloses the reasons why the presumption is rebutted and the factors that played a significant role in determining the useful life of the asset.

AMORTIZATION METHOD :

A variety of amortisation methods can be used to allocate the depreciable amount of an asset on a systematic basis over its useful life. These methods include the straight-line method, the diminishing balance method and the unit of production method. The method used for an asset is selected based on the expected pattern of consumption of economic benefits and is consistently applied from period to period, unless there is a change in the expected pattern of consumption of economic benefits to be derived from that asset. There will rarely, if ever, be persuasive evidence to support an amortisation method for intangible assets that results in a lower amount of accumulated amortisation than under the straight-line method.

RESIDUAL VALUE :

Residual value is the amount, which an enterprise expects to obtain for an asset at the end of its useful life after deducting the expected costs of disposal.

The residual value of an intangible asset should be assumed to be zero unless:

a. There is a commitment by a third party to purchase the asset at the end of its useful life or
b. There is an active market for the asset and:
   (i) Residual value can be determined by reference to that market and
   (ii) It is probable that such a market will exist at the end of the asset's useful life.

Review of amortisation period and amortisation method :

The amortisation period and the amortisation method should be reviewed at least at each financial year end. Such changes should be accounted for in accordance with AS 5.

Question 8 : ABC Ltd.

ABC Ltd. developed know-how by incurring expenditure of Rs 20 lakhs, the know-how was used by the company from 1.4.2009. The useful life of the asset is 10 years from the year of commencement of its use. The company has not amortised the asset till 31.3.2016. Pass Journal entry to give effect to the value of know-how as per Accounting Standard-26 for the year ended 31.3.2016.

8. IMPAIRMENT OF INTANGIBLE ASSETS :

Impairment losses of intangible assets are calculated on the basis of AS 28. AS 28 “Impairment of Assets” is not covered at Inter level.

9. RETIREMENT AND DISPOSAL :

An intangible asset should be derecognised (eliminated from the balance sheet) if

- disposed or
- when no future economic benefits are expected from its use and subsequent disposal.

Gains or losses arising from the retirement or disposal of an intangible asset should be determined as the difference between the net disposal proceeds and the carrying amount of the asset and should be recognised as income or expense in the statement of profit and loss.

10. DISCLOSURES :

The financial statements should disclose the following for each class of intangible assets, distinguishing between internally generated intangible assets and other intangible assets:

1. The useful lives or the amortisation rates used.
2. The amortisation methods used.
3. The gross carrying amount and the accumulated amortisation (aggregated with accumulated impairment losses) at the beginning and end of the period.
4. A reconciliation of the carrying amount at the beginning and end of the period showing:

(i) Additions, indicating separately those from internal development and through amalgamation.
(ii) Retirements and disposals.
(iii) Impairment losses recognised in the statement of profit and loss during the period.
(iv) Impairment losses reversed in the statement of profit and loss during the period.
(v) Amortisation recognised during the period and
(vi) Other changes in the carrying amount during the period.

PRACTICAL QUESTIONS :

Question 9 :

A company with a turnover of Rs 250 crores and an annual advertising budget of Rs 2 crores had taken up the marketing of a new product. It was estimated that the company would have a turnover of Rs 25 crores from the new product. The company had debited to its Profit and Loss account the total expenditure of Rs 2 crore incurred on extensive special initial advertisement campaign for the new product.

Is the procedure adopted by the company correct?

Question 10 :

On Jan 1, 2020, RM Ltd incurred preliminary expenses of Rs 24,000, What portion of this cost can be deferred to years subsequent to 2020.

Question 11 : Pluto Ltd.

Pluto Ltd. intends to open a new retail store in a new location in the next few weeks. Pluto Ltd has spent a substantial sum on a series of television advertisements to promote this new store. The Company has paid an amount of Rs.800,000 for advertisements before 31st March, 2011. Rs.700,000 of this sum relates to advertisements shown before 31st March, 2011 and Rs.100,000 to advertisements shown in April, 2011. Since 31st March, 2011. The Company has paid for further advertisements costing Rs.400,000. Pluto Ltd is of view that such costs can be carried forward as intangible assets. Since market research indicates that this new store is likely to be highly successful. Please explain and justify the treatment of the above costs in the financial statements for the year ended 31st March, 2011

Question 12 : Mercury Ltd.

Mercury Ltd. is preparing its accounts for the year ended 31st March, 2012 and is unsure about how to treat the following items.

(a) The company completed a grand marketing and advertising campaign costing Rs.4.8 lakh. The finance director had authorised this campaign on the basis that it would create Rs.8 lakh of additional profits over the next three years.

(b) A new product was developed during the year. The expenditure totaled Rs.3 lakh of which Rs.1.5 lakh was incurred prior to 30th September, 2011, the date on which it became clear that the product was technically viable. The new product will be launched in the next four months and its recoverable amount is estimated at Rs.1.4 lakh.

(c) Staff participated in a training programme which cost the company Rs.5 lakh. The training organisation had made a presentation to the directors of the company outlining that incremental profits to the business over the next twelve months would be Rs.7 lakh.

What amounts should appear as intangible assets in accordance with Ind AS 38 and Ind AS 36 in Mercury's balance sheet as on 31st March, 2012?

Question 13 : Development Phase Expenditure

Development Phase Expenditure on a new production process in 2011-2012:

	Rs.
1st April to 31st December	2,700
1st January to 31st March	900
	3,600

The production process met the intangible asset recognition criteria for development on 1st January, 2012. The amount estimated to be recoverable from the process is Rs.1,000.
What is the carrying amount of the intangible asset at 31st March, 2012 and the charge to profit or loss for 2011-2012?
Expenditure incurred in FY 2012-2013 is Rs.6,000.
At 31st March, 2013, the amount estimated to be recoverable from the process (including future cash outflows to complete the process before it is available for use) is Rs.5,000.
What is the carrying amount of the intangible asset at 31st March, 2013 and the charge to profit or loss for 2012-2013?

Question 14 : X Limited

X Limited engaged in the business of manufacturing fertilisers entered into a technical collaboration agreement with a foreign company Y Limited. As a result, Y Limited would provide the technical know-how enabling X Limited to manufacture fertiliser in a more efficient way. X Limited paid Rs.10,00,00,000 for the use of know-how for a period of 5 years. X Limited estimates the production of fertiliser as follows:

Year	(In metric tons)
1	50,000
2	70,000
3	1,00,000
4	1,20,000
5	1,10,000

At the end of the 1st year, it achieved its targeted production. At the end of 2nd year, 65,000 metric tons of fertiliser was being manufactured, and X Limited considered to revise the estimates for the next 3 years. The revised figures are 85,000, 1,05,000 and 1,15,000 metric tons for year 3, 4 & 5 respectively.
How will X Limited amortise the technical know-how fees as per Ind AS 38?

Question 15 : T Ltd.

T Ltd. is engaged is developing computer software. The expenditures incurred by T Ltd. in pursuance of its development of software is given below:

A. Paid Rs.2,00,000 towards salaries of the program designers.
B. Incurred Rs.5,00,000 towards other cost of completion of program design.
C. Incurred Rs.2,00,000 towards cost of coding and establishing technical feasibility.
D. Paid Rs.7,00,000 for other direct cost after establishment of technical feasibility.
E. Incurred Rs.2,00,000 towards other testing costs.
F. A focus group of other software developers was invited to a conference for the introduction of this new software. Cost of the conference aggregated to Rs.70,000.
G. On March 15, 20X1, the development phase was completed and a cash flow budget was prepared.

Net profit for the year was estimated to be equal Rs.40,00,000. How T Ltd. should account for the above mentioned cost?

Question 16 : RM Ltd.

RM Ltd acquired a patent at a cost of Rs 80,00,000 for a period of 5 years and the product life cycle is also 5 years. The company capitalized the cost and started amortising the asset at Rs 10,00,000 per annum. After 2 years it was found that the product life cycle may continue for another 5 years from then. The net cash flows from the product during these 5 years were expected to be Rs 36,00,000, Rs 46,00,000, Rs 44,00,000, Rs 40,00,000 and Rs 34,00,000. Find out the amortization cost of the patent for each of the year.

Question 17 :

A company acquired a patent at the cost of Rs 320 lakhs. The company capitalised the cost and started amortization the asset at Rs 32 lakhs per year based on the economic benefits derived from the product manufactured under patent. After 2 years it was found that the that product life cycle may continue for another 5 years from the then (the patent is renewable and the company can get renewed after 5 years). The net cash flows from the product during these 5 years were expected to be Rs 50 lakhs, 30 lakhs, 60 lakhs, Rs 70 lakhs and Rs 40 lakhs. Find out the amortisation cost of the patent for each of years.

Question 18 : A Ltd.

A Ltd. has started developing a new production process in financial year 2011-2012. Total expenditure incurred till September 30, 2013, was Rs.1,00,00,000 . The expenditure on the development of the production process meets the recognition criteria on July 1, 2011. The records of A Ltd. show that, out of total Rs.1,00,00,000, Rs.70,00,000 were incurred during July to September, 2011. A Ltd. publishes its financial results quarterly. How A Ltd. should account for the development expenditure?

MCQs :

1. Which of the following is not covered within the scope of AS 26?
   (a) Intangible assets held-for-sale in the ordinary course of business
   (b) Assets arising from employee benefits
   (c) (a) & (b) both
   (d) Research and development activities
2. Intangible asset is recognised if it:
   (a) meets the definition of an intangible asset
   (b) is probable that future economic benefits will flow
   (c) the cost can be measured reliably
   (d) meets all of the above parameters
3. Sun Limited has purchased a computer with various additional software. These are integral part of the computer. Which of the following are true in the context of AS 26:
   (a) Recognise Computer and software as tangible asset
   (b) Recognise tangible and intangible separately
   (c) Recognise computer and software as intangible asset
   (d) Does not recognize the software as an asset.
4. Hexa Ltd developed a technology to enhance the battery life of mobile devices. Hexa has capitalised development expenditure of Rs. 5,00,000. Hexa estimates the life of the technology developed to be 3 years but the company has forecasted that 50% of sales will be in year 1, 35% in year 2 and 15% in year 3. What should be the amortisation charge in the second year of the product's life?
   (a) Rs. 2,50,000 (b) Rs. 1,75,000
   (c) Rs. 1,66,667 (d) Rs. 1,85,000

Thanks ....

Chapter 25

AS 27 – FINANCIAL REPORTING OF INTEREST IN JOINT VENTURES

CHAPTER DESIGN

1. INTRODUCTION
2. SCOPE
3. DEFINITIONS
4. CONTRACTUAL ARRANGEMENT
5. FORMS OF JOINT VENTURE
6. JOINTLY CONTROLLED OPERATIONS (JCO)
7. JOINTLY CONTROLLED ASSETS (JCA)
8. JOINTLY CONTROLLED ENTITIES (JCE)
9. CONSOLIDATED FINANCIAL STATEMENTS OF A VENTURER

1. INTRODUCTION :

You would have come across many examples where 2 or more entities would have worked together to achieve a certain purpose. Hindustan Unilever Ltd (HUL), Tata Starbucks Ltd, Tata SIA Airlines Ltd. (Vistara), etc. are a few popular examples of Joint Ventures. Entities enter into such arrangements considering sharing of risk and expense, collaboration of know-how and skill-set, while also impacted by different work-cultures and management style. Depending on the contractual arrangement, the accounting and reporting for Joint Ventures is done.

AS 27, came into effect in respect of accounting periods commenced on or after 01.04.2002.This standard set out principles and procedures for accounting of interests in joint venture and reporting of joint venture assets, liabilities, income and expenses in the financial statements of venturers and investors regardless of the structures or forms under which the joint venture activities take place.

The standard deals with three broad types of joint ventures –

1. Jointly controlled operations,
2. Jointly controlled assets and
3. Jointly controlled entities.

The requirements relating to accounting for joint ventures in consolidated financial statements according to proportionate consolidation method, as contained in AS 27, apply only when consolidated financial statements are prepared by venturer Similarly existence of a contractual arrangement distinguishes interests which involve joint control from investments in associates in which the investor has significant influence (see Accounting Standard (AS) 23, Accounting for Investments in Associates in Consolidated Financial Statements). An investor in joint venture, which does not have joint control, should report its interest in a joint venture in its consolidated financial statements in accordance with AS 13, AS 21 and AS 23.

2. SCOPE :

This Standard should be applied in accounting for interests in joint ventures and the reporting of joint venture assets, liabilities, income and expenses in the financial statements of venturers and investors, regardless of the structures or forms under which the joint venture activities take place. The provisions of this AS need to be referred to for consolidated financial statement only when CFS is prepared and presented by the venturer.

3. DEFINITIONS :

1. **A joint venture** is a contractual arrangement whereby two or more parties undertake an economic activity, which is subject to joint control.

   From the above definition we conclude that the essential conditions for any business relation to qualify as joint venture are:

- **Two or more parties coming together :** Parties can be an individual or any form of business organization say, BOI, AOP, Company, firm.
- **Venturers undertake some economic activity :** Economic activity means activities with the profit-making motive. Joint venture is separate from the regular identity of the venturers, it may be in the form of independent and separate legal organization other than regular concern of the venturer engaged in the economic activity.
- **Venturers have joint control on the economic activity :** The operating and financial decisions are influenced by the venturers and they also share the results of the economic activity.
- **There exists a contractual agreement :** The relationship between venturers is governed by the contractual agreement. This agreement can be in the form of written and signed agreement or as minutes of venturer meeting or in any other written form.

2. **Joint control** is the contractually agreed sharing of control over an economic activity.

3. **Control** is the power to govern the financial and operating policies of an economic activity so as to obtain benefits from it.

4. A **venturer** is a party to a joint venture and has joint control over that joint venture.

5. An **investor** in a joint venture is a party to a joint venture and does not have joint control over that joint venture.

6. Proportionate consolidation is a method of accounting and reporting whereby a venturer's share of each of the assets, liabilities, income and expenses of a jointly controlled entity is reported as separate line items in the venturer's financial statements.

4. CONTRACTUAL ARRANGEMENT :

The joint venture covered under this statement is governed on the basis of contractual agreement. Non-existence of contractual agreement will disqualify an organization to be covered in AS 27. Joint ventures with contractual agreement will be excluded from the scope of AS 27 only if the investment qualifies as subsidiary under AS 21, in this case, it will be covered by AS 21. Contractual agreement can be in the form of written contract, minutes of discussion between parties (venturers), articles of the concern or by-laws of the relevant joint venture.

Irrespective of the form of the contract, the content of the contract ideally should include the following points:

- The activity, duration and reporting obligations of the joint venture.
- The appointment of the board of directors or equivalent governing body of the joint venture and the voting rights of the venturers.
- Capital contributions by the venturers.
- The sharing by the venturers of the output, income, expenses or results of the joint venture.

The main object of contractual agreement is to distribute the economic control among the venturers, it ensures that no venturer should have unilateral control. The arrangement identifies those decisions in areas essential to the goals of the joint venture which require the consent of all the venturers and those decisions which may require the consent of a specified majority of the venturers. If contractual agreement is signed by a party to safeguard its right, such agreement will not make the party a venturer.

The contractual arrangement may identify one venturer as the operator or manager of the joint venture. The operator does not control the joint venture but acts within the financial and operating policies which have been agreed to by the venturers in accordance with the contractual arrangement and delegated to the operator

Question 1 : IDBI

IDBI gave loan to the joint venture entity of L&T and Tantia Construction, they signed an agreement according to which IDBI will be informed for all important decisions of the joint venture entity. Does this agreement make IDBI an investor or Venturer

Question 2 : X Ltd.

X Ltd. invested Rs 200 crore as initial capital along with Y Ltd and Z Ltd in GFH Ltd. The purpose of X Ltd making this investment is to grow the business of GFH Ltd along with the other investors. All investors have a right to attend to the meetings and to take decisions with respect to the business of GFH Ltd. All investors are actively involved in running the business of GFH Ltd and have a share in the returns generated by GFH Ltd in an agreed proportion. Identify co-venturers in this case.

Question 3 : Mr. A, M/s. B & Co. and C Ltd.

Mr. A, M/s. B & Co. and C Ltd. entered into a joint venture, where according to the agreement, all the policies making decisions on financial and operating activities will be taken in a regular meeting attended by them or their representatives. Implementation and execution of these policies will be the responsibility of Mr. A. Identify co-venturers in this case.

5. FORMS OF JOINT VENTURE :

Joint ventures may take many forms and structures, this Statement identifies them in three broad types –

- Jointly Controlled Operations (JCO),
- Jointly Controlled Assets (JCA) and
- Jointly Controlled Entities (JCE).

Any structure which satisfies the following characteristics can be classified as joint ventures:

a) Two or more venturers are bound by a contractual arrangement and

b) The contractual arrangement establishes joint control.

6. JOINTLY CONTROLLED OPERATIONS (JCO) :

Under this set up, venturers do not create a separate entity for their joint venture business but they use their own resources for the purpose. They raise any funds required for joint venture on their own, they incur any expenses and sales are also realised individually. They use same set of assets and employees for joint venture business and their own business. The joint venture agreement usually provides means by which the revenue from the jointly controlled operations and any expenses incurred in common are shared among the venturers.

Since there is no separate legal entity and venturers don't recognize the transactions separately, they do not maintain a separate set of books for joint venture. All the transactions of joint venture are recorded in their books only.

In respect of its interests in jointly controlled operations, a venturer should recognise in its separate financial statements and consequently in its consolidated financial statements:

(a) the assets that it controls and the liabilities that it incurs; and

(b) the expenses that it incurs and its share of the income that it earns from the joint venture.

Question 4 : Mr. A, Mr. B and Mr. C

Mr. A, Mr. B and Mr. C entered into a joint venture to purchase a land, construct and sell flats. Mr. A purchased a land for Rs 60,00,000 on 01.01.20X1 and for the purpose he took loan from a bank for Rs 50,00,000 @ 8% interest p.a. He also paid registering fees Rs 60,000 on the same day. Mr. B supplied the materials for Rs 4,50,000 from his godown and further he purchased the materials for Rs 5,00,000 for the joint venture. Mr. C met all other expenses of advertising, labour and other incidental expenses which turnout to be Rs 9,00,000. On 30.06.20X1 each of the venturer agreed to take away one flat each to be valued at Rs 10,00,000 each flat and rest were sold by them as follow: Mr. A for ` 40,00,000; Mr. B for Rs 20,00,000 and Mr. C for Rs 10,00,000. Loan was repaid on the same day by Mr. A along with the interest and net proceeds were shared by the partners equally.

You are required to prepare the draft Consolidated Profit & Loss Account and Joint Venture Account in the books of each venturer.

7. JOINTLY CONTROLLED ASSETS (JCA) :

Separate legal entity is not created in this form of joint venture but venturer owns the assets jointly, which are used by them for the purpose of generating economic benefit to each of them. They take up any expenses and liabilities related to the joint assets as per the contract. We can conclude the following points:

- There is no separate legal identity.
- There is a common control over the joint assets.
- Venturers use this asset to derive some economic benefit to themselves.
- Each venturer incurs separate expenses for their transactions.
- Expenses on jointly held assets are shared by the venturers as per the contract.
- In their financial statement, venturer shows only their share of the asset and total income earned by them along with total expenses incurred by them.
- Since the assets, liabilities, income and expenses are already recognised in the separate financial statements of the venturer and consequently in its consolidated financial statements, no adjustments or other consolidation procedures are required in respect of these items when the venturer presents consolidated financial statements.
- Financial statements may not be prepared for the joint venture, although the venturers may prepare accounts for internal management reporting purposes so that they may assess the performance of the joint venture.

Question 5 : A Ltd., B Ltd. and C Ltd.

A Ltd., B Ltd. and C Ltd. decided to jointly construct a pipeline to transport the gas from one place to another that was manufactured by them. For the purpose following expenditure was incurred by them: Buildings Rs 12,00,000 to be depreciated @ 5% p.a., Pipeline for Rs 60,00,000 to be depreciated @ 15% p.a., computers and other electronics for Rs 3,00,000 to be depreciated @ 40% p.a. and various vehicles of Rs 9,00,000 to be depreciated @ 20% p.a.

They also decided to equally bear the total expenditure incurred on the maintenance of the pipeline that comes to Rs 6,00,000 each year.

You are required to show the consolidated balance sheet and the extract of Statement of Profit & Loss and Balance Sheet for each venturer.

8. JOINTLY CONTROLLED ENTITIES (JCE) :

This is the format where venturer creates a new entity for their joint venture business. A jointly controlled entity is a joint venture which involves the establishment of a corporation, partnership or other entity in which each venturer has an interest. The entity operates in the same way as other enterprises, except that a contractual arrangement between the venturers establishes joint control over the economic activity of the entity. All the venturers pool their resources under new banner and this entity purchases its own assets, create its own liabilities, expenses are incurred by the entity itself and sales are also made by this entity. The net result of the entity is shared by

the venturers in the ratio agreed upon in the contractual agreement. This contractual agreement also determines the joint control of the venturer. Each venturer usually contributes cash or other resources to the jointly controlled entity. These contributions are included in the accounting records of the venturer and are recognised in its separate financial statements as an investment in the jointly controlled entity.

A jointly controlled entity maintains its own accounting records and prepares and presents financial statements in the same way as other enterprises in conformity with the requirements applicable to that jointly controlled entity

Question 6 : A Ltd.

A Ltd. a UK based company entered into a joint venture with B Ltd. in India, wherein B Ltd. will import the goods manufactured by A Ltd. on account of joint venture and sell them in India. A Ltd. and B Ltd. agreed to share the expenses & revenues in the ratio of 5:4 respectively whereas profits are distributed equally. A Ltd. invested 49% of total capital but has equal share in all the assets and is equally liable for all the liabilities of the joint venture. Following is the trial balance of the joint venture at the end of the first year:

Particulars	Dr (Rs)	Cr (Rs)
Purchases	9,00,000	
Other Expenses	3,06,000	
Sales		13,05,000
Property, Plant and Equipment	6,00,000	
Current Assets	2,00,000	
Unsecured Loans		2,00,000
Current Liabilities		1,00,000
Capital		4,01,000

Closing inventory was valued at Rs 1,00,000.

You are required to prepare the Consolidated Financial Statement.

9. CONSOLIDATED FINANCIAL STATEMENTS OF A VENTURER :

Proportionate consolidation is a method of accounting and reporting whereby a venturer's share of each of the assets, liabilities, income and expenses of a jointly controlled entity is reported as separate line items in the venturer's financial statements.

Proportionate consolidation method of accounting is to be followed except in the following cases:

A) Investment is intended to be temporary because the investment is acquired and held exclusively with a view to its subsequent disposal in the near future. And

B) joint venture operates under severe long-term restrictions, which significantly impair its ability to transfer funds to the venturers.

In both the above cases, investment of venturer in the share of the investee is treated as investment according to AS 13.

Question 7 : A Ltd.

A Ltd. entered into a joint venture with B Ltd. on 1:1 basis and a new company C Ltd. was formed for the same purpose and following is the balance sheet of all the three companies:

Particulars	A Ltd	B Ltd	C Ltd
Share Capital	10,00,000	7,50,000	5,00,000
Reserve & Surplus	18,00,000	16,00,000	12,00,000
Loans	3,00,000	4,00,000	2,00,000
Current Liabilities	4,00,000	2,50,000	1,00,000
Property, Plant and Equipment	30,50,000	26,25,000	19,50,000
Investment in JV	2,50,000	2,50,000	-
Current Assets	2,00,000	1,25,000	50,000

Prepare the balance sheet of A Ltd. and B Ltd. under proportionate consolidation method.

Question 8 : JVR Limited

JVR Limited has made investments of ` 97.84 crores in equity shares of QSR Limited in pursuance of Joint Venture agreement till 20X1-X2 (i.e., more than 12 months). The investment has been made at par. QSR Limited has been in continuous losses for the last 2 years. JVR Limited is willing to reassess the carrying amount of its investment in QSR Limited and wish to provide for diminution in value of investments. However, QSR Limited has a futuristic and profitable business plans and projection for the coming years. Discuss whether the contention of JVR Limited to bring down the carrying amount of investment in QSR Limited is in accordance with the Accounting Standard.

MCQs :

1. State which of the following statements are incorrect.
   - (i) The requirements relating to accounting for joint ventures in consolidated financial statements according to proportionate consolidation method, as contained in AS 27, applies only when consolidated financial statements are prepared by venturer.
   - (ii) The requirements relating to accounting for joint ventures in consolidated financial statements according to proportionate consolidation method, as contained in AS 27, applies irrespective whether consolidated financial statements are prepared by venturer or not.
   - (iii) An investor in joint venture, which does not have joint control, should report its interest in a joint venture in its consolidated financial statements in accordance with AS 13, AS 21 and AS 23as the case may be.

   (a) Point (i) is incorrect. (b) Point (ii) is incorrect.
   (c) Point (iii) is incorrect. (d) None of the above

2. Identify which of the following is not a feature of a Jointly controlled operations (JCO):
   (a) Each venturer has his own separate business.
   (b) There is a separate entity for joint venture business.

(c) Each venturer record only his own transactions without any separately set of books maintained for the joint venture business.
(d) There is a common agreement between all of them.

3. Identify which of the following is/are not a feature of a Jointly controlled assets (JCA):
   (i) There is a separate legal identity.
   (ii) There is a common control over the joint assets.
   (iii) Expenses on jointly held assets are shared by the venturers as per the contract.
   (iv) In their financial statement, venturer shows only their share of the asset and total income earned by them along with total expenses incurred by them.

   (a) Point no. (i) only. (b) Point no. (i) and (iii).
   (c) Point no. (iii) and (iv). (d) Point (i) and (ii).

4. Identify which is/ are features of a Jointly controlled entity (JCE):
   (i) Venturer creates a new entity for their joint venture business.
   (ii) All the venturers pool their resources under new banner and this entity purchases its own assets, create its own liabilities, expenses are incurred by the entity itself and sales are also made by this entity.
   (iii) The revenues and expenses of the entity is shared by the venturers in the ratio agreed upon in the contractual agreement.

   (a) Point no. (i) only. (b) Point no. (i) and (ii).
   (c) Point no. (iii). (d) Point no. (iii).

5. Identify the correct statements.
   From the date of discontinuing the use of the proportionate consolidation method:
   (i) If interest in entity is more than 50%, investments in such joint ventures should be accounted for in accordance with AS 21, Consolidated Financial Statements.
   (ii) If interest is 20% or more but upto 50%, investments are to be accounted for in accordance with AS 23, Accounting for Investment in Associates in Consolidated Financial Statements.
   (iii) For all other cases investment in joint venture is treated as per AS 13, Accounting for Investments.
   (iv) For this purpose, the fair value of the investment at the date on which joint venture relationship ceases to exist should be regarded as cost thereafter.

   (a) Point no. 1 and 2. (b) Point no. 1, 2 and 3.
   (c) Point no. 1, 2, 3 and 4. (d) None of the above.

Thanks ....

Chapter 26

AS 28 – IMPAIRMENT OF ASSETS

CHAPTER DESIGN

1. INTRODUCTION
2. SCOPE
3. DEFINITIONS
4. ASSESSMENT
5. VALUE IN USE
6. RECOGNISING AND MEASURING AN IMPAIRMENT LOSS
7. CASH GENERATING UNIT
8. GOODWILL
9. CORPORATE ASSETS
10. REVERSAL OF IMPAIRMENT LOSS
11. REVERSAL OF IMPAIRMENT LOSS ON A CGU
12. REVERSAL OF IMPAIRMENT OF GOODWILL

1. INTRODUCTION :

Assets as defined by Framework for preparation and Presentation of Financial Statements means "Any resource controlled by an enterprise and from which future economic benefit are expected by that enterprise from that resource.

As per the above definition assets represents future economic benefit and hence should be measured according to benefit expected out of it. However if there is decline in amount of benefit expected than the asset should be revalued to reflect the amount i.e expected benefit.

If the carrying amount of asset is more than its recoverable amount, the excess of carrying amount over its recoverable amount is called as Impairment Loss.

"Impairment Loss = Carrying Amount – Recoverable Amount"

2. SCOPE :

The standard should be applied in accounting for impairment of all assets except

1. inventories (AS 2),
2. assets arising under construction contracts (AS 7),
3. financial assets including investments covered under AS 13, and
4. deferred tax assets (AS 22).

There are chances that the provision on account of impairment losses may increase sickness of companies and potentially sick companies may actually become sick.

3. DEFINITIONS :

1. An **impairment loss** is the amount by which the carrying amount of an asset exceeds its recoverable amount

2. **Carrying amount** is the amount at which an asset is recognised after deducting any accumulated depreciation (amortisation) and accumulated impairment losses thereon.

3. The **recoverable amount** of an asset or a cash-generating unit is the higher of its Net selling Price and its value in use.

4. **Net selling price** is the amount obtainable from the sale of an asset in an arm's length transaction between knowledgeable, willing parties, less the costs of disposal

5. **Costs of disposal** are incremental costs directly attributable to the disposal of an asset, excluding finance costs and income tax expense.

6. **Value in Use** is the present value of estimated future cash flows expected to arise from the continuing use of an asset and from its disposal at the end of its useful life.

   Estimating the value in use of an asset involves the following steps:

   a. Estimating the future cash inflows and outflows arising from continuing use of the asset and from its ultimate disposal; and

   b. Applying the appropriate discount rate to these future cash flows.

Question 1 : Rainbow Limited

Jupiter Ltd, a leading manufacturer of steel is having a furnace, which is carried in the balance sheet on 31.03.2011 at Rs.250 lakh. As at that date the value in use and Fair value is Rs.200 lakh. The cost of disposal is Rs.13 lakh.

Calculate the Impairment Loss to be recognised in the books of the Company?

Question 2 : Venus Ltd.

Venus Ltd. has an asset, which is carried in the Balance Sheet on March 31, 2011 at Rs.500 lakh. As at that date the value in use is Rs.400 lakh and the fair value less costs to sells is Rs.375 lakh.

From the above data:

(a) Calculate impairment loss.

(b) Prepare journal entries for adjustment of impairment loss.

(c) Show, how impairment loss will be shown in the Balance Sheet.

Question 3 : X Ltd.

X Ltd. is having a plant (asset) carrying amount of which is Rs.100 lacs on 31.03.2015. Its balance useful life in 5 years and residual value at the end of five years is Rs.5 lacs. Estimated future cash flows from using the plant in next five years are :

For the year ended on	Estimated Cash flows (Rupees in lacs)
31.03.2016	50
31.03.2017	30
31.03.2018	30
31.03.2019	20
31.03.2020	20

Calculate "value in use" for plant if the applicable discounts rate is 10% and also calculate the recoverable amount if the net selling price of plant on 31.03.2015 is Rs.60.00 lacs.

Question 4 : X Ltd.

NDA Ltd. acquired a machine for Rs.32,00,000 on 30.11.2015. The machine has five years life with Rs.5 lacs salvage value and was depreciated using straight – line method.

Present value of future cash flow	Rs.1,35,000
Net Selling price	Rs.15,50,000
Salvage value estimated	NIL

Assuming loss for impairment is recognized for the year 31.03.2016. What should be the depreciation expense for the year ended 31.03.2017?

Question 5 : Uttaranchal Industries Ltd.

Uttaranchal Industries Ltd. gives the following estimates of cash flows relating to fixed asset on 31.12.2015. The discount rate is 15%

Year	Cash Flows (Rs. In lacs)
2016	2000
2017	3000
2018	3000
2019	4000
2020	2000

Residual value at the end of 2020 is Rs.500 lacs

Fixed asset purchased on 01.01.2013 for Rs.20000 lacs

Useful life is 8 years

Residual value estimated Rs.500 lakhs at the end of 8 years

Net Selling price Rs.10,000 lacs

Calculate on 31.12.2015

a. Carrying amount at the end of 2015

b. Value is use on 31.12.2015

c. Recoverable amount on 31.12.2015

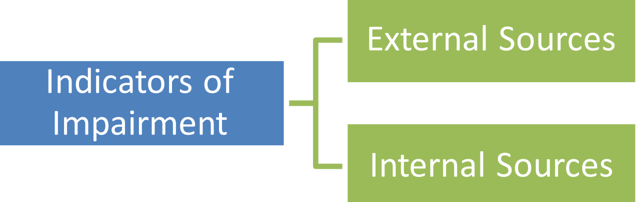
d. Impairment loss to be recognized for the year ended 31.12.2015

e. Revised carrying amount

f. Depreciation charges for 2016.

4. ASSESSMENT :

An enterprise should assess at each balance sheet date whether there is any indication that an asset may be impaired. If any such indication exists, the enterprise should estimate the recoverable amount of the asset. An asset is impaired when the carrying amount of the asset exceeds its recoverable amount. The requirements use the term 'an asset' but apply equally to an individual asset or a cash-generating unit. In assessing whether there is any indication that an asset may be impaired, an enterprise should consider, as a minimum, the following indications



External sources of information :

a. During the period, an asset's market value has declined significantly more than would be expected as a result of the passage of time or normal use.

b. Significant changes with an adverse effect on the enterprise have taken place during the period, or will take place in the near future, in the technological, market, economic or legal environment in which the enterprise operates or in the market to which an asset is dedicated.

c. Market interest rates or other market rates of return on investments have increased during the period, and those increases are likely to affect the discount rate used in calculating an asset's value in use and decrease the asset's recoverable amount materially.

d. The carrying amount of the net assets of the reporting enterprise is more than its market capitalization.

Internal Sources of Information :

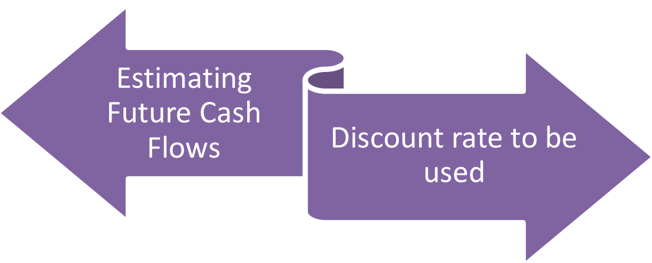
a. Evidence is available of obsolescence or physical damage of an asset.

b. Significant changes with an adverse effect on the enterprise have taken place during the period, or are expected to take place in the near future, in the extent to which, or manner in which, an asset is used or is expected to be used. These changes include plans to discontinue or restructure the operation to which an asset belongs or to dispose of an asset before the previously expected date and

c. Evidence is available from internal reporting that indicates that the economic performance of an asset is, or will be, worse than expected.

5. VALUE OF USE :

Value in use is the present value of the future cash flows expected to be derived from an asset or cashgenerating unit. Primarily two key decisions are involved in determining value in use



Question 6 :

From the following details of an asset, find out:

(a) Impairment loss and its treatment.

(b) Current year depreciation for the year end.

Particulars of assets:

Cost of Asset	Rs 56 lakhs
Usefull Life	10 years
Salvage Value	Nil
Carrying Value at the beginning of the year	Rs 27.30 lakhs
Remaining useful life	3 years
Recoverable amount at the beginning of the year	12 lakhs
Upward revaluation done in last year	14 lakhs

6. RECOGNISING AND MEASURING AN IMPAIRMENT LOSS :

When this recoverable amount is less than the carrying amount, this difference termed as Impairment Loss. It should be written off immediately as expenses to Profit & Loss Account.

Question 7 : NDA Ltd.

NDA Ltd. acquired plant on 01.04.2008 for Rs.50.00 lakhs having 10 years useful life and provides depreciation on SLM with nil residual value. On 01.04.2013. NDA Ltd revalued the plant at Rs.29 lakhs against its book value of Rs.25 lakhs and credited Rs.4 lakhs to revaluation reserve.

On 31.03.2015 the plant was impaired and its recoverable amount on this date was Rs.14 lakhs. Calculate the Impairment loss and how this loss should be treated in the accounts.

Question 8 : G Ltd.

G Ltd., acquired a machine on 1st April, 2010 for Rs.7 crore that had an estimated useful life of 7 years. The machine is depreciated on straight line basis and does not carry any residual value. On 1st April, 2014, the carrying value of the machine was reassessed at Rs.5.10 crore and the surplus arising out of the revaluation being credited to revaluation reserve. For the year ended March, 2016, conditions indicating an impairment of the machine existed and the amount recoverable ascertained to be only Rs.79 lakhs. You are required to calculate the loss on impairment of the machine and show how this loss is to be treated in the books of G Ltd. G Ltd., had followed the policy of writing down the revaluation surplus by the increased charge of depreciation resulting from the revaluation.

Question 9 : X Ltd.

X Ltd. purchased a Property, Plant and Equipment four years ago for Rs.150 lakhs and depreciates it at 10% p.a. on straight line method. At the end of the fourth year, it has revalued the asset at Rs.75 lakhs and has written off the loss on revaluation to the profit and loss account. However, on the date of revaluation, the market price is Rs.67.50 lakhs and expected disposal costs are Rs.3 lakhs. What will be the treatment in respect of impairment loss on the basis that fair value for revaluation purpose is determined by market value and the value in use is estimated at Rs.60 lakhs?

Question 10 :

An asset does not meet the requirements of environment laws which have been recently enacted. The asset has to be destroyed as per the law. The asset is carried in the Balance Sheet at the year end at Rs.6,00,000. The estimated cost of destroying the asset is Rs.70,000. How is the asset to be accounted for?

Question 11 : A plant

A plant was acquired 15 years ago at a cost of Rs.5 crores. Its accumulated depreciation as at 31st March 2014 was Rs.4.15 crores. Depreciation estimated for the financial year 2014-15 is Rs.25 lakhs. Estimated Net Selling Price as on 31st March 2014 was Rs.30 lakhs, which is expected to decline by 20% by the end of the next financial year.

Its value in use has been computed at Rs.35 lakhs as on 01st April 2014, which is expected to decrease by 30% by the end of the financial year.

i. Assuming that other conditions for applicability of the impairment Accounting Standard are satisfied, what should be the carrying amount of this plant as at 31.03.2015?

ii. How much will be the amount of write off for the financial year ended 31.03.2015?

iii. If the plant has been revalued ten years ago and the current revaluation reserves against this plant were to be Rs.12 Lakhs, how would your answer change?

If the value in use was zero and the enterprises were required to incur a cost od Rs. 2 lakhs to dispose of the plant (i.e. NSP = - Rs.2 lacs), what should be your response to questions (i) and (ii) above?

7. CASH GENERATING UNIT :

A cash generating unit is the smallest identifiable group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows from other assets or groups of assets.

If there is any indication that an asset may be impaired, the recoverable amount should be estimated for the individual asset, if it is not possible to estimate the recoverable amount of the individual asset because the value in use of the asset cannot be determined and it is probably different from scrap value. Therefore, the enterprise estimates the recoverable amount of the cash-generating unit to which the asset belongs.

If recoverable amount cannot be determined for an individual asset, an enterprise identifies the lowest aggregation of assets that generate largely independent cash inflows from continuing use. Even if part or all of the output produced by an asset or a group of assets is used by other units of the reporting enterprise, this asset or group of assets forms a separate cash-generating unit if the enterprise could sell this output in an active market. This is because this asset or group of assets could generate cash inflows from continuing use that would be largely independent of the cash inflows from other assets or groups of assets. In using information based on financial budgets/forecasts that relates to such a cashgenerating unit, an enterprise adjusts this information if internal transfer prices do not reflect management's best estimate of future market prices for the cashgenerating unit's output.

Cash-generating units should be identified consistently from period to period for the same asset or types of assets, unless a change is justified.

Question 12 : Kay Ltd.

Kay Ltd. purchased a Fixed Asset four year back at a cost of Rs.100 lakhs and depreciates it on SLM basis at 10% per annum. At the end of this year, it has revalued the asset at Rs.50 lakhs and has written off the loss on revaluation to the Profit and Loss Account. However on the date revaluation, the Market Price is Rs.45 lakhs and the expected disposal costs are Rs.2 lakhs. What will be the treatment in respect of Impairment Losses in the following situation on the basis that fair value for revaluation purpose is determined by market value?

a. Value in Use in not estimated
b. Value in use is estimated at Rs.40 lakhs
c. Value in use is estimated at Rs.48 lakhs

Question 13 : A publisher

A publisher owns 150 magazine titles of which 70 were purchased and 80 were self-created. The price paid for a purchased magazine title is recognised as an intangible asset. The costs of creating magazine titles and maintaining the existing titles are recognised as an expense when incurred. Cash inflows from direct sales and advertising are identifiable for each magazine title. Titles are managed by customer segments. The level of advertising

income for a magazine title depends on the range of titles in the customer segment to which the magazine title relates. Management has a policy to abandon old titles before the end of their economic lives and replace them immediately with new titles for the same customer segment. What is the cash-generating unit for an individual magazine title?

Question 14 : A mining entity

A mining entity owns a private railway to support its mining activities. The private railway could be sold only for scrap value and it does not generate cash inflows that are largely independent of the cash inflows from the other assets of the mine. Should the entity determine the recoverable amount for the private railway or for the mining business as a whole?

Question 15 : In north campus

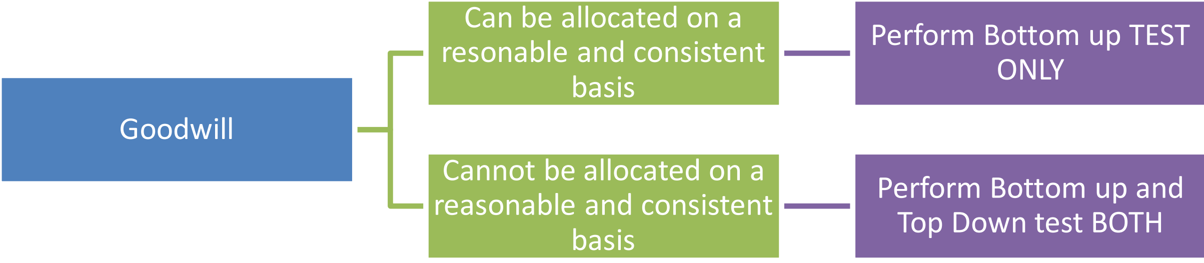
In north campus there are ten college under Delhi University having their own canteens, which provides food and beverage to be students and staff. Under a policy of the University the contract of running all the ten college canteens will be given to only one contractor. Out of these 7 canteens are profitable but 3 are loss making. Identify cash generating units.

Question 16 : Reliance Ltd.

Reliance Ltd. is a multi-product manufacturing company, its corporate office is housed in a building, as the area if building is large, the Reliance Ltd. has let out 1/3 area of building at a monthly rent of Rs.50 lakhs, the lease agreement with tenant is for next 5 years. Is the building cash-generating unit? If not what is the cash generating unit out of building?

8. GOODWILL :

Goodwill does not generate cash flows independently from other assets or groups of assets and, therefore, the recoverable amount of goodwill as an individual asset cannot be determined. As a consequence, if there is an indication that goodwill may be impaired, recoverable amount is determined for the cashgenerating unit to which goodwill belongs. This amount is then compared to the carrying amount of this cash-generating unit and any impairment loss is recognized.



Question 17 : A Ltd.

On 1/1/2003 A Ltd. acquired net assets of B Ltd. for Rs.70,00,000. The fair value of net assets was estimated at Rs.60,00,000. The goodwill, if any, was to be amortised over a period of 8 years, whereas the net assets were to be depreciated over 10 years (with no salvage value). During the year 2006, there was an indication of the impairment loss in respect of these assets. So, the cash inflows for the remaining life of the assets were estimated to be Rs.12,00,000, Rs.9,50,000, Rs.8,00,000, Rs.8,30,000, Rs.8,00,000, Rs.8,50,000 and Rs.6,00,000 respectively. The discount rate applicable to the company is 12%.

Find out impairment loss to be recognised by the company. How should it be treated?

Question 18 : X Ltd.

On 1/1/2000 X Ltd acquired Assets of Y Ltd. at a price of Rs.90,00,000. The fair value of Assets was established to be Rs.75,00,000. Assets is to be depreciated @10% and goodwill over 5 years. At the beginning of 2003 new govt. was voted to power and has some policy changes that affected the entity badly. Recoverable Amount was Rs.49,00,000. Calculate Impairment Loss and show the treatment.

Question 19 : A Ltd.

A Ltd. has 3 CGU with the fair value of Assets of these units in the ratio of 3 : 2 : 1 for unit A, B and C respectively.

B Ltd. acquired all the three cash generating units of A Ltd. at a price of Rs.2,500 lacs and recognised a goodwill of Rs.600 lacs at the time of acquisition. After a few years, it is found that unit A is incurring losses and the recoverable amount of unit A is 750 lacs. Presently the carrying amount of these units are Rs.725 lacs, Rs.500 lacs and Rs.220 lacs. The goodwill is appearing at Rs.420 lacs in the financial statements. Find the impairment loss to be recognised for CGU A, if

A. Goodwill can be allocated to cash generating units on a reasonable basis, and

B. Goodwill cannot be allocated to cash generating units and the recoverable amount of the three units taken together is

   (i) Rs. 1700 or

   (ii) Rs. 1400

Question 20 :

A cash generating unit has these net assets

	Rs in million
Goodwill	10
Property	20

Plant and Equipment	30
Total	**60**

The recoverable Amount has been determined at Rs.45 million.

Required :

Allocate the impairment loss to net assets of the entity.

9. CORPORATE ASSETS :

Corporate Assets do not generate separate cash inflows, the recoverable amount of individual corporate assets cannot be determined unless management decided to dispose the Assets Is there is indication that corporate asset may be impaired, recoverable amount is determined with reference to Cash generating unit to which corporate asset belongs. Corporate Assets shall be treated in similar way to goodwill

Question 21 : An Enterprise

An enterprise has 3 CGU I, II, and III which have carrying amount of Rs.20,00,000, Rs.30,00,000 and Rs.40,00,000 respectively. There are some indications for the impairment of assets of the enterprise. Besides the CGU there is a Head office (H.O) building and Research centre appearing at the value of Rs.40,00,000 and Rs.15,00,000 respectively.

The remaining life of unit 1 is 8 years while units II and III have life of 10 years. The carrying amount of H.O can be allocated on a reasonable basis to CGU I, II and III but the carrying amount of Research centre cannot be so allocated.

In order to identify the impairment loss, the net selling price of these unit were estimated at Rs.20,00,000, Rs.28,00,000 and Rs.50,00,000 respectively. However, the annual cash flows expected from these units over the remaining life are Rs.3,20,000 (unit 1), Rs.3,10,000 (unit II) and Rs.5,70,000 (unit III). The discount rate applicable to the enterprise is 12%. The recoverable amount of the total enterprise is Rs.1,15,00,000. Find out the impairment loss to be recognised and show the allocation of impairment loss to be recognised and show the allocation of impairment loss.

10. REVERSAL :

An entity is required to assess at the end of each reporting period whether there is any indication that an impairment loss recognised in prior periods for an asset other than goodwill may no longer exist or may have decreased. If any such indication exists, the entity shall estimate the recoverable amount of that asset. If impairment loss was written off to profit and loss account, then the reversal of impairment loss should be recognized as income in the financial statement immediately.

If impairment loss was adjusted with the Revaluation Reserve; then reversal of impairment loss will be written back to the reserve account to the extent it was adjusted, any surplus will be recognised as revenue.

11. REVERSAL OF IMPAIRMENT LOSS ON A CGU :

- A reversal of an impairment loss for a cash-generating unit shall be allocated to the assets of the unit, except for goodwill, pro rata with the carrying amounts of those assets. These increases in carrying amounts shall be treated as reversals of impairment losses for individual assets and recognised as discussed above.
- In allocating a reversal of an impairment loss for a cash-generating unit, the carrying amount of an asset shall not be increased above the lower of: a) its recoverable amount (if determinable); and b) the carrying amount that would have been determined (net of amortisation or depreciation) had no impairment loss been recognised for the asset in prior periods.
- The amount of the reversal of the impairment loss that would otherwise have been allocated to the asset is allocated pro rata to the other assets of the unit, except for goodwill.

12. REVERSAL OF IMPAIRMENT OF GOODWILL

This Statement does not permit an impairment loss to be reversed for goodwill because of a change in estimates, an impairment loss recognised for goodwill should not be reversed in a subsequent period unless:

a. The impairment loss was caused by a specific external event of an exceptional nature that is not expected to recur; and

b. Subsequent external events have occurred that reverse the effect of that event

Question 22 : An enterprise

An enterprise has 3 CGU I, II, and III which have carrying amount of Rs.20,00,000, Rs.30, 00,000 and Rs.40,00,000 respectively. There are some indications for the impairment of assets of the enterprise. Besides the CGU there is a Head office (H.O) building and Research centre appearing at the value of Rs.40,00,000 and Rs.15,00,000 respectively.

The remaining life of unit 1 is 8 years while units II and III have life of 10 years. The carrying amount of H.O can be allocated on a reasonable basis to CGU I, II and III but the carrying amount of Research centre cannot be so allocated.

In order to identify the impairment loss, the net selling price of these unit were estimated at Rs.20,00,000, Rs.28,00,000 and Rs.50,00,000 respectively. However, the annual cash flows expected from these units over the remaining life are Rs.3,20,000 (unit 1), Rs.3,10,000 (unit II) and Rs.5,70,000 (unit III). The discount rate applicable to the enterprise

is 12%. The recoverable amount of the total enterprise is Rs.1,15,00,000. Find out the impairment loss to be recognised and show the allocation of impairment loss to be recognised and show the allocation of impairment loss.

Question 23 : P Ltd.

At the end of year 2000 P Ltd acquired Assets of Q Ltd. at a price of Rs.90,00,000. The fair value of Assets was established to be Rs.75,00,000. Assets is to be depreciated @10% and goodwill over 5 years. At the beginning of 2003 new govt. was voted to power and has some policy changes that affected the entity badly. Recoverable Amount was Rs.49,00,000.

During the year 2005, the government adopted liberal policies which are expected to improve the working position and profitability of P Ltd. the recoverable amount at the end of year 2005, is estimated at Rs.40,00,000.

Find out the impairment loss in year 2003 and the reversal of impairment loss and its treatment in the year 2005.

Question 24 : RM Ltd.

RM Ltd. is in the business of manufacturing and export. In 2005, the government put a restriction on export of goods leading to impairment of its Assets. RM Ltd acquired at the end of 2001, identifiable assets worth Rs.400 lakhs for Rs.600 lakhs, the balance being treated as goodwill. The usefull life of the identifiable assets is 15 years and depreciated on SLM. When government put the restriction at the end of 2005, the company recognised the impairment loss by determining the recoverable amount of assets at Rs.272 lakhs. In 2007, the restriction was withdrawn by the government and due to this favourable change RM Ltd. estimates its recoverable amount at Rs.342 lakhs.

You are required to

a. calculate and allocate impairment loss in 2005

b. compute amount of Reversal of impairment loss and its allocation in 2007.

MCQs :

1. If there is indication that an asset may be impaired but the recoverable amount of the asset is more than the carrying amount of the asset, the following are true:

   (a) No further action is required and the company can continue the asset in the books at the book value itself.

   (b) The entity should review the remaining useful life, scrap value and method of depreciation and amortization for the purposes of AS 10.

   (c) The entity can follow either (a) or (b).

(d) The entity should review the scrap value and method of depreciation and amortization for the purposes of AS 10.

2. In case Goodwill appears in the Balance Sheet of an entity, the following is true:
   (a) Apply Bottom up test if goodwill cannot be allocated to CGU (cash generating unit) under review.
   (b) Apply Top down test if goodwill cannot be allocated to CGU (cash generating unit) under review.
   (c) Apply both Bottom up test and Top down test if goodwill cannot be allocated to CGU (cash generating unit) under review.
   (d) Apply either Bottom up test or Top down test if goodwill cannot be allocated to CGU (cash generating unit) under review.
3. In case of Corporate assets in the Balance Sheet of an entity, the following is true:
   (a) Apply Bottom up test if corporate assets cannot be allocated to CGU (cash generating unit) under review.
   (b) Apply Top down test if corporate assets cannot be allocated to CGU (cash generating unit) under review.
   (c) Apply both Bottom up test and Top down test if corporate assets cannot be allocated to CGU (cash generating unit) under review.
   (d) Apply either Bottom up test or Top down test if corporate assets cannot be allocated to CGU (cash generating unit) under review.
4. In case of reversal of impairment loss, which statement is true:
   (a) Goodwill written off can never be reversed.
   (b) Goodwill written off can be reversed without any conditions to be met.
   (c) Goodwill written off can be reversed only if certain conditions are met.
   (d) Goodwill written off can be reversed.

Thanks ....

Rahul Malkan

Chapter 27

AS 29 – PROVISIONS, CONTINGENT LIABILITIES & CONTINGENT ASSETS

CHAPTER DESIGN

1. INTRODUCTION
2. SCOPE
3. PROVISIONS
4. CONTINGENT LIABILITIES
5. CONTINGENT ASSETS

1. INTRODUCTION :

The objective of AS 29 (Revised) is to ensure that appropriate recognition criteria and measurement bases are applied to provisions and contingent liabilities and sufficient information is disclosed in the notes to the financial statements to enable users to understand their nature, timing and amount. The objective of AS 29 (Revised) is also to lay down appropriate accounting for contingent assets.

2. SCOPE :

AS 29 should be applied in accounting for provisions and contingent liabilities and in dealing with contingent assets, other than

a. Those resulting from financial instruments that are carried at fair value;
b. Those resulting from executory contracts except where the contract is onerous;
c. Those arising in insurance enterprises from contracts with policy-holders; and
d. Those covered by another Accounting Standard.

Where another Accounting Standard such as AS 7; AS 9; AS 15; AS 19 and AS 22 deals with a specific type of provision, contingent liability or contingent asset, an enterprise applies that Standard instead of AS 29.

3. PROVISIONS :

3.1 Definitions :

1. Provisions :

A **Provision** is a liability which can be measured only by using a substantial degree of estimation.

2. Liability :

A **Liability** is a present obligation of the enterprise arising from past events, the settlement of which is expected to result in an outflow from the enterprise of resources embodying economic benefits.

3. Obligating Event :

An **Obligating event** is an event that creates an obligation that results in an enterprise having no realistic alternative to settling that obligation.

Example :

X Ltd. entered into a contract with Y Ltd. for supply of some material. As per the terms of contract in case of breach of contract, the party who breaches the contract has to pay Rs 50,00,000 to other party. X Ltd. breached the contract with

Y Ltd. Now in this case the obligating event is the breach of contract that gave rise to present obligation and X Ltd. must settle the obligation.

4. A **legal obligation** is an obligation that derives from:
   (a) a contract (through its explicit or implicit terms);
   (b) legislation; or
   (c) other operation of law.

Example :
In the aforesaid example regarding breach of the contract, the obligation is a legal obligation that arises from the terms of contract.

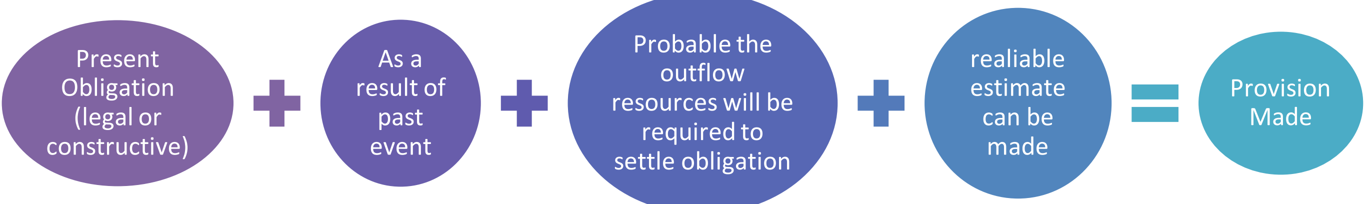
5. A constructive obligation is an obligation that derives from an entity's actions where:
   (a) by an established pattern of past practice, published policies or a sufficiently specific current statement, the entity has indicated to other parties that it will accept certain responsibilities; and
   (b) as a result, the entity has created a valid expectation on the part of those other parties that it will discharge those responsibilities.

Example :
X Ltd. is engaged in the manufacture of fertilisers. Effluents discharged in the manufacturing process have polluted the river near the manufacturing plant. The residents of the nearby locality launched a massive agitation against the pollution. X Ltd. agreed to their demands to reduce the water pollution by installing the necessary Effluent Treatment Plant. However, during the year no steps are taken to install the plant. No legislation requiring the company to reduce its pollution is in existence. In this case, though there is no law but by promising to take steps to reduce pollution, X Ltd. has created a valid expectation on the part of public that it will discharge its responsibilities. So the obligation in this case is a constructive obligation.

6. **Present obligation** - an obligation is a present obligation if, based on the evidence available, its existence at the balance sheet date is considered probable, i.e., more likely than not.

7. **Possible obligation** - an obligation is a possible obligation if, based on the evidence available, its existence at the balance sheet date is considered not probable.

3.2. Recognition :



A provision should be recognised when:

(a) An enterprise has a present obligation as a result of a past event;

(b) It is probable that an outflow of resources embodying economic benefits will be required to settle the obligation; and

(c) A reliable estimate can be made of the amount of the obligation.

If these conditions are not met, no provision should be recognised.

Question 1 : X Shipping Ltd.

X Shipping Ltd. is required by law to overhaul its shipping fleet once in every 3 years. The company's finance team was of the view that recognising the costs only when paid would prevent matching of revenue earned all the time with certain costs of large amounts which are incurred occasional. Thereby, it has formulated an accounting policy of providing in its books of account for the future cost of maintenance (overhauls, annual inspection etc.) by calculating a rate per hours sailed on sea and accumulating a provision over time. The provision is adjusted when the expenditure is actually incurred. Is the accounting policy of X Shipping Ltd. correct?

Question 2 : X Chemical Ltd.

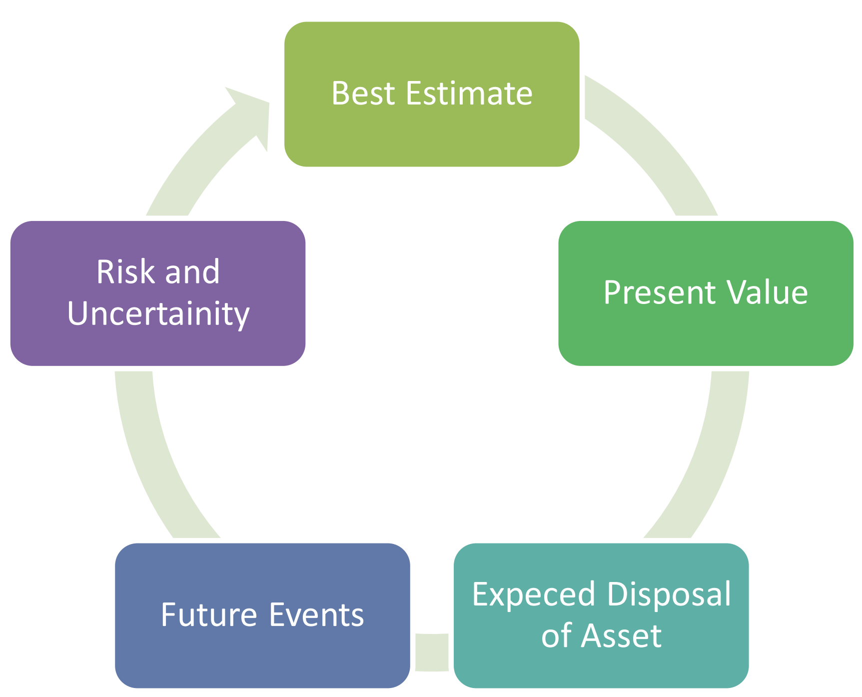
X Chemical Ltd. is operating in the vicinity of a river since 20 years. A community living near X Chemical Ltd. claims that its operations has caused contamination of drinking water. X Chemical Ltd. has received notice from the governmental environmental agency that official investigations will be made into claims of pollution caused by the entity. If it is found that X Chemical Ltd. has caused contamination, then penalties and fine would be levied on it.

X Chemical Ltd. believes that it has implemented all environmental safety measures to an extent that it is unlikely to cause pollution. Management is not sure whether it has all the information about the entire 20 years. Therefore, neither management nor external

experts are able to assess X Chemical Ltd.'s responsibility until the investigation has completed.

In such situation, how should management of X Chemical Ltd. account for a liability?

3.3 Measurement :



1. Best Estimate :

The amount recognised as a provision should be the best estimate of the expenditure required to settle the present obligation at the balance sheet date.

The estimates of outcome and financial effect are determined by the judgment of the management of the enterprise, supplemented by experience of similar transactions and, in some cases, reports from independent experts.

2. Present Value :

The amount of a provision should not be discounted to its present value except in case of decommissioning, restoration and similar liabilities that are recognised as cost of Property, Plant and Equipment. The discount rate (or rates) should be a pre-tax rate (or rates) that reflect(s) current market assessments of the time value of money and the risks specific to the liability. The discount rate(s) should not reflect risks for which future cash flow estimates have been adjusted. Periodic unwinding of discount should be recognised in the statement of profit and loss.

Question 3 : RM Solar Power Ltd.

RM Solar Power Ltd., a power company, has a present obligation to dismantle its plant after 35 years of useful life. RM Solar Power Ltd. cannot cancel this obligation or transfer to third party. RM Solar Power Ltd. has estimated the total cost of dismantling at Rs.50,00,000, the present value of which is Rs.30,00,000. Based on the facts and circumstances, RM Solar Power Ltd. considers the risk factor of 5% i.e., the risk that the actual outflows would be more from the expected present value. How should RM Solar Power Ltd. account for the obligation?

3. Risks and Uncertainty :

The risks and uncertainties that inevitably surround many events and circumstances should be taken into account in reaching the best estimate of a provision.

4. Future Events :

Future events that may affect the amount required to settle an obligation should be reflected in the amount of a provision where there is sufficient objective evidence that they will occur.

For example, an enterprise may believe that the cost of cleaning up a site at the end of its life will be reduced by future changes in technology. The amount recognised reflects a reasonable expectation of technically qualified, objective observers, taking account of all available evidence as to the technology that will be available at the time of the clean-up. Thus, it is appropriate to include, for example, expected cost reductions associated with increased experience in applying existing technology or the expected cost of applying existing technology to a larger or more complex clean-up operation than has previously been carried out. However, an enterprise does not anticipate the development of a completely new technology for cleaning up unless it is supported by sufficient objective evidence.

Question 4 : RM Chemicals Ltd.

RM Chemicals Ltd. engaged in the chemical industry causes environmental damage by dumping waste in the river near its factory. It does not clean up because there is no environmental legislation requiring cleaning up and RM Chemicals Ltd. is causing damage for last 40 years. As at March 31, 2012, the State Legislature has passed a path breaking legislation requiring all polluting factories to clean-up the river water already contaminated. The formal Gazette notification of the law is pending. How should RM Chemicals Ltd. deal with this situation?

5. Expected Disposal of Assets :

Gains on the expected disposal of assets are not taken into account in measuring a provision, even if the expected disposal is closely linked to the event giving rise to the provision. Instead, an enterprise recognises gains on expected disposals of assets at the time specified by the Accounting Standard dealing with the assets concerned.

6. Reimbursements :

An, enterprise with a present obligation may be able to seek reimbursement of part or all of the expenditure from another party, for example via:

- An insurance contract arranged to cover a risk;
- An indemnity clause in a contract; or
- A warranty provided by a supplier.

In most cases, the enterprise will remain liable for the whole of the amount in question so that the enterprise would have to settle the full amount if the third party failed to pay for any reason. In this situation, a provision is recognised for the full amount of the liability, and a separate asset for the expected reimbursement is recognised when it is virtually certain that reimbursement will be received if the enterprise settles the liability.

Party fails to pay. In such a case, the enterprise has no liability for those costs and they are not included in the provision.

An obligation for which an enterprise is jointly and severally liable is a contingent liability to the extent that it is expected that the obligation will be settled by the other parties.

Table – Reimbursements :

Some or all of the expenditure required to settle a provision is expected to be reimbursed by another party.		
The enterprise has no obligation for the part of the expenditure to be reimbursed by the other party.	The obligation for the amount expected to be reimbursed remains with the enterprise and it is virtually certain that reimbursement will be received if the enterprise settles the provision.	The obligation for the amount expected to be reimbursed remains with the enterprise and the reimbursement is not virtually certain if the enterprise settles the provision.

The enterprise has no liability for the amount to be reimbursed.	The reimbursement is recognised as a separate asset in the balance sheet and may be offset against the expense in the statement of profit and loss. The amount recognised for the expected reimbursement does not exceed the liability.	The expected reimbursement is not recognised as an asset.
No disclosure is required.	The reimbursement is disclosed together with the amount recognised for the reimbursement.	The expected reimbursement is disclosed.

Question 5 : X Beauty Solutions Ltd.

X Beauty Solutions Ltd. is selling cosmetic products under its brand name 'B', but it is getting its product manufactured from Y Ltd. It has an understanding (enforceable agreement) with Y Ltd. that if the company becomes liable for any damage claims, due to any injury or harm to the customer of the cosmetic products, 30% will be reimbursed to it by Y Ltd. During the financial year 2011-2012, a claim of Rs.30,00,000 becomes payable to customers by X Beauty Solutions Ltd. How should X Beauty Solutions Ltd. account for the claim that becomes payable?

3.4 Changes in Provisions :

Provisions should be reviewed at each balance sheet date and adjusted to reflect the current best estimate. If it is no longer probable that an outflow of resources embodying economic benefits will be required to settle the obligation, the provision should be reversed.

3.5 Use of Provisions :

A provision should be used only for expenditures for which the provision was originally recognised. Only expenditures that relate to the original provision are adjusted against it. Adjusting expenditures against a provision that was originally recognised for another purpose would conceal the impact of two different events.

3.6 Application of Recognition and Measurement Rules :

1. **Future Operating Losses :**

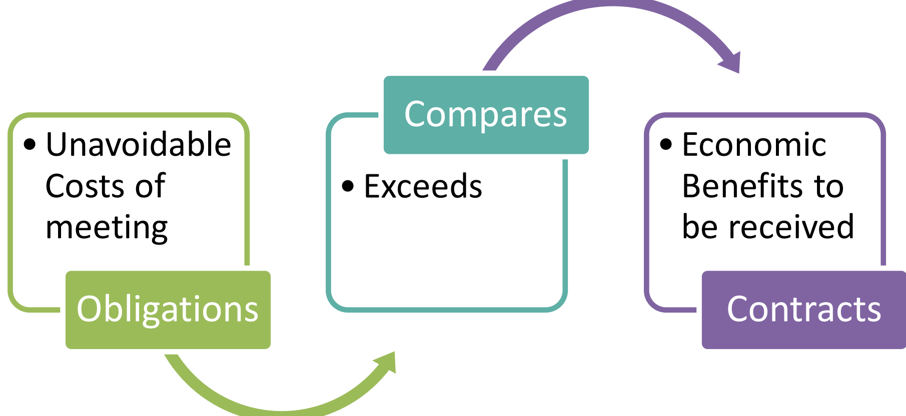
Future operating losses do not meet the definition of a liability and the general recognition criteria, therefore provisions should not be recognised for future operating losses.

Question 6 : X Packaging Ltd.

X Packaging Ltd. has two segments, packaging division and paper division. In March 2011, the board of directors approved and announced a formal plan to sell the paper division in June 2011. Operating losses of the paper division are estimated to be approximately R. 50,00,000 during the period from April 1, 2011 to the expected date of disposal. Management of X Packaging Ltd. wants to include the future operating loss of Rs.50,00,000 in a provision for restructuring in the financial statements for the period ended March 31, 2011. Can X Packaging Ltd. include these operating losses in a provision for restructuring?

2. Onerous Contracts :

If an entity has a contract that is onerous, the present obligation under the contract should be recognised and measured as a provision



Question 7 : X Metals Ltd.

X Metals Ltd. had entered into a non-cancellable contract with Y Ltd. to purchase 10,000 units of raw material at Rs.50 per unit at a contract price of Rs.5,00,000. As per the terms of contract, X Metals Ltd. would have to pay Rs.60,000 to exit the said contract. X Metals Ltd. has discontinued manufacturing the product that would use the said raw material. For that X Metals Ltd. has identified a third party to whom it can sell the said raw material at Rs 45 per unit.

How should X Metals Ltd. account for this transaction in its books of account in respect of the above contract?

3. Restructuring :

The following are examples of events that may fall under the definition of restructuring:

(a) Sale or termination of a line of business

(b) The closure of business locations in a country or region or the relocation of business activities from one country or region to another

(c) Changes in management structure, for example, eliminating a layer of management

(d) Fundamental re-organisations that have a material effect on the nature and focus of the enterprise's operations

A provision for restructuring costs is recognised only when the recognition criteria for provisions are met. No obligation arises for the sale of an operation until the enterprise is committed to the sale, i.e., there is a binding sale agreement. Until there is a binding sale agreement, the enterprise will be able to change its mind and indeed will have to take another course of action if a purchaser cannot be found on acceptable terms.

Question 8 : X Cements Ltd.

X Cements Ltd. has three manufacturing units situated in three different states of India. The board of directors of X Cements Ltd., in their meeting held on January 10, 2011, decided to close down its operations in one particular state on account of environmental reasons. A detailed formal plan for shutting down the above unit was also formalised and agreed by the board of directors in that meeting, which specifies the approximate number of employees who will be compensated and expenditure expected to be incurred. Date of implementation of plan has also been mentioned. Meetings were also held with customers, suppliers, and workers to communicate the features of the formal plan to close down the operations in the said state, and representatives of all interested parties were present in those meetings. Do the actions of the board of directors create a constructive obligation that needs a provision for restructuring?

3.7 Disclosures :

For each class of provision, an enterprise should disclose:

(a) The carrying amount at the beginning and end of the period;

(b) Additional provisions made in the period, including increases to existing provisions;

(c) Amounts used (i.e. incurred and charged against the provision) during the period; and

(d) Unused amounts reversed during the period.

Note : SMCs are exempt from the above disclosure requirements of AS 29 (Revised)

An enterprise should disclose the following for each class of provision:

(a) A brief description of the nature of the obligation and the expected timing of any resulting outflows of economic benefits;

(b) An indication of the uncertainties about those outflows. Where necessary to provide adequate information, an enterprise should disclose the major assumptions made concerning future events, and

(c) The amount of any expected reimbursement, stating the amount of any asset that has been recognised for that expected reimbursement.

Note: SMCs are exempt from the above disclosure requirements of AS 29 (Revised)

4. CONTINGENT LIABILITIES :

4.1 Definitions :

A Contingent liability is:

(a) A possible obligation that arises from past events and the existence of which will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the enterprise; or

(b) A present obligation that arises from past events but is not recognised because:

- (i) It is not probable that an outflow of resources embodying economic benefits will be required to settle the obligation; or
- (ii) A reliable estimate of the amount of the obligation cannot be made.

Present obligation - an obligation is a present obligation if, based on the evidence available, its existence at the balance sheet date is considered probable, i.e., more likely than not.

Possible obligation - an obligation is a possible obligation if, based on the evidence available, its existence at the balance sheet date is considered not probable.

4.2 Recognition :

- An entity should not recognise a contingent liability.
- A contingent liability should be disclosed, if the possibility of an outflow of resources embodying economic benefits is not remote.
- Where an entity is jointly and severally liable for an obligation, the part of the obligation that is expected to be met by other parties should be treated as a contingent liability.

- The entity should recognise a provision for the part of the obligation for which an outflow of resources embodying economic benefits is probable, except in the extremely rare circumstances where no reliable estimate can be made.
- Contingent liabilities may develop in a way not initially expected. Therefore, they are assessed continually to determine whether an outflow of resources embodying economic benefits has become probable.
- If it becomes probable that an outflow of future economic benefits will be required for an item previously dealt with as a contingent liability, a provision should be recognised in the financial statements of the period in which the change in probability occurs (except in the extremely rare circumstances where no reliable estimate can be made).

4.3 Provisions v/s Contingent Liabilities :

Where, as a result of past events, there may be an outflow of resources embodying future economic benefits in settlement of: (a) a present obligation the one whose existence at the balance sheet date is considered probable; or (b) a possible obligation the existence of which at the balance sheet date is considered not probable.		
There is a present obligation that probably requires an outflow of resources and a reliable estimate can be made of the amount of obligation.	There is a possible obligation or a present obligation that may, but probably will not, require an outflow of resources.	There is a possible obligation or a present obligation where the likelihood of an outflow of resources is remote.
A provision is recognised.	No provision is recognised.	No provision is recognised.
Disclosures are required for the provision.	Disclosures are required for the contingent liability.	No disclosure is required.

5. CONTINGENT ASSETS :

A **Contingent asset** is a possible asset that arises from past events the existence of which will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the enterprise.

An enterprise should not recognise a contingent asset, since this may result in the recognition of income that may never be realised. However, when the realisation of income is virtually certain, then the related asset is not a contingent asset and its recognition is appropriate. A contingent asset is not disclosed in the financial statements. It is usually disclosed in the report of the approving authority (Board of Directors in the case of a company, and, the corresponding

approving authority in the case of any other enterprise), where an inflow of economic benefits is probable.

Contingent assets are assessed continually and if it has become virtually certain that an inflow of economic benefits will arise, the asset and the related income are recognised in the financial statements of the period in which the change occurs.

Where, as a result of past events, there is a possible asset whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future evens not wholly within the control of the entity		
The inflow of economic benefits is virtually certain	**The inflow of economic benefits is probable, but not virtually certain**	**The inflow is not probable**
The asset is not contingent and its recognition is appropriate	No asset is recognised	No asset is recognised
	Disclosures are required	No disclosure is required

MCQs :

1. Which of the following best describes a provision?
   (a) A provision is a liability of uncertain timing or amount.
   (b) A provision is a possible obligation of uncertain timing.
   (c) A provision is a credit balance set up to offset a contingent asset so that the effect on the statement of financial position is nil.
   (d) A provision is a possible obligation of uncertain amount.
2. X Co is a business that sells second hand cars. If a car develops a fault within 30 days of the sale, X Co will repair it free of charge. At 1st March 20X1, X Co had made a provision for repairs of Rs. 25,000. At 31st March 20X1, X Co calculated that the provision should be Rs. 20,000. What entry should be made for the provision in X Co's income statement for the month 31st March 20X1?
   (a) A charge of Rs. 5,000 (b) A credit of Rs. 5,000
   (c) A charge of Rs. 20,000 (d) A credit of Rs. 25,000
3. Which of the following item does the statement below describe?
   "A possible obligation that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the entity's control"
   (a) A provision (b) A current liability
   (c) A contingent liability (d) Deferred tax liability

4. Z Ltd has commenced a legal action against Y Ltd claiming substantial damages for supply of a faulty product. The lawyers of Y Ltd have advised that the company is likely to lose the case, although the chances of paying the claim is not remote. The estimated potential liability estimated by the lawyers are:

   Legal cost (to be incurred irrespective of the outcome of the case) Rs. 50,000

   Settlement if the claim is required to be paid Rs. 5,00,000

   What is the appropriate accounting treatment in the books of Z Ltd.?

   (a) Create a Provision of Rs. 5,50,000

   (b) Make a Disclosure of a contingent liability of Rs. 5,50,000

   (c) Create a Provision of Rs. 50,000 and make a disclosure of contingent liability of Rs. 5,00,000

   (d) Create a Provision of Rs. 5,00,000

Thanks ....

Rahul Malkan

Chapter 28

PREPARATION OF FINANCIAL STATEMENTS

CHAPTER DESIGN

1. MAINTENANCE OF BOOKS OF ACCOUNT
2. FINAL ACCOUNTS
3. MANAGERIAL REMUNERATION
4. DIVISIBLE PROFITS
5. FINANCIAL STATEMENTS AS PER SCHEDULE III OF COMPANIES ACT 2013

1. MAINTENANCE OF BOOKS OF ACCOUNTS :

As per Section 128 of the Companies Act, 2013, Every company should prepare and keep at its registered office books of account and other relevant books and papers and financial statement for every financial year which give a true and fair view of the state of the affairs of the company

2. FINAL ACCOUNTS :

Under Section 129 of the Companies Act, 2013, at the annual general meeting of a company, the Board of Directors of the company should lay financial statements before the company:

Financial Statements as per Section 2(40) of the Companies Act, 2013, inter-alia include –

(i) a balance sheet as at the end of the financial year;

(ii) a profit and loss account, or in the case of a company carrying on any activity not for profit, an income and expenditure account for the financial year;

(iii) cash flow statement for the financial year;

(iv) a statement of changes in equity, if applicable; and

(v) any explanatory note annexed to, or forming part of, any document referred to in (i) to (iv) above

As per section 133 of the Companies Act, it is mandatory to comply with accounting standards notified by the Central Government from time to time

As per section 129 of the Companies Act, 2013, Financial statements should give a true and fair view of the state of affairs of the company or companies and comply with the accounting standards notified under section133 and should be in the form or forms as may be provided for different class or classes of companies in Schedule III under the Act.

3. MANAGERIAL REMUNERATION :

Managerial remuneration is calculated as a percentage of profit. Managerial remuneration payable by a company is governed by various sections of the Companies Act, 2013 and also Schedule V under the Companies Act, 2013.

Section 197 prescribes the overall maximum managerial remuneration payable and also managerial remuneration in case of absence or inadequacy of profits.

As per Section 197 of the Companies Act, 2013, total managerial remuneration payable by a public company, to its directors, including managing director and whole-time director, and its manager in respect of any financial year should not exceed 11% of the net profits of that company for that financial year computed in the manner laid down in section 198 except that the remuneration of the directors should not be deducted from the gross profits. The company in general meeting may, with the approval of the Central Government, authorise the payment of remuneration exceeding 11% of the net profits of the company, subject to the provisions of Schedule V.

Provided further that, except with the approval of the company in general meeting,—

(i) the remuneration payable to any one managing director; or whole-time director or manager should not exceed 5% of the net profits of the company and if there are more than one such director, remuneration should not exceed 10% of the net profits to all such directors and manager taken together;

(ii) the remuneration payable to directors who are neither managing directors nor whole-time directors should not exceed,—

  (A) 1% of the net profits of the company, if there is a managing or wholetime director or manager;

  (B) 3% of the net profits in any other case.

Schedule V consists of four parts.

- Part I lays down conditions to be fulfilled for the appointment of a managing or whole-time director or a manager without the approval of the Central Government.
- Part II deals with remuneration payable to managerial person by companies having profits and also by companies having no profits or inadequate profits.
- Part III specifies the provisions applicable to parts 1 and 2 of this schedule and
- Part IV deals with Central Government's power to relax any requirements in this Schedule

The relevant details given under Part II of Schedule V are as follows:

1. **Section I - Remuneration payable by companies having profits:**
   Subject to the provisions of section 197, a company having profits in a financial year may pay remuneration to a managerial person or persons not exceeding the limits specified in such section.

2. **Section II - Remuneration payable by companies having no profit or inadequate profit:**
   Where in any financial year during the currency of tenure of a managerial person, a company has no profits or its profits are inadequate, it may, pay remuneration to the managerial person not exceeding the higher of the limits under (A) and (B) given below:-

	(1)	(2)
	Where the effective capital is	Limit of yearly remuneration payable should not exceed (Rupees)
(i)	Negative or less than 5 crores	60 Lakhs
(ii)	5 crores and above but less than 100 crores	84 Lakhs

(iii)	100 crores and above but less than 250 crores	120 Lakhs
(iv)	250 crores and above	120 lakhs plus 0.01% of the effective capital in excess of ` 250 crores.

Provided that the remuneration in excess of the above limits may be paid if the resolution passed by the shareholders is a special resolution.

Question 1 : Mudra Ltd.

The following is the Draft Profit & Loss A/c of Mudra Ltd., the year ended 31st March, 20X1:

	Rs.		Rs.
To Administrative, Selling and distribution expenses	8,22,542	By Balance b/d	5,72,350
To Directors fees	1,34,780	By Balance from Trading A/c	40,25,365
To Interest on debentures	31,240	By Subsidies received from Govt.	2,73,925
To Managerial remuneration	2,85,350		
To Depreciation on fixed assets	5,22,543		
To Provision for Taxation	12,42,500		
To General Reserve	4,00,000		
To Investment Revaluation Reserve	12,500		
To Balance c/d	14,20,185		
	48,71,640		**48,71,640**

Depreciation on fixed assets as per Schedule II of the Companies Act, 2013 was Rs.5,75,345. You are required to calculate the maximum limits of the managerial remuneration as per Companies Act, 2013.

Question 2 : X Ltd.

The following extract of Balance Sheet of X Ltd. was obtained:

Balance Sheet (Extract) as on 31st March, 20X1

Liabilities	Rs.
Authorised capital:	
20,000, 14% preference shares of Rs.100	20,00,000
2,00,000 Equity shares of Rs.100 each	2,00,00,000
	2,20,00,000
Issued and subscribed capital:	
15,000, 14% preference shares of Rs.100 each fully paid	15,00,000
1,20,000 Equity shares of Rs.100 each, Rs.80 paid-up	96,00,000
Share suspense account	20,00,000

Reserves and surplus:	
Capital reserves (Rs.1,50,000 is revaluation reserve)	1,95,000
Securities premium	50,000
Secured loans:	
15% Debentures	65,00,000
Unsecured loans:	
Public deposits	3,70,000
Cash credit loan from SBI (short term)	4,65,000
Current Liabilities:	
Trade Payables	3,45,000
Assets:	
Investment in shares, debentures, etc.	75,00,000
Profit and Loss account (Dr. balance)	15,25,000

Question 3 : Kumar Ltd.

Kumar Ltd., a non-investment company has been incurring losses for the past few years. The company provides the following information for the current year:

	(Rs. In lakhs)
Paid up equity share capital	120
Paid up Preference share capital	20
Reserves (including Revaluation reserve Rs.10 lakhs)	150
Securities premium	40
Long term loans	40
Deposits repayable after one year	20
Application money pending allotment	720
Accumulated losses not written off	20
Investments	180

Kumar Ltd. has only one whole-time director, Mr. X. You are required to calculate the amount of maximum remuneration that can be paid to him if no special resolution is passed at the general meeting of the company in respect of payment of remuneration for a period not exceeding three years.

4. DIVISIBLE PROFITS :

One of the important functions of company accounting is to determine the amount of profits which is available for distribution to the shareholders as dividend. This is necessary since the amount of profits disclosed by the Profit & Loss Account, in every case, is not available for distribution. The availability of profits for distribution depends on a number of factors, e.g., their composition, the amount of provisions and appropriations that must be made out of them in priority, etc.

Dividends cannot be declared except out of profits. Capital cannot be returned to the shareholders by way of dividend

Question 4 : XYZ Ltd.

Due to inadequacy of profits during the year ended 31st March, 20X2, XYZ Ltd. proposes to declare 10% dividend out of general reserves. From the following particulars, ascertain the amount that can be utilised from general reserves, according to the Companies (Declaration of dividend out of Reserves) Rules, 2014:

	(Rs. In lakhs)
17,500 9% Preference shares of Rs.100 each, fully paid up	17,50,000
8,00,000 Equity shares of Rs.10 each, fully paid up	80,00,000
General Reserves as on 1.4.20X1	25,00,000
Capital Reserves as on 1.4.20X1	3,00,000
Revaluation Reserves as on 1.4.20X1	3,50,000
Net profit for the year ended 31st March, 20X2	3,00,000
Average rate of dividend during the last three years has been 12%.	

5. FINANCIAL STATEMENTS AS PER SCHEDULE III OF COMPANIES ACT 2013 :

Part 1 – Balance sheet

Name of the company

Balance sheet as at.....

Particulars	Note No	Current year	Previous year
I. Equity and Liabilities			
1. Shareholders Funds			
(a) Share capital			
(b) Reserves and Surplus			
(c) Money received against share warrant			
2. Share application money pending allotment			
3. Non-Current Liabilities			
(a) Long-term borrowings			
(b) Deferred Tax Liability			

	(c) Other long term liability			
	(d) Short – term provisions			
4.	Current Liabilities			
	(a) Short-term borrowings			
	(b) Trade payables			
	(c) Other current liabilities			
	(d) Short-term provisions			
Total				
II.	**Assets**			
1.	Non-current Assets			
	(a) Fixed assets			
	(i) Tangible assets			
	(ii) Intangible assets			
	(iii) Capital work-in-progress			
	(iv) Intangible assets under development			
	(b) Non-current investments			
	(c) Deferred tax assets (net)			
	(d) Long term loans and advances			
	(e) Other non-current assets			
2.	Current Assets			
	(a) Current investments			
	(b) Inventories			
	(c) Trade receivables			
	(d) Cash and cash equivalents			
	(e) Short-term loans and advances			
	(f) Other current assets			
Total				

General instructions for preparation of Balance sheet :

Current and Non-Current Assets

An entity shall classify an asset as current when:

(a) it expects to realise the asset, or intends to sell or consume it, in its normal operating cycle;

(b) it holds the asset primarily for the purpose of trading;

(c) it expects to realise the asset within twelve months after the reporting period; or

(d) the asset is cash or a cash equivalent (as defined in Ind AS 7) unless the asset is restricted from being exchanged or used to settle a liability for at least twelve months after the reporting period.

An entity shall classify all other assets as non-current :

Current and Non-current Liabilities :

An entity shall classify a liability as current when:

(a) it expects to settle the liability in its normal operating cycle;

(b) it holds the liability primarily for the purpose of trading;

(c) the liability is due to be settled within twelve months after the reporting period; or

(d) it does not have an unconditional right to defer settlement of the liability for at least twelve months after the reporting period. Terms of a liability that could, at the option of the counterparty, result in its settlement by the issue of equity instruments do not affect its classification.

An entity shall classify all other liabilities as non-current :

Operating Cycle :

The operating cycle of an entity is the time between the acquisition of assets for processing and their realisation in cash or cash equivalents. When the entity's normal operating cycle is not clearly identifiable, it is assumed to be twelve months.

When receivable shall be classified as a "trade receivable" ?

If it is in respect of the amount due on account of goods sold or services rendered. In The Normal Course Of Business

When payable shall be classified as a "trade payable" ?

If it is in respect of the amount due on account of goods purchased or services received. In The Normal Course Of Business

Part II – Profit and Loss Account

Name of the company

Profit and loss Account for the year ended

	Particulars	Note No	Current Year	Previous Year
	Continuing Operations (1)			
I	Revenue from operations			
II	Other Income			
III	Total Revenue (I + II)			

IV	Expenses			
	a. Cost of Material Consumed			
	b. Purchase of Stock in trade			
	c. Changes in inventory of finished goods, work-in-progress and stock in trade			
	d. Employee benefits			
	e. Finance Costs			
	f. Depreciation and Amortization			
	g. Other expenses			
	Total Expenses			
V	Profit before exceptional and extra-ordinary items and tax (III – IV)			
VI	Exceptional items			
VII	Profit / Loss before extra-ordinary items			
VIII	Extra-ordinary Items			
IX	Profit before Tax			
X	Tax expenses (Current tax and deferred tax)			
XI	Profit after tax from continuing operations			
XII	Profit from discontinuing operations			
XIII	Tax expense from discontinuing operations			
XIV	Profit from discontinuing operations			
XV	Profit / Loss for the period			
XVI	Earnings per share			

Question 5 : Omega Limited

The following is the Trial Balance of Omega Limited as on 31.3.20X2:

(Figures in Rs.'000)

	Debit		Credit
Land at cost	220	Equity Capital (Shares of Rs.10 each)	300
Plant & Machinery at cost	770	10% Debentures	200
Trade Receivables	96	General Reserve	130
Inventories (31.3.X2)	86	Profit & Loss A/c	72
Bank	20	Securities Premium	40

Adjusted Purchases	320	Sales	700
Factory Expenses	60	Trade Payables	52
Administration Expenses	30	Provision for Depreciation	172
Selling Expenses	30	Suspense Account	4
Debenture Interest	20		
Interim Dividend Paid	18		
	1,670		**1,670**

Additional Information:

(i) The authorised share capital of the company is 40,000 shares of Rs. 10 each.

(ii) The company on the advice of independent valuer wish to revalue the land at Rs. 3,60,000.

(iii) Declared final dividend @ 10%.

(iv) Suspense account of Rs. 4,000 represents cash received for the sale of some of the machinery on 1.4.20X1. The cost of the machinery was Rs. 10,000 and the accumulated depreciation thereon being Rs. 8,000.

(v) Depreciation is to be provided on plant and machinery at 10% on cost.

You are required to prepare Omega Limited's Balance Sheet as on 31.3.20X2 and Statement of Profit and Loss with notes to accounts for the year ended 31.3.20X2 as per Schedule III. Ignore previous years' figures & taxation.

Question 6 : Haria Chemicals Ltd.

You are required to prepare Balance sheet and statement of Profit and Loss from the following trial balance of Haria Chemicals Ltd. for the year ended 31st March, 20X1.

Haria Chemicals Ltd.

Trial Balance as at 31st March, 20X1

Particulars	Rs.		Rs.
Inventory	6,80,000	Equity Shares	
Furniture	2,00,000	Capital (Shares of Rs. 10 each)	25,00,000
Discount	40,000	11% Debentures	5,00,000
Loan to Directors	80,000	Bank loans	6,45,000
Advertisement	20,000	Trade payables	2,81,000
Bad debts	35,000	Sales	42,68,000
Commission	1,20,000	Rent received	46,000
Purchases	23,19,000	Transfer fees	10,000
Plant and Machinery	8,60,000	Profit & Loss account	1,39,000
Rentals	25,000	Depreciation provision:	

Current account	45,000	Machinery	1,46,000
Cash	8,000		
Interest on bank loans	1,16,000		
Preliminary expenses	10,000		
Fixtures	3,00,000		
Wages	9,00,000		
Consumables	84,000		
Freehold land	15,46,000		
Tools & Equipments	2,45,000		
Goodwill	2,65,000		
Trade receivables	4,40,000		
Dealer aids	21,000		
Transit insurance	30,000		
Trade expenses	37,000		
Distribution freight	54,000		
Debenture interest	55,000		
	85,35,000		**85,35,000**

Additional information: Closing Inventory on 31-3-20X1: Rs. 8,23,000.

Question 7 : International Hotels Ltd.

You are required to prepare a Statement of Profit and Loss and Balance Sheet from the following Trial Balance extracted from the books of the International Hotels Ltd., on 31st March, 20X2:

		Dr. (Rs.)	Cr. (Rs.)
Authorised Capital-divided into 5,000 6% Preference Shares of Rs.100 each and 10,000 equity Shares of Rs.100 each			15,00,000
Subscribed Capital -			
5,000 6% Preference Shares of Rs.100 each			5,00,000
Equity Capital			8,05,000
Purchases - Wines, Cigarettes, Cigars, etc.		45,800	
- Foodstuffs		36,200	
Wages and Salaries		28,300	
Rent, Rates and Taxes		8,900	
Laundry			750
Sales - Wines, Cigarettes, Cigars, etc.			68,400
- Food			57,600

Coal and Firewood		3,290	
Carriage and Cooliage		810	
Sundry Expenses		5,840	
Advertising		8,360	
Repairs		4,250	
Rent of Rooms			48,000
Billiard			5,700
Miscellaneous Receipts			2,800
Discount received			3,300
Transfer fees			700
Freehold Land and Building		8,50,000	
Furniture and Fittings		86,300	
Inventory on hand, 1st April, 20X1			
Wines, Cigarettes. Cigars, etc.		12,800	
Foodstuffs		5,260	
Cash in hand		2,200	
Cash with Bankers		76,380	
Preliminary and formation expenses		8,000	
2,000 Debentures of Rs.100 each (6%)			2,00,000
Profit and Loss Account			41,500
Trade payables			42,000
Trade receivables		19,260	
Investments		2,73,300	
Goodwill at cost		5,00,000	
General Reserve			2,00,000
		19,75,000	19,75,000
Wages and Salaries Outstanding	1,280		
Inventory on 31st March, 20X2			
Wines, Cigarettes and Cigars, etc.	22,500		
Foodstuffs	16,400		

Depreciation : Furniture and Fittings @ 5% p.a. : Land and Building @ 2% p.a.

The Equity capital on 1st April, 20X1 stood at Rs. 7,20,000, that is 6,000 shares fully paid and 2,000 shares Rs. 60 paid. The directors made a call of Rs. 40 per share on 1st October 20X1. A shareholder could not pay the call on 100 shares and his shares were then forfeited and reissued @ Rs. 90 per share as fully paid. The Directors declare a dividend of 8% on equity shares, transferring any amount that may be required from General Reserve. Ignore Taxation.

Question 8 : Pioneer Ltd.

From the following particulars furnished by Pioneer Ltd., prepare the Balance Sheet as at 31st March, 20X1 as required by Schedule III of the Companies Act. Give notes at the foot of the Balance Sheet as may be found necessary -

		Dr. (Rs.)	Cr. (Rs.)
Equity Capital (Face value of Rs.100)			10,00,000
Calls in Arrears		1,000	
Land		2,00,000	
Building		3,50,000	
Plant and Machinery		5,25,000	
Furniture		50,000	
General Reserve			2,10,000
Loan from State Financial Corporation			1,50,000
Inventory :			
Finished Goods	2,00,000		
Raw Materials	50,000	2,50,000	
Provision for Taxation			68,000
Trade receivables		2,00,000	
Advances		42,700	
Dividend Payable			60,000
Profit and Loss Account			86,700
Cash Balance		30,000	
Cash at Bank		2,47,000	
Loans (Unsecured)			1,21,000
Trade payables (For Goods and Expenses)			2,00,000
		18,95,700	**18,95,700**

The following additional information is also provided :

(1) 2,000 equity shares were issued for consideration other than cash.

(2) Trade receivables of Rs.52,000 are due for more than six months.

(3) The cost of assets:

Building	Rs.4,00,000
Plant and Machinery	Rs.7,00,000
Furniture	Rs.62,500

(4) The balance of Rs.1,50,000 in the loan account with State Finance Corporation is inclusive of Rs.7,500 for interest accrued but not due. The loan is secured by hypothecation of the Plant and Machinery.

(5) Balance at Bank includes Rs.2,000 with Perfect Bank Ltd., which is not a Scheduled Bank.

(6) The company had contract for the erection of machinery at Rs.1,50,000 which is still incomplete.

PRACTICAL QUESTIONS :

Question 9 :

State under which head these accounts should be classified in Balance Sheet, as per Schedule III of the Companies Act, 2013:

(i) Share application money received in excess of issued share capital.

(ii) Share option outstanding account.

(iii) Unpaid matured debenture and interest accrued thereon.

(iv) Uncalled liability on shares and other partly paid investments.

(v) Calls unpaid.

(vi) Money received against share warrant.

Question 10 : Star Ltd.

The following extract of Balance Sheet of Star Ltd. (non- investment) company was obtained:

Balance Sheet (Extract) as on 31st March, 20X1

Liabilities	Rs.
Authorised capital:	
60,000, 14% preference shares of Rs.100	60,00,000
6,00,000 Equity shares of Rs.100 each	6,00,00,000
	6,60,00,000
Issued and subscribed capital:	
45,000, 14% preference shares of Rs.100 each fully paid	45,00,000
3,60,000 Equity shares of Rs.100 each, Rs.80 paid-up	2,88,00,000
Share suspense account	60,00,000
Reserves and surplus:	
Capital reserves (Rs.4,50,000 is revaluation reserve)	5,85,000
Securities premium	1,50,000
Secured loans:	
15% Debentures	1,95,00,000
Unsecured loans:	
Public deposits	11,10,000
Cash credit loan from SBI (short term)	3,95,000
Current Liabilities:	
Trade Payables	10,35,000
Assets:	
Investment in shares, debentures, etc.	2,25,00,000
Profit and Loss account (Dr. balance)	45,75,000

Share suspense account represents application money received on shares, the allotment of which is not yet made.

You are required to compute effective capital as per the provisions of Schedule V. Would your answer differ if Star Ltd. is an investment company?

Question 11 : Bose and Sen Ltd.

On 31st March, 20X1 Bose and Sen Ltd. provides to you the following ledger balances after preparing its Profit and Loss Account for the year ended 31st March, 20X1:

Credit Balances :

	Rs.
Equity shares capital, fully paid shares of Rs.10 each	70,00,000
General Reserve	15,49,100
Loan from State Finance Corporation	10,50,000
(Secured by hypothecation of Plant & Machinery Repayable	
within one year Rs.2,00,000)	
Loans: Unsecured (Long term)	8,47,000
Sundry Creditors for goods &expenses	14,00,000
(Payable within 6 months)	
Profit &Loss Account	7,00,000
Provision for Taxation	8,16,900
	1,33,63,000

Debit Balances :

	Rs.
Calls in arrear	7,000
Land	14,00,000
Buildings	20,50,000
Plant and Machinery	36,75,000
Furniture& Fixture	3,50,000
Inventories: Finished goods	14,00,000
Raw Materials	3,50,000
Trade Receivables	14,00,000
Advances: Short-term	2,98,900
Cash in hand	2,10,000
Balances with banks	17,29,000
Preliminary Expenses	93,100
Patents &Trademarks	4,00,000
	1,33,63,000

The following additional information is also provided in respect of the above balances:

(i) 4,20,000 fully paid equity shares were allotted as consideration for land & buildings.

(ii) Cost of Building Rs.28,00,000

(iii) Cost of Plant & Machinery Rs.49,00,000

Cost of Furniture & Fixture Rs.4,37,500

(iv) Trade receivables for Rs.3,80,000 are due for more than 6 months.

(v) The amount of Balances with Bank includes Rs.18,000 with a bank which is not a scheduled Bank and the deposits of Rs.5 lakhs are for a period of 9 months.

(vi) Unsecured loan includes Rs.2,00,000 from a Bank and Rs.1,00,000 from related parties.

You are not required to give previous year figures. You are required to prepare the Balance Sheet of the Company as on 31stMarch,20X1 as required under Schedule III of the Companies Act,2013.

Question 12 : Alpha Ltd.

From the following particulars furnished by Alpha Ltd., prepare the Balance Sheet as on 31st March 20X1 as required by Part I, Schedule III of the Companies Act, 2013.

Particulars		Dr.(Rs.)	Cr.(Rs.)
Equity Share Capital (Face value of Rs.100 each)			50,00,000
Call in Arrears		5,000	
Land & Building		27,50,000	
Plant & Machinery		26,25,000	
Furniture		2,50,000	
General Reserve			10,50,000
Loan from State Financial Corporation			7,50,000
Inventory:			
Raw Materials	2,50,000		
Finished Goods	10,00,000	12,50,000	
Provision for Taxation			6,40,000
Trade receivables		10,00,000	
Short term Advances		2,13,500	
Profit & Loss Account			4,33,500
Cash in Hand		1,50,000	
Cash at Bank		12,35,000	
Unsecured Loan			6,05,000
Trade payables (for Goods and Expenses)			8,00,000
Loans & advances from related parties			2,00,000

The following additional information is also provided:

(i) 10,000 Equity shares were issued for consideration other than cash.

(ii) Trade receivables of Rs. 2,60,000 are due for more than 6 months.

(iii) The cost of the Assets were:
Building Rs. 30,00,000, Plant & Machinery Rs. 35,00,000 and Furniture Rs. 3,12,500

(iv) The balance of Rs. 7,50,000 in the Loan Account with State Finance Corporation is inclusive of Rs. 37,500 for Interest Accrued but not Due. The loan is secured by hypothecation of Plant & Machinery.

(v) Balance at Bank includes Rs. 10,000 with Omega Bank Ltd., which is not a Scheduled Bank.

(vi) Transfer Rs. 20,000 to general reserve is proposed by Board of directors.

(vii) Board of directors has declared dividend of 5% on the paid up capital.

Question 13 : Ring Ltd.

Ring Ltd. was registered with a nominal capital of Rs.10,00,000 divided into shares of Rs.100 each. The following Trial Balance is extracted from the books on 31st March, 20X2:

Particulars	Rs.		Rs.
Buildings	5,80,000	Sales	10,40,000
Machinery	2,00,000	Outstanding Expenses	4,000
Closing Stock	1,80,000	Provision for Doubtful Debts (1-4-20X1)	6,000
Loose Tools	46,000	Equity Share Capital	4,00,000
Purchases (Adjusted)	4,20,000	General Reserve	80,000
Salaries	1,20,000	Profit and Loss A/c (1-4-20X1)	50,000
Directors' Fees	20,000	Creditors	1,84,000
Rent	52,000	Provision for depreciation:	
Depreciation	40,000	On Building 1,00,000	
Bad Debts	12,000	On Machinery 1,10,000	2,10,000
Investment	2,40,000	14% Debentures	4,00,000
Interest accrued on investment	4,000	Interest on Debentures accrued but not due	28,000
Debenture Interest	56,000	Interest on Investments	24,000
Advance Tax	1,20,000	Unclaimed dividend	10,000
Sundry expenses	36,000		
Debtors	2,50,000		
Bank	60,000		
	24,36,000		**24,36,000**

You are required to prepare statement of Profit and Loss for the year ending 31st March, 20X2 and Balance sheet as at that date after taking into consideration the following information:

(a) Closing stock is more than opening stock by Rs. 1,60,000;
(b) Provide to doubtful debts @ 4% on Debtors
(c) Make a provision for income tax @30%.
(d) Depreciation expense included depreciation of Rs. 16,000 on Building and that of Rs. 24,000 on Machinery.
(e) The directors declared a dividend @ 25% and transfer to General Reserve @ 10%.
(f) Bills Discounted but not yet matured Rs. 20,000.

MCQs :

1. Trade payables as per Schedule III will include:
   (a) Dues payable in respect to statutory obligation
   (b) Interest accrued on trade payables
   (c) Bills payables.
   (d) Bills receivables
2. Securities Premium Account is shown on the liabilities side in the Balance Sheet under the heading:
   (a) Reserves and Surplus.
   (b) Current Liabilities.
   (c) Share Capital.
   (d) Share application money pending allotment
3. "Fixed assets held for sale" will be classified in the company's balance sheet as
   (a) Current asset (b) Non-current asset
   (c) Capital work- in- progress (d) Deferred tax assets
4. Current maturities of long- term debt will come under
   (a) Current Liabilities. (b) Short term borrowings.
   (c) Long term borrowings. (d) Short term provisions
5. Declaration of dividends for current year is made after providing for
   (a) Depreciation of past years only.
   (b) Depreciation on assets for the current year and arrears of depreciation of past years (if any).
   (c) Depreciation on current year only and by forgoing arrears of depreciation of past years.
   (d) Excluding current year depreciation

Thanks ....

Chapter 29

AS 21 – CONSOLIDATED FINANCIAL STATEMENTS

CHAPTER DESIGN

1. PRACTICAL QUESTIONS
2. MCQ'S

1. PRACTICAL QUESTIONS :

Question : R and M Ltd.

Following is the Balance Sheet of R and M Ltd as on 31st March 2017.

	R	M		R	M
Share Capital	50	30	Fixed Assets	50	40
Reserves	10	-	Share of M Ltd. (100%)	30	-
Liabilities	40	20	Current Assets	20	10
			Misc. Exp	-	
Total	**100**	**50**	**Total**	**100**	**50**

Prepare consolidated Balance Sheet.

Question 2 : S and R Ltd.

Following is the Balance Sheet of S and R Ltd as on 31st March 2017.

	R	M		R	M
Share Capital	50	30	Fixed Assets	50	40
Reserves	10	-	Share of R Ltd.	30	-
Liabilities	40	20	Current Assets	20	10
			Misc. Exp	-	
Total	**100**	**50**	**Total**	**100**	**50**

Prepare consolidated Balance Sheet.

Question 3 : A and B Ltd.

Following is the Balance Sheet of A and B Ltd. as on 31st March, 2017

	A	B		A	B
Share Capital	700	200	Fixed Assets	600	250
Reserves	300	100	Share of B Ltd. (80%)	210	-
Liabilities	200	50	Current Assets	390	100
			Misc. Exp	-	-
Total	**1200**	**350**	**Total**	**1200**	**350**

Prepare consolidated Balance Sheet. Reserves of B Ltd. stood at 60 on the date when A purchased shares of B Ltd.

Question 4 : X and Y Ltd.

Following is the Balance Sheet of X and Y Ltd as on 31st March 2017.

	X	Y		X	Y
Share Capital	700	200	Fixed Assets	600	250
Profit and Loss A/c	200	70	Share of Y Ltd.	210	-
General Reserve	100	30	Current Assets	380	95

Liabilities	200	50	Misc. Exp	10	5
Total	**1200**	**350**	**Total**	**1200**	**350**

When X Ltd. purchased the shares of Y Ltd, general reserve stood at Rs. 10 and Profit and loss A/c. at Rs. 40. Prepare consolidated Balance Sheet

Question 5 : Jai Ltd.

Jai Ltd. acquired 15,000 Shares in Hind Ltd., for Rs 1,55,000 on 1st April 2017. The balance sheet of the two companies as on 31 st March, 2018 were as follows:

Liabilities	**Jai Ltd.**	**Hind Ltd.**
	Rs	**Rs**
Equity shares of Rs 10 each, fully paid-up	9,00,000	2,50,000
General reserves	1,60,000	40,000
Profit and loss account	80,000	25,000
Bills payable	40,000	20,000
Creditors	50,000	30,000
	12,30,000	**3,65,000**
Assets		
Machinery	7,00,000	1,50,000
Furniture	1,00,000	70,000
Investments	1,55,000	-
Stock	1,00,000	50,000
Debtors	60,000	35,000
Cash at bank	90,000	40,000
Bills receivable	25,000	20,000
	12,30,000	**3,65,000**

Additional information:

i. General reserve appearing in the balance sheet of Hind Ltd., has remained unchanged since 31st March, 2017.

ii. Profit earned by Hind Ltd. for the year ended 31st March, 2018 amounted to Rs 20,000,

iii. Jai Ltd. sold to Hind Ltd. goods costing Rs 8,000 for Rs 10,000, This is still in stock of Hind Ltd. on 31st March, 2018. Creditors of Hind Ltd. include Rs4,000 due to Jai Ltd. on account of these goods.

iv. Out of Hind Ltd.'s acceptance, RS 7,000 were those which were accepted in favour of Jai Ltd.

You are required to :

Draw a consolidated balance sheet as on 31st March, 2018.

Question 6 : H Ltd. And S Ltd.

Balance sheets of H Ltd. and S Ltd. as at 31st March, 2018 are given below:

Liabilities	H Ltd	S Ltd
	Rs.	**Rs.**
Share capital of Rs 10 each, fully paid	5,00,000	2,00,000
General reserves	1,00,000	50,000
Profit and loss account	60,000	35,000
Creditors	80,000	60,000
	7,40,000	**3,45,000**
Assets	**H Ltd.**	**S Ltd.**
	Rs.	**Rs.**
Fixed assets	3,00,000	1,00,000
60% shares in S Ltd., at cost	1,62,400	-
Current assets	2,77,600	2,39,000
Preliminary expenses	-	6,000
	7,40,000	**3,45,000**

1. H Ltd. acquired the shares on 1st April, 2017 and on that date general reserve and profit and loss account of S Ltd. showed balances of Rs 40,000 and 8,000 respectively. Prepare a consolidated balance sheet of H Ltd. and its subsidiary S Ltd. as on 31st March, 2006
2. S Ltd. sold goods worth Rs. 10,000 to H Ltd. for Rs. 12,000. Goods are still in stock of H Ltd.
3. Debtors of H Ltd. includes Rs. 12,000 from S Ltd, however creditors of S Ltd, include Rs. 10,000 to H Ltd.

Question 7 : H Ltd.

Following are the balance sheets of H Ltd. and its subsidiary S. Ltd. as at 31st March, 2017:

Liabilities	H Ltd	S Ltd
	Rs	**Rs**
Equity share capital:		
Share of Rs 10 each fully paid	6,00,000	2,00,000
General reserves	3,40,000	80,000
Profit and loss account	1,00,000	60,000
creditors	70,000	35,000
	11,10,000	**3,75,000**
Assets	**Rs.**	**Rs.**
Plant and Machinery	3,90,000	1,35,000
Furniture's	80,000	40,000
80% shares in S Ltd. (at cost)	3,40,000	-

Stock	1,80,000	1,20,000
Debtors	50,000	30,000
Cash at bank	70,000	50,000
	11,10,000	**3,75,000**

Additional information :

1. Profit and loss account of S Ltd stood at Rs 30,000 on 1st April, 2016 whereas general reserve stood at Rs 80,000 even on this date.
2. H Ltd. acquired 80% shares in S. Ltd. on 1st April2016.
3. S Ltd's plant and machinery which stood at Rs 1,50,000 on 1st April 2016 was considered worth Rs 1,80,000, this figure is to be considered while consolidating the balance sheets.

You are required to:

Prepare the consolidated balance sheet as at 31st March, 2017.

Question 8 : M Ltd.

From the following balance sheet of M Ltd. and its subsidiary N Ltd. drawn up at 31st torch, 2017, prepare a consolidated balance sheet as at that date, having regard to the following:

a. Reserves and Profit and loss A/c of N Ltd. stood at Rs.25,000 and Rs.15,000 respectively on the date of acquisition of its 80% shares by M Ltd. on 1st April, 2016.
b. Machinery (Book-value Rs.1,00,000) and Furniture (Book value Rs.20,000) of N Ltd. were revalued at Rs.1,50,000 and Rs.15,000 respectively on 1.4.2016 for the purpose of fixing the price of its shares. [Rates of depreciation : Machinery 10%, Furniture 15%]

Balance sheet of M Ltd. and N Ltd. as on 31st March, 2017

Liabilities	M Ltd.	N Ltd.	Assets	M Ltd.	N Ltd.
	Rs.	**Rs.**		**Rs.**	**Rs.**
Share capital			Machinery	3,00,000	90,000
Shares of Rs.100	6,00,000	1,00,000	Furniture	1,50,000	17,000
Reserves	2,00,000	75,000	Other assets	4,40,000	1,50,000
Profit and Loss A/c	1,00,000	25,000	Shares in S Ltd. 800 shares at Rs. 200	1,60,000	–
Creditors	1,50,000	57,000			
Total	**10,50,000**	**2,57,000**	**Total**	**10,50,000**	**2,57,000**

Question 9 : X Ltd.

X Ltd. acquired 1,600 ordinary shares of Rs.100 each of Y Ltd. on 1st July, 2017. On December 31, 2017 the balance sheets of the two companies were as given below:

Liabilities	X Ltd.	Y Ltd.	Assets	X Ltd.	Y Ltd.
	Rs.	**Rs.**		**Rs.**	**Rs.**

Capital (Shares of Rs.100 each fully	5,00,000	2,00,000	Land and buildings	1,50,000	1,80,000
Reserves	2,40,000	1,00,000	Plant and machinery	2,40,000	1,35,000
Profit and loss A/c	57,200	82,000	Investment in Y Ltd. at cost	3,40,000	–
Bank overdraft	80,000	–	Stock	1,20,000	36,400
Bills payable	–	8,400	Sundry debtors	44,000	40,000
Creditors	47,100	9,000	Bills receivable	15,800	–
			Cash	14,500	8,000
	9,24,300	**3,99,400**		**9,24,300**	**3,99,400**

The Profit and loss A/c of Y Ltd. showed a credit balance of Rs.30,000 on 1st January, 2017 out of which a dividend of 10% was paid on 1st August. X Ltd. has credited the dividend received to its Profit and Loss A/c. The plant and machinery which stood at Rs.1,50,000 on 1st January, 2017 was considered as worth for Rs.1,80,000 on 1st July, 2017; this figure is to be considered while consolidating the Balance sheets. Prepare the consolidated balance sheet as on December 31, 2017. No transfers are done to Reserves in current year.

Question 10 : H Ltd.

From the following summarized balance sheets of H Ltd. and its subsidiary S Ltd. drawn up at 31st March, 2017, prepare a consolidated balance sheet as at that date, having regard to the following:

Reserves and Profit and Loss Account of S Ltd. stood at Rs.25,000 and Rs. 15,000 respectively on the date of acquisition of its 80% shares by H Ltd. on 1st April, 2016.

Machinery (Book-value Rs. 1,00,000) and Furniture (Book value Rs. 20,000) of S Ltd. were revalued at Rs. 1,50,000 and Rs. 15,000 respectively on 1st April, 2016 for the purpose of fixing the price of its shares. [Rates of depreciation computed on the basis of useful lives: Machinery 10%, Furniture 15%.]

Summarised Balance Sheet of H Ltd. as on 31st March, 2017

Liabilities	H Ltd.	S. Ltd.	Assets	H Ltd.	S Ltd.
	Rs.	**Rs.**		**Rs.**	**Rs.**
Equity and			Non-current		
Liabilities					
Shareholders' funds			Fixed assets		
Share Capital			Machinery	3,00,000	90,000
Shares of Rs. 100	6,00,000	1,00,000	Furniture	1,50,000	17,000
Reserves	2,00,000	75,000	Other non-current assets	4,40,000	1,50,000
			Non-current Investments		

Profit and Loss	1,00,000	25,000	Shares in S Ltd.:		
Trade Payables	1,50,000	57,000	800 shares at Rs. 200 each	1,60,000	—
	10,50,000	**2,57,000**		**10,50,000**	**2,57,000**

Question 11 : B Ltd.

Consider the following summarized balance sheets of subsidiary B Ltd.:

	2015	2016		2015	2016
	Rs.	Rs.		Rs.	Rs.
Share-Capital			Fixed Assets		
Issued & subscribed 5,000 equity shares of Rs 100 each	5,00,000	5,00,000	Cost	3,20,000	3,20,000
			Less: Accumulated depreciation	(48,000)	(96,000)
				2,72,000	2,24,000
Reserves & Surplus	2,86,000	7,14,000	Investments at		
Current Liabilities &			Non-current	—	4,00,000
Trade Payables	4,90,000	4,94,000	Inventory	5,97,000	7,42,000
Bank overdraft	—	1,70,000	Trade	5,94,000	8,91,000
Provision for	3,10,000	4,30,000	Prepaid	72,000	48,000
			Cash at Bank	51,000	3,000
	15,86,000	**23,08,000**		**15,86,000**	**23,08,000**

Also consider the following information:

(a) B Ltd. is a subsidiary of A Ltd. Both the companies follow calendar year as the accounting year.

(b) A Ltd. values inventory on weighted average basis while B Ltd. used FIFO basis. To bring B Ltd.'s values in line with those of A Ltd, its value of inventory is required to be reduced by Rs.12,000 at the end of 2015 and Rs. 34,000 at the end of 2016.

(c) B Ltd. deducts 1% from Trade Receivables as a general provision against doubtful debts.

(d) Prepaid expenses in B Ltd. include advertising expenditure carried forward of Rs. 60,000 in 2015 andRs. 30,000 in 2016, being part of initial advertising expenditure of Rs. 90,000 in 2015 which is being written off over three years. Similar amount of advertising expenditure of A Ltd. has been fully written off in 2015.

Restate the balance sheet of B Ltd. as on 31st December, 2016 after considering the above information, for the purpose of consolidation. Would restatement be necessary to make the accounting policies adopted by A Ltd. and B Ltd. uniform.

Question 12 : H Ltd.

On 31st March, 2017 the summarized Balance Sheets of H Ltd. and its subsidiary S Ltd. stood as follows :

Liabilities	H Ltd.	S Ltd.
	Rs. in lakhs	**Rs. in lakhs**
Share Capital:		
Authorized	15000	6000
Issued and Subscribed:		
Equity Shares of Rs. 10 each, fully paid up	12000	4800
General Reserve	2,784	1,380
Profit and Loss Account	2,715	1,620
Bills Payable	372	160
Trade Payables	1,461	854
Provision for Taxation	855	394
Dividend payable	1,200	
	21,387	**9,208**
Assets	**H Ltd.**	**S Ltd.**
	Rs. in lakhs	**Rs. in lakhs**
Land and Buildings	2,718	–
Plant and Machinery	4,905	4,900
Furniture and Fittings	1,845	586
Investments in shares in S Ltd.	3,000	–
Stock	3,949	1,956
Trade Receivables	2,600	1,363
Cash and Bank Balances	1,490	204
Bills Receivable	360	199
Sundry Advances	520	–
	21,387	**9,208**

The following information is also provided to you:

(a) H Ltd. purchased 180 lakh shares in S Ltd. on 31st March, 2016 when the balances of General Reserve and Profit and Loss Account of S Ltd. stood at Rs. 3,000 lakh and Rs. 1,200 lakh respectively.

(b) On 1st April, 2016, S Ltd. declared a dividend @ 20% for the year ended 31st March, 2016. H Ltd. credited the dividend received by it to its Profit and Loss Account.

(c) On 1st January, 2017, S Ltd. issued 3 fully paid-up bonus shares for every 5 shares held out of balances of its general reserve as on 31st March, 2016.

(d) On 31st March, 2017, all the bills payable in S Ltd.'s balance sheet were acceptances in favour of H Ltd. But on that date, H Ltd. held only Rs. 45 lakh of these acceptances in hand, the rest having been endorsed in favour of its trade payables.

(e) On 31st March, 2017, S Ltd.'s inventory included goods which it had purchased for Rs. 100 lakh from H Ltd. which made a profit @ 25% on cost.

Prepare a Consolidated Balance Sheet of H Ltd. and its subsidiary S Ltd. as at 31st March, 2017.

Question 13 :

The following data is provided to you:

Case	Subsidiary Company	% shares owned	Cost	Date of acquisition		Consolidation Date	
				1.1.2018		31.12.2018	
				Share Capital	Profit & Loss Account	Share Capital	Profit & Loss Account
			Rs.	Rs.	Rs.	Rs.	Rs.
Case 1	A	90%	1,40,000	1,00,000	50,000	1,00,000	70,000
Case 2	B	85%	1,04,000	1,00,000	30,000	1,00,000	20,000
Case 3	C	80%	56,000	50,000	20,000	50,000	20,000
Case 4	D	100%	1,00,000	50,000	40,000	50,000	55,000

Determine in each case:

(1) Minority interest at the date of acquisition and at the date of consolidation.

(2) Goodwill or Capital Reserve.

Question 14 : H Ltd.

The following summarised Balance Sheets of H Ltd. and its subsidiary S Ltd. were prepared as on 31st March, 2019:

	H Ltd. (Rs.)	S Ltd. (Rs.)
Equity and Liabilities		
Shareholders' Funds		
Equity Share Capital (fully paid up shares of Rs.10 each)	12,00,000	2,00,000
Reserves and Surplus		
General Reserve	4,35,000	1,55,000
Profit and Loss Account	2,80,000	65,000
Current Liabilities		

Trade Payables	3,25,000	1,25,000
Total	**22,40,000**	**5,45,000**
	H Ltd. (Rs.)	**S Ltd. (Rs.)**
Assets		
Non-Current Assets		
Property, Plant and Equipment		
Machinery	6,40,000	1,80,000
Furniture	3,75,000	34,000
Non-Current Investments		
Shares in S Ltd. - 16,000 shares @ Rs.20 each	3,20,000	-
Current Assets		
Inventories	2,68,000	62,000
Trade Receivables	4,73,000	2,37,000
Cash and Bank	1,64,000	32,000
Total	**22,40,000**	**5,45,000**

H Ltd. acquired the 80% shares of S Ltd. on 1st April, 2018. On the date of acquisition, General Reserve and Profit Loss Account of S Ltd. stood at Rs. 50,000 and Rs. 30,000 respectively.

Machinery (book value Rs. 2,00,000) and Furniture (book value Rs. 40,000) of S Ltd. were revalued at Rs. 3,00,000 and Rs. 30,000 respectively on 1st April,2018 for the purpose of fixing the price of its shares (rates of depreciation computed on the basis of useful lives: Machinery 10% and Furniture 15%). Trade Payables of H Ltd. include Rs. 40,000 due to S Ltd. for goods supplied since the acquisition of the shares. These goods are charged at 10% above cost. The inventories of H Ltd. includes goods costing Rs. 55,000 (cost to H Ltd.) purchased from S Ltd.

You are required to prepare the Consolidated Balance Sheet of H Ltd. with its subsidiary S Ltd. as at 31st March, 2019.

Problem 15 : H Ltd.

On 31st March, 2020 the summarised Balance sheet of H Ltd. and its subsidiary S Ltd. stood as follows :

Liabilities	H Ltd.	S Ltd.
	Rs.	**Rs.**
Shareholders' fund		
Issued and subscribed		
Equity shares of Rs.10 each	13,40,000	2,40,000

Reserve and Surplus	4,80,000	1,80,000
Profit and Loss Account	2,40,000	60,000
Secured Loans		
12% Debentures	1,00,000	-
Current Liabilities		
Trade Payables	2,00,000	1,22,000
Bank Overdraft	1,00,000	-
Bills Payable	60,000	14,800
Total	**25,20,000**	**6,16,800**
Assets		
Non-Current Assets		
(a) Property, Plant & Equipment		
Machinery	7,20,000	2,16,000
Furniture	3,60,000	40,800
(b) Investments		
Investments in S Ltd.	3,84,000	–
(19,200 shares at Rs.20 each)		
Current Assets		
Inventories	6,00,000	2,00,000
Trade Receivables	3,00,000	90,000
Bill Receivables	1,00,000	30,000
Cash at bank	56,000	40,000
Total	**25,20,000**	**6,16,800**

The following information is also provided to you :

(a) H Ltd. purchased 19,200 share of S Ltd. on 1st April, 2019, when the balances of Reserves & Surplus and Profit & Loss account of S Ltd. stood at Rs.60,000 and Rs.36,000 respectively.

(b) Machinery (Book value Rs.2,40,000) and Furniture (book value Rs.48,000) of S Ltd. were revalued at Rs.3,60,000 and Rs.36,000 respectively on 1st April, 2019, for the purpose of fixing the price of its shares. (Rates of depreciation computed on the basis of useful lives : Machinery 10%, Furniture 155)

(c) On 31st March, 2020, Bills payable of Rs.12,000 in S Ltd.'s Balance Sheet were accepted in favour of H ld.

You are required to prepare Consolidated Balance Sheet of H Ltd. and its subsidiary S Ltd. as at 31st March, 2020.

Question 16 : A Ltd.

The Profit and Loss Accounts of A Ltd. and its subsidiary B Ltd. for the year ended 31st March, 2018 are given below :

Rs. in Lakhs

	A Ltd.	B Ltd.
Sales and other income	7,500	1,500
Increase in Inventory	1,500	300
Total	9,000	1,800
Expenses		
Raw material consumed	1,200	300
Wages and Salaries	1,200	225
Production expenses	300	150
Administrative expenses	300	150
Selling and distribution expenses	300	75
Interest	150	75
Depreciation	150	75
Total	3,600	1,050
Profit before tax	5,400	750
Provision for tax	1,800	300
Profit after tax	3,600	450
Dividend paid	1,800	225
Balance of Profit	1,800	225

The following information is also given:

(i) A Ltd sold goods of Rs.180 Lakhs to B Ltd at cost plus 25%. (1/6 of such goods were still in inventory of B Ltd at the end of the year)

(ii) Administrative expenses of B Ltd include Rs.8 Lakhs paid to A Ltd as consultancy fees.

(iii) Selling and distribution expenses of A Ltd include Rs.15 Lakhs paid to B Ltd as commission.

(iv) A Ltd holds 72% of the Equity Capital of B Ltd. The Equity Capital of B Ltd prior to 2016-17 is Rs.1,500 Lakhs

Prepare a consolidated Profit and Loss Account for the year ended 31st March, 2018.

Problem 17 : MNT Ltd.

Consider the following summarized Balance Sheets of subsidiary MNT Ltd.

Liabilities	2017-18	2018-19
	Amount in Rs.	Amount in Rs.
Share Capital		

Issued and subscribed 7500 Equity Shares of Rs.100	7,50,000	7,50,000
Reserve and Surplus		
Revenue Reserve	2,14,000	5,05,000
Securities Premium	72,000	2,07,000
Current Liabilities and Provisions		
Trade Payables	2,90,000	2,46,000
Bank Overdraft	-	1,70,000
Provision for Taxation	2,62,000	4,30,000
	15,88,000	23,08,000
Assets		
Fixed Assets (Cost)	9,20,000	9,20,000
Less: Accumulated Depreciation	(1,70,000)	2,82,500)
	7,50,000	6,37,500
Investment at Cost	-	5,30,000
Current Assets		
Inventory	4,12,300	6,90,000
Trade Receivable	2,95,000	3,43,000
Prepaid expenses	78,000	65,000
Cash at Bank	52,700	42,500
	15,88,000	23,08,000

Other Information:

(1) MNT Ltd. is a subsidiary of LTC Ltd.

(2) LTC Ltd. values inventory on FIFO basis, while MNT Ltd. used LIFO basis. To bring MNT Ltd.'s inventories values in line with those of LTC Ltd., its value of inventory is required to be reduced by Rs.5,000 at the end of 2017-2018 and increased by Rs.12,000 at the end of 2018-2019. (Inventory of 2017-18 has been sold out during the year 2018-19)

(3) MNT Ltd. deducts 2% from Trade Receivables as a general provision against doubtful debts.

(4) Prepaid expenses in MNT Ltd. include Sales Promotion expenditure carried forward of Rs. 25 ,000 in 2017-18 and Rs. 12,500 in 2018-19 being part of initial Sales Promotion expenditure of Rs. 37,500 in 2017-18, which is being written off over three years. Similar nature of Sales Promotion expenditure of LTC Ltd. has been fully written off in 2017-18.

Restate the balance sheet of MNT Ltd. as on 31st March, 2019 after considering the above information for the purpose of consolidation. Such restatement is necessary to make the accounting policies adopted by LTC Ltd. and MNT Ltd. uniform.

Problem 18 : H Ltd.

H Ltd acquires 64000 Equity Shares of Rs. 10 each in S Ltd as on 1st October 2019. The Balance Sheets of the two companies as on 31st March 2020 were as under

Particulars	H Ltd (Rs.)	S Ltd (Rs.)
Equities and liabilities		
Equity Share Capital of Rs. 10 each	20,00,000	8,00,000
General Reserve (1st April 2019)	9,60,000	4,20,000
Profit and loss accounts	2,28,000	3,28,000
Preliminary Expenses (1st April 2019)	-	-20,000
Bank Overdraft	3,00,000	-
Bills Payable	-	52,000
Trade Payable	1,66,400	80,000
Total	**36,55,200**	**16,60,000**
Assets		
Land and building	7,20,000	7,60,000
Plant & Machinery	9,60,000	5,40,000
Investments in equity shares of S Ltd	12,27,200	-
Inventories	4,56,000	1,68,000
Trade Receivables	1,76,000	1,60,000
Bills Receivables	59,200	-
Cash in hand	56,800	32,000
Total	**36,55,200**	**16,60,000**

Additional Information :

1. The Profit & Loss Accounts of S Ltd showed a balance of Rs. 1,20,000 on 1st April 2019. S. Ltd paid a dividend of 10% out of the same on 1st November 2019 for the year 2018-19. The dividend was correctly accounted for by H Ltd
2. The Plant & Machinery of S Ltd which stood at Rs. 6,00,000 on 1st April 2019 was considered worth Rs. 5,20,000 on the date of acquisition by H Ltd. S Ltd charges depreciation @ 10% per annum on Plant & Machinery

Prepare consolidated Balance Sheet of H Ltd and its subsidiary S Ltd as on 31st March 2020 as per scheduled III of the companies Act, 2013.

2. MCQs :

1. Minority interest should be presented in the consolidated balance sheet
   - (a) As a part of liabilities.
   - (b) As a part of equity of the parent's shareholders.
   - (c) Separately from liabilities and the equity of the parent's shareholders.
   - (d) As a part of assets.

2. Minority of the subsidiary is entitled to
   (a) Capital profits of the subsidiary company.
   (b) Revenue profits of the subsidiary company.
   (c) Both capital and revenue profits of the subsidiary company.
   (d) Neither capital nor revenue profits of the subsidiary..
3. In consolidation of accounts of holding and subsidiary company _________ is eliminated in full.
   (a) Current liabilities of subsidiary company.
   (b) Reserves and surplus of both holding and subsidiary company.
   (c) Mutual indebtedness.
   (d) Nothing.
4. In consolidated balance sheet, the share of the outsiders in the net assets of the subsidiary must be shown as
   (a) Minority interest. (b) Capital reserve.
   (c) Current liability. (d) Current assets.
5. Provision for Tax made by the subsidiary company will appear in the consolidated balance sheet as an item of
   (a) Current liability. (b) Revenue profit.
   (c) Capital profit. (d) Current assets.

Thanks ....

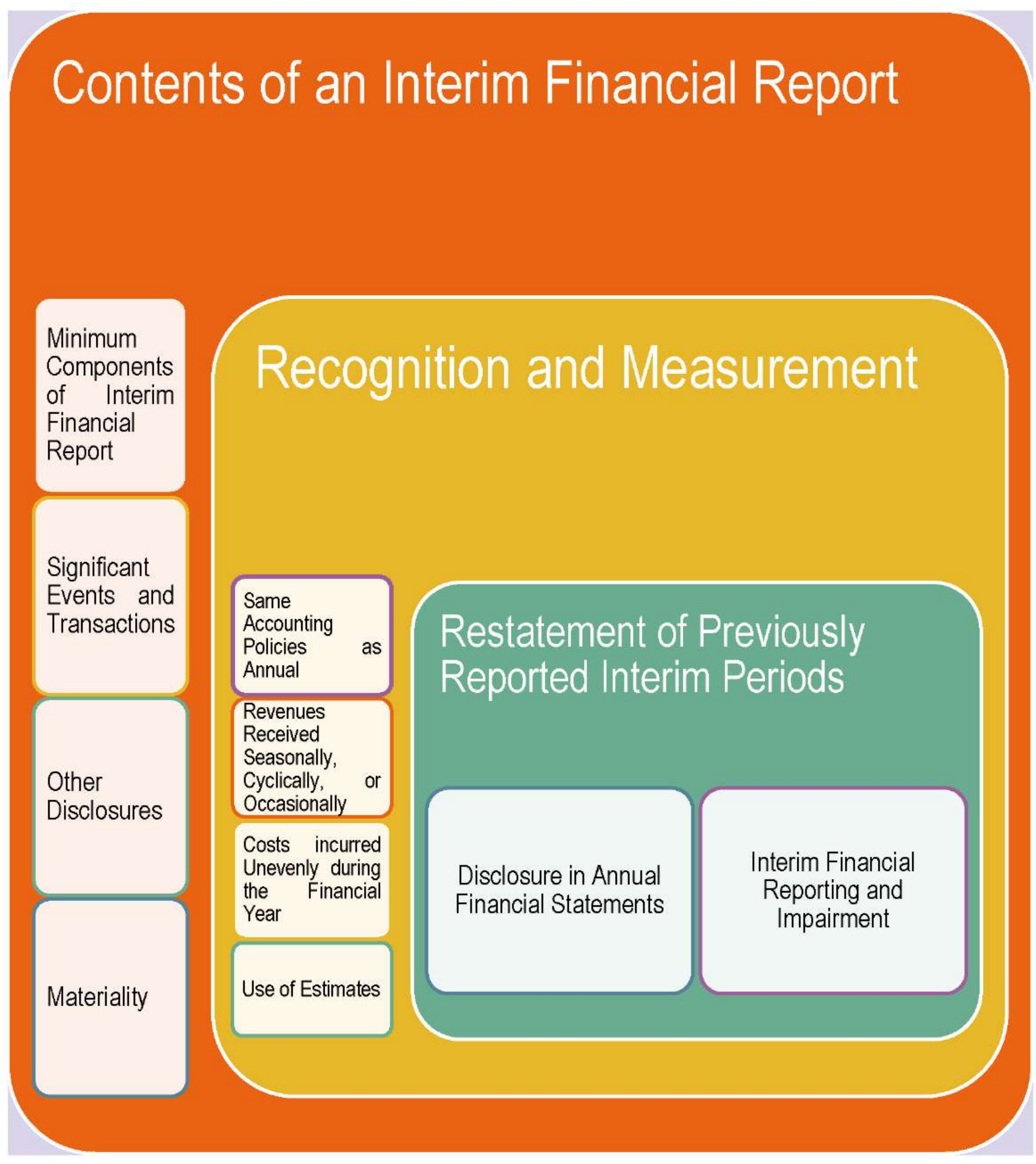
Chapter 30

AS 25 – INTERIM FINANCIAL REPORTING

CHAPTER DESIGN

1. INTRODUCTION
2. OBJECTIVE
3. SCOPE
4. DEFINITIONS
5. CONTENTS OF AN INTERIM FINANCIAL REPORT
6. DISCLOSURE IN ANNUAL FINANCIAL STATEMENTS
7. RECOGNITION AND MEASUREMENT
8. RESTATEMENT OF PREVIOUSLY REPORTED INTERIM PERIODS
9. INTERIM FINANCIAL REPORTING AND IMPAIRMENT

1. INTRODUCTION :



Interim Financial Reporting applies when an entity prepares an interim financial report. Ind AS 34 does not mandate an entity as when to prepare such a report. Timely and reliable interim financial reporting improves the ability of investors, creditors, and others to understand an entity's capacity to generate earnings and cash flows and its financial condition and liquidity. Permitting less information to be reported than in annual financial statements (on the basis of providing an update to those financial statements), the standard outlines the recognition, measurement and disclosure requirements for interim reports.

2. OBJECTIVE :

The objective of this Standard is to prescribe

a) the minimum content of an interim financial report

b) the principles for recognition and measurement in complete or condensed financial statements for an interim period.

3. SCOPE :

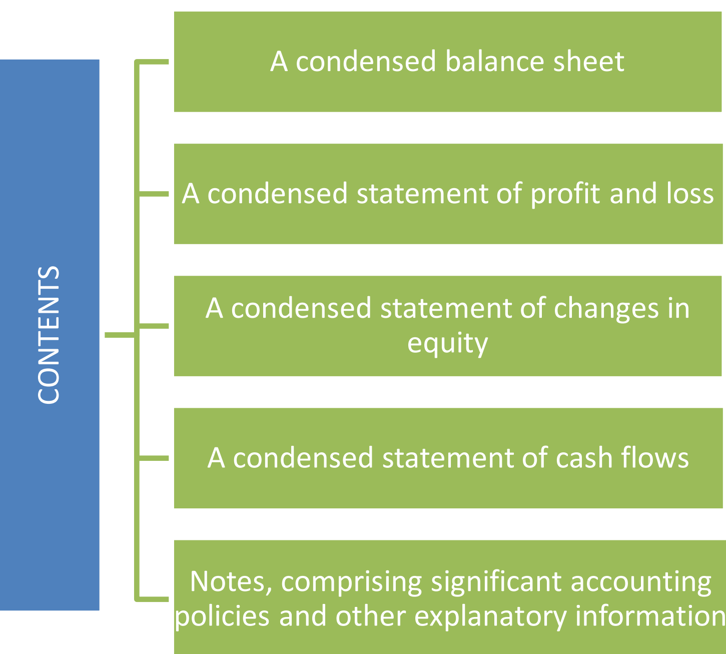
- This Standard does not mandate which entities should be required to publish interim financial reports, how frequently, or how soon after the end of an interim period.
- This Standard applies if an entity is required or elects to publish an interim financial report in accordance with Indian Accounting Standards (Ind AS).
- Each financial report, annual or interim, is evaluated on its own for conformity to Ind AS. The fact that an entity may not have provided interim financial reports during a particular financial year or may have provided interim financial reports that do not comply with this Standard does not prevent the entity's annual financial statements from conforming to Ind AS if they otherwise do so.
- If an entity's interim financial report is described as complying with Ind AS, it must comply with all of the requirements of this Standard.

4. DEFINITIONS :

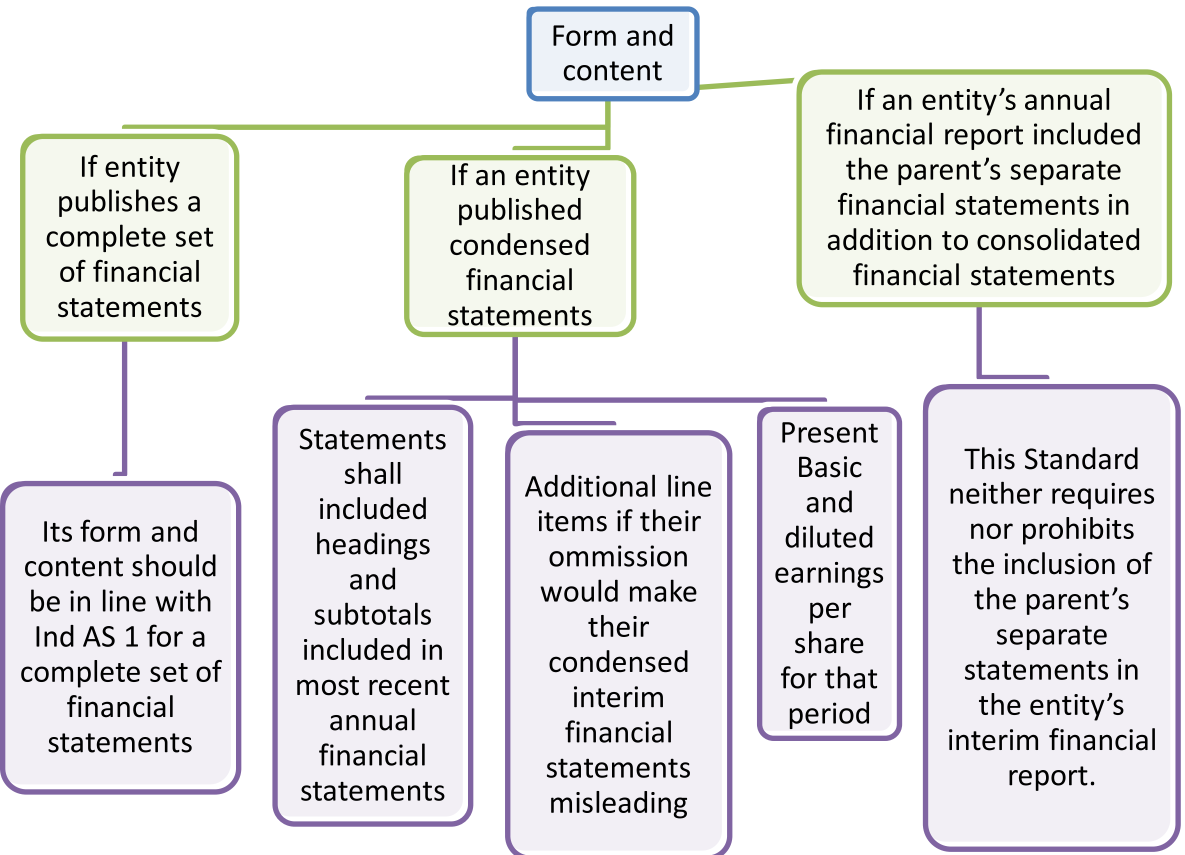
1. **Interim period** is a financial reporting period shorter than a full financial year.

2. **Interim financial report** means a financial report containing either a complete set of financial statements (as described in Ind AS 1, Presentation of Financial Statements), or a set of condensed financial statements (as described in this Standard) for an interim period.

5. CONTENTS OF INTERIM FINANCIAL :



5.1 Form And Content of Interim Financial Report :



5.2 Significant Events and Transactions :

The following is a list of events and transactions for which disclosures would be required if they are significant: the list is not exhaustive.	
1.	the write-down of inventories to net realisable value and the reversal of such writedown;
2.	recognition of a loss from the impairment of financial assets, property, plant and equipment, intangible assets, assets arising from contracts with customers, or other assets, and the reversal of such an impairment loss;
3.	the reversal of any provisions for the costs of restructuring;
4.	acquisitions and disposals of items of property, plant and equipment;
5.	commitments for the purchase of property, plant and equipment;
6.	litigation settlements;
7.	corrections of prior period errors;
8.	changes in the business or economic circumstances that affect the fair value of the entity's financial assets and financial liabilities, whether those assets or liabilities are recognised at fair value or amortised cost;

9.	any loan default or breach of a loan agreement that has not been remedied on or before the end of the reporting period;
10.	related party transactions;
11.	transfers between levels of the fair value hierarchy used in measuring the fair value of financial instruments;
12.	changes in the classification of financial assets as a result of a change in the purpose or use of those assets; and
13.	changes in contingent liabilities or contingent assets.

5.3 Other Disclosures :

a)	a statement that the same accounting policies and methods of computation are followed in the interim financial statements. If those recently used policies or methods have been changed, a description of the nature and effect of the change should also be given.
b)	explanatory comments about the seasonality or cyclicality of interim operations.
c)	the nature and amount of items affecting assets, liabilities, equity, net income or cash flows that are unusual because of their nature, size or incidence.
d)	the nature and amount of changes in estimates of amounts reported in prior interim periods of the current financial year or changes in estimates of amounts reported in prior financial years.
e)	issues, repurchases and repayments of debt and equity securities.
f)	dividends paid (aggregate or per share) separately for ordinary shares and other shares
g)	Segment information as per IND AS 108
h)	events after the interim period that have not been reflected in the financial statements for the interim period.
i)	the effect of changes in the composition of the entity during the interim period, including business combinations, obtaining or losing control of subsidiaries and long-term investments, restructurings, and discontinued operations. In the case of business combinations, the entity shall disclose the information required by Ind AS 103, Business Combinations.
j)	for financial instruments, the disclosures about fair value of Ind AS 113, Fair Value Measurement, and Ind AS 107, Financial Instruments: Disclosures.
k)	for entities becoming, or ceasing to be, investment entities, as defined in Ind AS 110, Consolidated Financial Statements, the disclosures in Ind AS 112, Disclosure of Interests in Other Entities.
l)	the disaggregation of revenue from contracts with customers required by Ind AS 115, Revenue from Contracts with Customers.

5.4 Periods for which Interim Financial Statements are Required to be Presented :

Interim reports shall include interim financial statements (condensed or complete) for periods as follows:

(a) balance sheet as of the end of the current interim period and a comparative balance sheet as of the end of the immediately preceding financial year.

(b) statements of profit and loss for the current interim period and cumulatively for the current financial year to date, with comparative statements of profit and loss for the comparable interim periods (current and year-to-date) of the immediately preceding financial year.

(c) statement of changes in equity cumulatively for the current financial year to date, with a comparative statement for the comparable year-to-date period of the immediately preceding financial year.

(d) statement of cash flows cumulatively for the current financial year to date, with a comparative statement for the comparable year-to-date period of the immediately preceding financial year. For an entity whose business is highly seasonal, financial information for the twelve months up to the end of the interim period and comparative information for the prior twelve-month period may be useful.

Question 1 : A Company

A company has to prepare interim financial statements for the period ended 31st Dec, 2016. As per IND AS 34 describes the periodicity of its interim financial statements along with comparatives.

5.5 Materiality :

- In deciding how to recognise, measure, classify, or disclose an item for interim financial reporting purposes, materiality shall be assessed in relation to the interim period financial data.
- In making assessments of materiality, it shall be recognised that interim measurements may rely on estimates to a greater extent than measurements of annual financial data.
- While judgement is always required in assessing materiality, this Standard bases the recognition and disclosure decision on data for the interim period by itself for reasons of understand ability of the interim figures
- Unusual items, changes in accounting policies or estimates, and errors are recognised and disclosed on the basis of materiality in relation to interim period data to avoid misleading inferences that might result from non-disclosure.

6. DISCLOSURE IN ANNUAL FINANCIAL STATEMENTS :

- If an estimate of an amount reported in an interim period is changed significantly during the final interim period of the financial year but a separate financial report is not published for that final interim period, the nature and amount of that change in estimate shall be disclosed in a note to the annual financial statements for that financial year.
- Ind AS 8 requires disclosure of the nature and (if practicable) the amount of a change in estimate that either has a material effect in the current period or is expected to have a material effect in subsequent periods.
- An entity is not required to include additional interim period financial information in its annual financial statements.

7. RECOGNITION AND MEASUREMENT :

1. Accounting Policies :

An entity shall apply the same accounting policies in its interim financial statements as are applied in its annual financial statements, except for accounting policy changes made after the date of the most recent annual financial statements that are to be reflected in the next annual financial statements.

2. Revenues received cyclically, occasionally or seasonally :

1. Revenues that are received seasonally, cyclically, or occasionally within a financial year shall not be anticipated or deferred as of an interim date if anticipation or deferral would not be appropriate at the end of the entity's financial year.
   Examples include dividend revenue, royalties, and government grants.
2. Certain entities earn more revenue in certain interim periods of a financial year than other interim periods. Such revenues are recognised when they occur.
   Example seasonal revenues of retailers.

3. Costs incurred unevenly during the financial year :

Costs that are incurred unevenly during an entity's financial year shall be anticipated or deferred for interim reporting purposes if, and only if, it is also appropriate to anticipate or defer that type of cost at the end of the financial year

4. Use of Estimates :

1. To ensure that the resulting information is reliable and that all material financial information that is relevant to an understanding of the financial position or performance of the entity is appropriately disclosed.
2. The preparation of interim financial reports requires a greater use of estimation methods than annual financial reports.

Examples :

Employer payroll taxes and insurance contributions

If employer payroll taxes or contributions to government-sponsored insurance funds are assessed on an annual basis, the employer's related expense is recognised in interim periods using an estimated average annual effective payroll tax or contribution rate, even though a large portion of the payments may be made early in the financial year. A common example is an employer payroll tax or insurance contribution that is imposed up to a certain maximum level of earnings per employee. For higher income employees, the maximum income is reached before the end of the financial year, and the employer makes no further payments through the end of the year.

Major planned periodic maintenance or overhaul

The cost of a planned major periodic maintenance or overhaul or other seasonal expenditure that is expected to occur late in the year is not anticipated for interim reporting purposes unless an event has caused the entity to have a legal or constructive obligation. The mere intention or necessity to incur expenditure related to the future is not sufficient to give rise to an obligation.

Provisions

A provision is recognised when an entity has no realistic alternative but to make a transfer of economic benefits as a result of an event that has created a legal or constructive obligation. The amount of the obligation is adjusted upward or downward, with a corresponding loss or gain recognised in profit or loss, if the entity's best estimate of the amount of the obligation changes. This Standard requires that an entity apply the same criteria for recognising and measuring a provision at an interim date as it would at the end of its financial year. The existence or non-existence of an obligation to transfer benefits is not a function of the length of the reporting period. It is a question of fact.

Year-end bonuses

The nature of year-end bonuses varies widely. Some are earned simply by continued employment during a time period. Some bonuses are earned based on a monthly, quarterly, or annual measure of operating result. They may be purely discretionary, contractual, or based on years of historical precedent.

A bonus is anticipated for interim reporting purposes if, and only if, (a) the bonus is a legal obligation or past practice would make the bonus a constructive obligation for which the entity has no realistic alternative but to make the payments, and (b) a reliable estimate of the obligation can be made. Ind AS 19, Employee Benefits provides guidance.

Variable lease payments

Contingent lease payments can be an example of a legal or constructive obligation that is recognised as a liability. If a lease provides for contingent payments based on the lessee achieving a certain level of annual sales, an obligation can arise in the interim periods of the financial year before the required annual level of sales has been achieved, if that required level of sales is expected to be achieved and the entity, therefore, has no realistic alternative but to make the future lease payment.

Intangible assets

An entity will apply the definition and recognition criteria for an intangible asset in the same way in an interim period as in an annual period. Costs incurred before the recognition criteria for an intangible asset are met, are recognised as an expense. Costs incurred after the specific point in time at which the criteria are met are recognised as part of the cost of an intangible asset. 'Deferring' costs as assets in an interim balance sheet in the hope that the recognition criteria will be met later in the financial year is not justified.

Vacations, holidays, and other short-term compensated absences

Accumulating compensated absences are those that are carried forward and can be used in future periods if the current period's entitlement is not used in full. Ind AS 19, Employee Benefits requires that an entity measure the expected cost of and obligation for accumulating compensated absences at the amount the entity expects to pay as a result of the unused entitlement that has accumulated at the end of the reporting period. That principle is also applied at the end of interim financial reporting periods. Conversely, an entity recognises no expense or liability for non-accumulating compensated absences at the end of an interim reporting period, just as it recognises none at the end of an annual reporting period.

Other planned but irregularly occurring costs

An entity's budget may include certain costs expected to be incurred irregularly during the financial year, such as charitable contributions and employee training costs. Those costs generally are discretionary even though they are planned and tend to recur from year to year. Recognising an obligation at the end of an interim financial reporting period for such costs that have not yet been incurred generally is not consistent with the definition of a liability.

Measuring interim income tax expense

Interim period income tax expense is accrued using the tax rate that would be applicable to expected total annual earnings, that is, the estimated average annual effective income tax rate applied to the pre-tax income of the interim period.

Depreciation and amortisation

Depreciation and amortisation for an interim period is based only on assets owned during that interim period. It does not take into account asset acquisitions or dispositions planned for later in the financial year.

Question 2 : Company A

Company A has reported Rs.60,000 as pre tax profit in first quarter and expects a loss of Rs.15,000 each in the subsequent quarters. It has a corporate tax slab of 20 percent on the first Rs.20,000 of annual earnings and 40 per cent on all additional earnings. Calculate the amount of tax to be shown in each quarter.

Question 3 : An enterprise

An enterprise reports quarterly. At the end of Q-1 estimate of pre-tax annual profit was Rs.6 lakhs and aggregate of deductions from GTO under tax laws was estimated at Rs.1 lakh.

At the end of Q-2, estimate of Pre-tax annual profit was Rs.6.30 lakhs and aggregate of deductions from GTI under tax law was estimated at Rs. 84,000.

The pre-tax earnings of Q-1 and Q-2 was 1.2 lakh and 1.3 lakh. Tax rate is 30%. Compute PAT for the quarters.

Question 4 : An enterprise

An enterprise that reports quarterly earned Rs.1 lakhs before tax at the end of Q1 and Rs.1.5 lakhs at the end of Q2. The annual PBT estimated at the end of Q1 was Rs.4 lakhs and that the end of Q2 was Rs.5 lakhs. The company has a carry forward loss of Rs.1 lakh. The applicable tax rate is 40%. Compute PAT for the quarters.

Question 5 : (May 2011 – 4 marks)

An enterprise reports quarterly, estimates an annual income of Rs.10 lakhs. Assume tax rates on 1st 5,00,000 at 30% and on the balance income at 40%. The estimated quarterly income are Rs.75,000, Rs.2,50,000, Rs.3,75,000 and Rs.3,00,000

Calculate the tax expense to be recognised in each quarter.

Question 6 : X Ltd.

X Ltd. holds equity shares worth in Y Ltd. Y Ltd is doing well and is sure to declare dividend for the current year. While preparing the IFR, X Ltd. recognises pro-rate dividend income, which has not actually been received by it. Is the treatment right ? Discuss.

Question 7 : Innovative Corporation Private Limited

Innovative Corporation Private Limited (or “ICPL”) is dealing in seasonal product and the sales pattern of the product, quarter wise is as under during the financial year 20X1-20X2:

Qtr. I	Qtr. II	Qtr. III	Qtr. IV
ending 30 June	ending 30 September	ending 31 December	ending 31 March
10%	10%	60%	20%

For the first quarter ending on 30 June, 20X1, ICPL has provided the following information :

Particulars	Amounts (in crore)
Sales	70
Employees benefits expenses	25
Administrative and other expenses	12
Finance cost	4

ICPL while preparing interim financial report for first quarter wants to defer Rs.16 crores expenditure to third quarter on the argument that third quarter is having more sales therefore third quarter should be debited by more expenditure. Considering the seasonal nature of business and that the expenditures are uniform throughout all quarte Rs.

Calculate the result of first quarter as per Ind AS 34 and comment on the company’s view.

Question 8 : Innovative Corporation Private Limited

Fixed production overheads for the financial year is Rs. 10,000. Normal expected production for the year, after considering planned maintenance and normal breakdown, also considering the future demand of the product is 2,000 MT. It is considered that there are no quarterly / seasonal variations. Therefore, the normal expected production for each quarter is 500 MT and the fixed production overheads for the quarter are Rs. 2,500.

Actual production achieved	Quantity (In MT)
First quarter	400
Second quarter	600
Third quarter	500
Fourth quarter	400
Total	**1,900**

Presuming that there are no quarterly / seasonal variation, calculate the allocation of fixed production overheads for all the four quarters as per Ind AS 34 read with Ind AS 2. Will the quarterly results affect the annual results?

8. RESTATEMENT OF PREVIOUSLY REPORTED INTERIM PERIODS :

A change in accounting policy, other than one for which the transition is specified by a new Ind AS, shall be reflected by:

(a) restating the financial statements of prior interim periods of the current financial year and the comparable interim periods of any prior financial years that will be restated in the annual financial statements in accordance with Ind AS 8; or

(b) when it is impracticable to determine the cumulative effect at the beginning of the financial year of applying a new accounting policy to all prior periods, adjusting the financial statements of prior interim periods of the current financial year, and comparable interim periods of prior financial years to apply the new accounting policy prospectively from the earliest date practicable.

9. INTERIM FINANCIAL REPORTING AND IMPAIRMENT :

An entity is required to assess goodwill for impairment at the end of each reporting period, and, if required, to recognise an impairment loss at that date in accordance with Ind AS 36. However, at the end of a subsequent reporting period, conditions may have so changed that the impairment loss would have been reduced or avoided had the impairment assessment been made only at that date.

Accordingly, an entity shall not reverse an impairment loss recognised in a previous interim period in respect of goodwill.

Question 9 : ABC Ltd.

ABC Limited manufactures automobile parts. ABC Limited has shown a net profit of Rs 20,00,000 for the third quarter of 2011.

Following adjustments are made while computing the net profit:

(i) Bad debts of Rs.1,00,000 incurred during the quarter. 50% of the bad debts have been deferred to the next quarter.

(ii) Additional depreciation of Rs.4,50,000 resulting from the change in the method of depreciation.

(iii) Rs.5,00,000 expenditure on account of administrative expenses pertaining to the third quarter is deferred on the argument that the fourth quarter will have more sales; therefore fourth quarter should be debited by higher expenditure. The expenditures are uniform throughout all quarters.

Ascertain the correct net profit to be shown in the Interim Financial Report of third quarter to be presented to the Board of Directors.

PRACTICAL QUESTIONS :

Question 10 : A Ltd.

A Ltd has Rs.1,02,000 net income for the quarter ended 31sr December, 2017 including the following items.

Rs.16,000 cumulative effect loss resulting from change in method of inventory valuation method was recognised on Nov 2, 2017. Out of the this loss Rs.10,000 relates to the previous quarters.

Compute the profit as per IND AS – 34 for the quarter ended 31st Dec, 2017.

Question 11 : RM Ltd. (May 2005)

RM Ltd. is dealing in seasonal products

For the first quarter ending 31st March, 2017. RM gives you the following information

Sales	50 crores
Salary and other expenses	30 crores
Advertisement Expenses	2 crores
Administrative and Selling expenses	8 crores

While preparing interim financial report for the first quarter RM wants to defer Rs.21 crores expenditure to third quarter on the argument that third quarter is having more sales, therefore third quarter should be debited by higher expenditure, considering the seasonal nature of business

Calculate the result of first quarter.

Question 12 – X Limited (May 2012 – 5 Marks)

On 30-6-2011, X Limited incurred Rs.3,00,000 net loss from disposal of a business segment. Also on 31-7-2011, the company paid Rs.80,000 for property taxes assessed for the calendar year 2011. How should the above transactions be included in determination of net income of X Limited for the six months interim period ended on 30-9-2011?

Question 13 – SM Ltd.

SM Ltd shows the net profit of Rs.5,40,000 for the quarter III after incorporating the following

- Extraordinary loss of Rs.28,000 incurred during the quarter has been fully recognised in this quarter
- Additional Depreciation of Rs.36,000 resulting from the change of method of depreciation.

Do you agree with the treatments adopted by the company? If not, find out the correct quarterly income.

Question 14 : Company A

Company A expects to earn Rs. 15,000 pre-tax profit each quarter and has a corporate tax slab of 20 percent on the first Rs. 20,000 of annual earnings and 40 per cent on all additional earnings. Actual earnings match expectations. Calculate the amount of income tax to be shown in each quarter.

Question 15 : Narayan Ltd.

Narayan Ltd. provides you the following information and asks you to calculate the tax expense for each quarter, assuming that there is no difference between the estimated taxable income and the estimated accounting income:

Estimated Gross Annual Income 33,00,000

(inclusive of Estimated Capital Gains of Rs. 8,00,000)

Estimated Income of Quarter I is Rs. 7,00,000, Quarter II is Rs. 8,00,000, Quarter III (including Estimated Capital Gains of Rs. 8,00,000) is Rs. 12,00,000 and Quarter IV is Rs. 6,00,000.

Tax Rates:	On Capital Gains		12%
	On Other Income:	First Rs. 5,00,000	30%
		Balance Income·	40%

Question 16 : An entity

An entity reports quarterly, earns Rs. 1,50,000 pre-tax profit in the first quarter but expects to incur losses of Rs. 50,000 in each of the three remaining quarter Rs. The entity operates in a jurisdiction in which its estimated average annual income tax rate is 30%.

The management believes that since the entity has zero income for the year, its income-tax expense for the year will be zero. State whether the management's views are correct or not? If not, then calculate the tax expense for each quarter as well as for the year as per Ind AS 34.

Question 17 : Happy India Ltd.

Due to decline in market price in second quarter, Happy India Ltd. incurred an inventory loss. The Market price is expected to return to previous levels by the end of the year. At the end of year, the decline had not reversed. When should the loss be reported in interim statement of profit and loss of Happy India Ltd.?

Question 18 : An entity

An entity's accounting year ends is 31st December, but its tax year end is 31st March. The entity publishes an interim financial report for each quarter of the year ended 31st December, 2019. The entity's profit before tax is steady at Rs.10,000 each quarter, and the estimated effective tax rate is 25% for the year ended 31st March, 2019 and 30% for the year ended 31st March, 2020.

How the related tax charge would be calculated for the year 2019 and its quarters.

MCQs :

1. AS 25 mandates the following in relation to interim financial reports.
   (a) which entities should publish interim financial reports.
   (b) how frequently it should publish interim financial reports.
   (c) how soon it should publish after the end of interim period.
   (d) none of the above.
2. The standard defines Interim financial Report as a financial report for an interim period that contains a set of ………. financial statements.
   (a) Complete
   (b) Condensed
   (c) Financial statement similar to annual
   (d) Either complete or condensed
3. ABC Limited has reported Rs. 85,000 as per tax profit in first quarter and expects a loss of Rs. 25,000 each in subsequent quarters. It has corporate tax rate slab of 20% on the first Rs. 20,000 earnings and 40% on all additional earnings. Calculate tax expenses that should report in first quarter interim financial report.
   (a) Rs. 17,000
   (b) Rs. 30,000
   (c) Rs. 2,000
   (d) AS 25 does not mandate to report tax expenses
4. An entity prepares quarterly interim financial reports in accordance with AS 25. The entity is engaged in sale of mobile phones and normally 5% of customers claim on their warranty. The provision in the first quarter was calculated as 5% of sales to date, which was Rs.10 million. However, in the second quarter, a fault was found and warranty claims were expected to be 10% for the whole of the year. Sales in the second quarter were Rs.15 million. What would be the provision charged in the second quarter's interim financial statements?
   (a) Rs.1 million (b) Rs. 2 million
   (c) Rs. 1.25 million (d) Rs. 1.5 million

Thanks ….

Chapter 31

AMALGAMATION OF COMPANIES

CHAPTER DESIGN

1. PRACTICAL QUESTIONS
2. MCQ'S

1. PRACTICAL QUESTIONS :

Question 1 : S Ltd.

S. Ltd. is absorbed by P. Ltd. The draft balance sheet of S. Ltd. is as under:

Balance Sheet

	Rs.		Rs.
Share Capital:			
2,000 7% Preference shares of Rs.100 each (fully paid-up)	2,00,000	Sundry Assets	13,00,000
5,000 Equity shares of Rs.100 each (fully paid-up)	5,00,000		
Reserves	3,00,000		
6% Debentures	2,00,000		
Trade payables	1,00,000		
	13,00,000		**13,00,000**

P. Ltd. has agreed:

(i) to issue 9% Preference shares of Rs.100 each, in the ratio of 3 shares of P. Ltd. for 4 preference shares in S. Ltd.

(ii) to issue to the debenture-holders in S. Ltd. 8% Mortgage Debentures at Rs.96 in lieu of 6% Debentures in S. Ltd. which are to be redeemed at a premium of 20%;

(iii) to pay Rs.20 per share in cash and to issue six equity shares of Rs.100 each (market value Rs.125) in lieu of every five shares held in S. Ltd.; and

(iv) to assume the liability to trade payables.

You are required to calculate the purchase consideration.

Question 2 : Y Ltd.

Y Ltd. decides to absorb X Ltd. The draft Balance Sheet of X Ltd. is as follows:

	Rs.		Rs.
3,000 Equity shares of Rs.100 each (fully paid)	3,00,000	Net assets	2,90,000
Preference shares	60,000	Profit and Loss Account	70,000
	3,60,000		**3,60,000**

Y Ltd. agrees to take over the net assets of X Ltd. An equity share in X Ltd., for purposes of absorption, is valued @ Rs.70. Y Ltd. agrees to pay Rs.60,000 in cash for payment to preference shareholders equity shares will be issued at value of Rs.120 each. Calculate purchase consideration to be paid by Y Ltd. and how will it be discharged?

Question 3 : Neel Ltd. and Gagan Ltd.

Neel Ltd. and Gagan Ltd. amalgamated to form a new company on 1.04.20X1. Following is the Draft Balance Sheet of Neel Ltd. and Gagan Ltd. as at 31.3.20X1:

Liabilities	Neel	Gagan	Assets	Neel	Gagan
	Rs.	Rs.		Rs.	Rs.
Capital	7,75,000	8,55,000	Plant & Machinery	4,85,000	6,14,000
Current liabilities	6,23,500	5,57,600	Building	7,50,000	6,40,000
			Current assets	1,63,500	1,58,600
	13,98,500	**14,12,600**		**13,98,500**	**14,12,600**

Following are the additional information:

(i) The authorised capital of the new company will be Rs.25,00,000 divided into 1,00,000 equity shares of Rs.25 each.

(ii) Liabilities of Neel Ltd. includes Rs.50,000 due to Gagan Ltd. for the purchases made. Gagan Ltd. made a profit of 20% on sale to Neel Ltd.

(iii) Neel Ltd. had purchased goods costing Rs.10,000 from Gagan Ltd. All these goods are included in the current asset of Neel Ltd. as at 31st March, 20X1.

(iv) The assets of Neel Ltd. and Gagan Ltd. are to be revalued as under:

	Neel	Gagan
	Rs.	Rs.
Plant and machinery	5,25,000	6,75,000
Building	7,75,000	6,48,000

(v) The purchase consideration is to be discharged as under:

(a) Issue 24,000 equity shares of Rs.25 each fully paid up in the proportion of their profitability in the preceding 2 years.

(b) Profits for the preceding 2 years are given below:

	Neel	Gagan
	Rs.	Rs.
1st year	2,62,800	2,75,125
2nd year	2,12,200	2,49,875
Total	4,75,000	5,25,000

(c) Issue 12% preference shares of Rs.10 each fully paid up at par to provide income equivalent to 8% return on net assets in the business as on 31.3.20X1 after revaluation of assets of Neel Ltd. and Gagan Ltd. respectively.

You are required to compute the

(i) equity and preference shares issued to Neel Ltd. and Gagan Ltd.,

(ii) Purchase consideration.

Question 4 : X Ltd. and Y Ltd.

Consider the following summarized balance sheets of X Ltd. and Y Ltd.

Balance Sheet as on 31st March, 20X1

Liabilities	X Ltd.	Y Ltd.	Assets	X Ltd.	Y Ltd.
	Rs. '000	Rs. '000		Rs. '000	Rs. '000
Equity Share Capital (Rs.10 each)	50,00	30,00	Land & Building	25,00	15,50
14% Preference Share Capital (Rs.100 each)	22,00	17,00	Plant & Machinery	32,50	17,00
General Reserve	5,00	2,50	Furniture & Fittings	5,75	3,50
Export Profit Reserve	3,00	2,00	Investments	7,00	5,00
Investment Allowance		1,00	Inventory	12,50	9,50
Reserve			Trade receivables	9,00	10,30
Profit & Loss A/c	7,50	5,00	Cash & Bank	7,25	5,20
13% Debentures (Rs.100 each)	5,00	3,50			
Trade payables	4,50	3,50			
Other Current Liabilities	2,00	1,50			
	99,00	66,00		99,00	66,00

X Ltd. takes over Y Ltd. on 1st April, 20X1. X Ltd. discharges the purchase consideration as below:

(i) Issued 3,50,000 equity shares of Rs.10 each at par to the equity shareholders of Y Ltd.

(ii) Issued 15% preference shares of Rs.100 each to discharge the preference shareholders of Y Ltd. at 10% premium.

The debentures of Y Ltd. will be converted into equivalent number of debentures of X Ltd.

The statutory reserves of Y Ltd. are to be maintained for 2 more years.

Show the balance sheet of X Ltd. after amalgamation on the assumption that:

(a) the amalgamation is in the nature of merger.

(b) the amalgamation is in the nature of purchase.

Question 5 : Better Ltd.

The following draft Balance Sheets are given as on 31st March, 20X1:

(Rs. In lakhs)

Liabilities	Best Ltd.	Better Ltd.	Assets	Best Ltd.	Better Ltd.
	Rs.	Rs.		Rs.	Rs.
Share Capital:			Fixed Assets	25	15
Shares of Rs.100, each fully paid	20	10	Investments	5	–
Reserve and Surplus	10	8	Current Assets	20	5
Other Liabilities	20	2			
	50	20		50	20

The following further information is given —

(a) Better Limited issued bonus shares on 1st April, 20X1, in the ratio of one share for every two held, out of Reserves and Surplus.

(b) It was agreed that Best Ltd. will take over the business of Better Ltd., on the basis of the latter's Balance Sheet, the consideration taking the form of allotment of shares in Best Ltd.

(c) The value of shares in Best Ltd. was considered to be Rs.150 and the shares in Better Ltd. were valued at Rs.100 after the issue of the bonus shares. The allotment of shares is to be made on the basis of these values.

(d) Liabilities of Better Ltd., included Rs.1 lakh due to Best Ltd., for purchases from it, on which Best Ltd., made profit of 25% of the cost. The goods of Rs.50,000 out of the said purchases, remained in stock on the date of the above Balance Sheet.

Make the closing ledger in the Books of Better Ltd. and the opening journal entries in the Books of Best Ltd., and prepare the Balance Sheet as at 1st April, 20X1 after the takeover.

Question 6 : K Ltd. and L Ltd.

K Ltd. and L Ltd. amalgamate to form a new company LK Ltd. The financial position of these two companies on the date of amalgamation was as under:

Liabilities	K Ltd.	L Ltd.	Assets	K Ltd.	L Ltd.
	Rs.	Rs.		Rs.	Rs.
Share Capital			Goodwill	80,000	
Equity Shares of Rs.100 each	8,00,000	3,00,000	Land & Building	4,50,000	3,00,000
7% Preference Share of Rs.100 each	4,00,000	3,00,000	Plant & Machinery	6,20,000	5,00,000

5% Debentures	2,00,000	-	Furniture and Fittings	60,000	20,000
General Reserve	-	1,00,000	Trade receivables	2,75,000	1,75,000
Profit and Loss Account	3,71,375	97,175	Stores & inventory	2,25,000	1,40,000
Trade payables	1,00,000	2,10,000	Cash at Bank	1,20,000	55,000
Secured Loan	-	2,00,000	Cash in hand	41,375	17,175
	18,71,375	**12,07,175**		**18,71,375**	**12,07,175**

The terms of amalgamation are as under:

(A) (1) The assumption of liabilities of both the Companies.

(2) Issue of 5 Preference shares of Rs.20 each in LK Ltd. @ Rs.18 paid up at premium of Rs.4 per share for each preference share held in both the Companies.

(3) Issue of 6 Equity shares of Rs.20 each in LK Ltd. @ Rs.18 paid up at a premium of Rs.4 per share for each equity share held in both the Companies. In addition, necessary cash should be paid to the Equity Shareholders of both the Companies as is required to adjust the rights of shareholders of both the Companies in accordance with the intrinsic value of the shares of both the Companies.

(4) Issue of such amount of fully paid 6% debentures in LK Ltd. as is sufficient to discharge the 5% debentures in K Ltd. at a discount of 5% after takeover.

(B) (1) The assets and liabilities are to be taken at book values inventory and trade receivables for which provisions at 2% and 2 ½ % respectively to be raised.

(2) The trade receivables of K Ltd. include Rs.20,000 due from L Ltd.

(C) The LK Ltd. is to issue 15,000 new equity shares of Rs.20 each, Rs.18 paid up at premium of Rs.4 per share so as to have sufficient working capital. Prepare ledger accounts in the books of K Ltd. and L Ltd. to close their books.

Question 7 : A Ltd. and B Ltd.

The following are the summarized Balance Sheets of A Ltd. and B Ltd. as on 31.3.20X1:

		(Rs. in thousands)
	A Ltd.	**B Ltd.**
Liabilities		
Share capital:		
Equity shares of 100 each fully paid up	2,000	1,000
Reserves	1,000	---

10% Debentures	500	---
Loans from Banks	250	450
Bank overdrafts	---	50
Trade payables	300	300
Total	**4,050**	**1,800**
Assets		
Tangible assets/fixed assets	2,700	850
Investments	700	---
Trade receivables	400	150
Cash at bank	250	---
Accumulated loss	---	800
Total	**4,050**	**1,800**

B Ltd. has acquired the business of A Ltd. The following scheme of merger was approved:

(i) Banks agreed to waive off the loan of Rs.60 thousands of B Ltd.

(ii) B Ltd. will reduce its shares to Rs.10 per share and then consolidate 10 such shares into one share of Rs.100 each (new share).

(iii) Shareholders of A Ltd. will be given one share (new) of B Ltd. in exchange of every share held in A Ltd.

(iv) Trade payables of B Ltd. includes Rs.100 thousands payable to A Ltd.

Pass necessary entries in the books of B Ltd. and prepare Balance Sheet after merger.

Question 8 : P Ltd. and Q Ltd.

The following are the summarized Balance Sheets of P Ltd. and Q Ltd. as on 31st March, 20X1:

Liabilities	P Ltd.	Q Ltd.	Assets	P Ltd.	Q Ltd.
	Rs.	Rs.		Rs.	Rs.
Share Capital			Fixed Assets	7,00,000	2,50,000
Equity Shares of Rs.10 each	6,00,000	3,00,000	Investment	80,000	80,000
10% Pref. Shares of Rs.100 each	2,00,000	1,00,000	Current Assets:		
Reserves and Surplus	3,00,000	2,00,000	Inventory	2,40,000	3,20,000
Secured Loans:			Trade receivables	4,20,000	2,10,000
12% Debentures	2,00,000	1,50,000	Cash at Bank	1,10,000	40,000
Current Liabilities:					
Trade payables	2,50,000	1,50,000			

	15,50,000	**9,00,000**		**15,50,000**	**9,00,000**

Details of Trade receivables and trade payables are as under:

	P Ltd. (Rs.)	Q Ltd. (Rs.)
Trade receivables		
Debtors	3,60,000	1,90,000
Bills Receivable	60,000	20,000
	4,20,000	2,10,000
Trade payables		
Sundry Creditors	2,20,000	1,25,000
Bills Payable	30,000	25,000
	2,50,000	1,50,000

Fixed Assets of both the companies are to be revalued at 15% above book value. Inventory in Trade and Debtors are taken over at 5% lesser than their book value. Both the companies are to pay 10% Equity dividend, Preference dividend having been already paid.

After the above transactions are given effect to, P Ltd. will absorb Q Ltd. on the following terms:

(i) 8 Equity Shares of Rs.10 each will be issued by P Ltd. at par against 6 shares of Q Ltd.

(ii) 10% Preference Shareholders of Q Ltd. will be paid at 10% discount by issue of 10% Preference Shares of Rs.100 each at par in P Ltd.

(iii) 12% Debenture holders of Q Ltd. are to be paid at 8% premium by 12% Debentures in P Ltd. issued at a discount of 10%.

(iv) Rs.30,000 is to be paid by P Ltd. to Q Ltd. for Liquidation expenses. Sundry Creditors of Q Ltd. include Rs.10,000 due to P Ltd.

Prepare:

(a) Journal entries in the books of P Ltd.

(b) Statement of consideration payable by P Ltd.

Question 9 : Hari Ltd. and Vayu Ltd.

The financial position of two companies Hari Ltd. and Vayu Ltd. as on 31st March, 20X1 was as under:

Assets	Hari Ltd. (Rs.)	Vayu Ltd. (Rs.)
Goodwill	50,000	25,000
Building	3,00,000	1,00,000
Machinery	5,00,000	1,50,000
Inventory	2,50,000	1,75,000

Trade receivables	2,00,000	1,00,000
Cash at Bank	50,000	20,000
	13,50,000	5,70,000
Liabilities	**Hari Ltd. (Rs.)**	**Vayu Ltd. (Rs.)**
Share Capital:		
Equity Shares of Rs.10 each	10,00,000	3,00,000
9% Preference Shares of Rs.100 each	1,00,000	–
10% Preference Shares of Rs.100 each	–	1,00,000
General Reserve	70,000	70,000
Retirement Gratuity fund	50,000	20,000
Trade payables	1,30,000	80,000
	13,50,000	5,70,000

Hari Ltd. absorbs Vayu Ltd. on the following terms:

(a) 10% Preference Shareholders are to be paid at 10% premium by issue of 9% Preference Shares of Hari Ltd.

(b) Goodwill of Vayu Ltd. is valued at Rs.50,000, Buildings are valued at Rs.1,50,000 and the Machinery at Rs.1,60,000.

(c) Inventory to be taken over at 10% less value and Provision for Doubtful Debts to be created @ 7.5%.

(d) Equity Shareholders of Vayu Ltd. will be issued Equity Shares @ 5% premium.

Prepare necessary Ledger Accounts to close the books of Vayu Ltd. and show the acquisition entries in the books of Hari Ltd. Also draft the Balance Sheet after absorption as at 31st March, 20X1.

Question 10 : Yes Ltd. and No Ltd.

The following are the summarised Balance Sheets of Yes Ltd. and No Ltd. as on 31st October, 20X1:

		Yes Ltd.		No Ltd.
		Rs. (in crores)		**Rs. (in crores)**
Sources of funds:				
Share capital:				
Authorised	-	25		5
Issued and Subscribed :				
Equity Shares of Rs.10 each fully paid		12		5
Reserves and surplus		88		10
Shareholders funds		100		15
Unsecured loan from Yes Ltd.	-	—		10

	-	100		25
Funds employed in :				
Fixed assets: Cost		70		30
Less: Depreciation	-	(50)		(24)
Written down value		20		6
Investments at cost:				
30 lakhs equity shares of Rs.10 each		3		
Long-term loan to No. Ltd.		10		
Current assets	100		34	
Less : Current liabilities	(33)	67	(15)	19
		100		25

On that day Yes Ltd. absorbed No Ltd. The members of No Ltd. are to get one equity share of Yes Ltd. issued at a premium of Rs.2 per share for every five equity shares held by them in No Ltd. The necessary approvals are obtained.

You are asked to pass journal entries in the books of the two companies to give effect to the above.

Question 11 : X Ltd. and Y Ltd.

The following are the summarised Balance Sheets of X Ltd. and Y Ltd. :

	X Ltd.	Y Ltd.
	Rs.	Rs.
Liabilities :		
Equity Share Capital	1,00,000	50,000
Profit & Loss A/c	10,000	–
Trade payables	25,000	5,000
Loan X Ltd.	—	15,000
	1,35,000	70,000
Assets :		
Sundry Assets	1,20,000	60,000
Loan Y Ltd.	15,000	—
Profit & Loss A/c	—	10,000
	1,35,000	70,000

A new company XY Ltd. is formed to acquire the sundry assets and trade payables of X Ltd. and Y Ltd. and for this purpose, the sundry assets of X Ltd. are revalued at Rs.1,00,000. The debt due to X Ltd. is also to be discharged in shares of XY Ltd.

Show the Ledger Accounts to close the books of X Ltd.

Question 12 : Super Express Ltd.

Super Express Ltd. and Fast Express Ltd. were in competing business. They decided to form a new company named Super Fast Express Ltd. The summarized balance sheets of both the companies were as under:

Super Express Ltd.
Balance Sheet as at 31st December, 20X1

	Rs.		Rs.
20,000 Equity shares of Rs.100 each	20,00,000	Buildings	10,00,000
Provident fund	1,00,000	Machinery	4,00,000
Trade Payables	60,000	Inventory	3,00,000
Insurance reserve	1,00,000	Trade receivables	2,40,000
		Cash at bank	2,20,000
		Cash in hand	1,00,000
	22,60,000		22,60,000

Fast Express Ltd.
Balance Sheet as at 31st December, 20X1

	Rs.		Rs.
10,000 Equity shares of Rs.100 each	10,00,000	Goodwill	1,00,000
Employees profit sharing account	60,000	Buildings	6,00,000
Trade Payables	40,000	Machinery	5,00,000
Reserve account	1,00,000	Inventory	40,000
Surplus	1,00,000	trade receivables	40,000
		Cash at bank	10,000
		Cash in hand	10,000
	13,00,000		13,00,000

The assets and liabilities of both the companies were taken over by the new company at their book values. The companies were allotted equity shares of Rs.100 each in lieu of purchase consideration amounting to Rs.30,000 (20,000 for Super Fast Express Ltd and 10,000 for Fast Express Ltd.).

Prepare opening balance sheet of Super Fast Express Ltd considering pooling method.

Question 13 : P Ltd. and V Ltd.

The following were the summarized Balance Sheets of P Ltd. and V Ltd. as at 31st March, 20X1:

Liabilities	P Ltd.	V Ltd.
	(Rs. in lakhs)	(Rs. in lakhs)

Equity Share Capital (Fully paid shares of Rs.10 each)	15,000	6,000
Securities Premium	3,000	–
Foreign Project Reserve	–	310
General Reserve	9,500	3,200
Profit and Loss Account	2,870	825
12% Debentures	–	1,000
Trade payables	1,200	463
Provisions	1,830	702
	33,400	12,500
Assets	**P Ltd.**	**V Ltd.**
	(Rs. in lakhs)	**(Rs. in lakhs)**
Land and Buildings	6,000	–
Plant and Machinery	14,000	5,000
Furniture, Fixtures and Fittings	2,304	1,700
Inventory	7,862	4,041
Trade receivables	2,120	1,100
Cash at Bank	1,114	609
Cost of Issue of Debentures	—	50
	33,400	12,500

All the bills receivable held by V Ltd. were P Ltd.'s acceptances.

On 1st April 20X1, P Ltd. took over V Ltd in an amalgamation in the nature of merger. It was agreed that in discharge of consideration for the business P Ltd. would allot three fully paid equity shares of Rs.10 each at par for every two shares held in V Ltd. It was also agreed that 12% debentures in V Ltd. would be converted into 13% debentures in P Ltd. of the same amount and denomination.

Details of trade receivables and trade payables as under:

Assets	P Ltd.	V Ltd.
	(Rs. in lakhs)	**(Rs. in lakhs)**
Trade payables		
Bills Payable	120	-
Creditors	1,080	463
	1,200	**463**
Trade receivables		
Trade receivables	2,120	1,020
Bills Receivable	—	80
	2,120	**1,100**

Expenses of amalgamation amounting to Rs.1 lakh were borne by P Ltd.

You are required to :

(i) Pass journal entries in the books of P Ltd. and

(ii) Prepare P Ltd.'s Balance Sheet immediately after the merger considering that the cost of issue of debentures shown in the balance sheet of the V Ltd. company is not transferred to the P Ltd. company.

Question 14 : Wye Ltd.

Wye Ltd. acquires the business of Zed Ltd. whose balance sheet as at 31st March, 20X1 is as under:

		Particulars	Notes	Rs.
		Equity and Liabilities		
1		**Shareholders' funds**		
	A	Share capital	1	12,00,000
	B	Reserves and Surplus	2	1,58,000
2		**Non-current liabilities**		
	A	Long-term borrowings	3	2,00,000
3		**Current liabilities**		
	A	Trade Payables		1,20,000
	B	Other current liabilities		12,000
		(Interest payable on debentures)		
		Total		**16,90,000**
		Assets		
1		**Non-current assets**		
	A	Property, Plant and Equipment	4	10,00,000
	B	Intangible assets	5	2,90,000
2		**Current assets**		
	A	Inventories		1,50,000
	B	Trade receivables		1,80,000
	C	Cash and Cash equivalents		70,000
		Total		**16,90,000**

Note to Accounts :

		Rs.
1	**Share Capital**	
	Equity Share capital (Rs.100 each)	8,00,000
	6% Preference Share capital (Rs.100 each)	4,00,000
		12,00,000

2	**Reserves and Surplus**	
	Capital reserve	1,00,000
	Profit and loss A/c	50,000
	Workmen compensation reserve	
	(Expected liability Rs.5,000)	8,000
		1,58,000
3	**Long-term borrowings**	
	6% Debentures	2,00,000
		2,00,000
4	**Property, Plant and Equipment**	
	Land and Building	4,00,000
	Plant and machinery	6,00,000
		10,00,000
5	**Intangible assets**	
	Goodwill	2,40,000
	Patents	50,000
		2,90,000

Wye Ltd. was to take over all assets (except cash) and liabilities (except for interest due on debentures) and to pay following amounts:

(i) Rs. 2,00,000 7% Debentures (Rs. 100 each) in Wye Ltd. for the existing debentures in Zed Ltd.; for the purpose, each debenture of Wye Ltd. is to be treated as worth Rs. 105.

(ii) For each preference share in Zed Ltd. Rs. 10 in cash and one 9% preference share of Rs. 100 each in Wye Ltd.

(iii) For each equity share in Zed Ltd. Rs. 20 in cash and one equity share in Wye Ltd. of Rs. 100 each having the market value of Rs. 140.

(iv) Expense of liquidation of Zed Ltd. are to be reimbursed by Wye Ltd. to the extent of Rs. 10,000. Actual expenses amounted to Rs. 12,500.

Wye Ltd. valued Land and building at Rs. 5,50,000 Plant and Machinery at Rs. 6,50,000 and patents at Rs. 20,000 of Zed Ltd for the purpose of amalgamation.

Question 15 : Sun and Neptune

Sun and Neptune had been carrying on business independently. They agreed to amalgamate and form a new company Jupiter Ltd. with an authorised share capital of Rs. 4,00,000 divided into 80,000 equity shares of Rs. 5 each. On 31st March, 20X3 the respective information of Sun and Neptune were as follows:

	Sun (Rs.)	Neptune (Rs.)
Share capital	3,65,000	3,52,500
Current liabilities	5,97,000	1,80,250
Property, Plant and Equipment	6,35,000	3,65,000
Current assets	3,27,000	1,67,750

Additional Information:

(a) Revalued figures of non-current and Current assets were as follows:

	Sun (Rs.)	Neptune (Rs.)
Property, Plant and Equipment	7,10,000	3,90,000
Current Assets	2,99,500	1,57,750

(b) The debtors and creditors include ` 43,350 owed by Sun to Neptune.

The purchase consideration is satisfied by issue of the following shares and debentures.

(i) 60,000 equity shares of Jupiter Ltd. to Sun and Neptune in the proportion to the profitability of their respective business based on the average net profit during the last three years which were as follows:

	Sun (Rs.)	Neptune (Rs.)
20X1 Profit	4,49,576	2,73,900
20X2 (Loss)/Profit	(2,500)	3,42,100
20X3 Profit	3,77,924	3,59,000

(ii) 15% debenture in Jupiter Ltd. at par to provide an income equivalent to 8% return business as on capital employed in their respective business as on 31st March, 20X3 after revaluation of assets.

You are required to:

(1) Compute the amount of debentures and shares to be issued to Sun and Neptune.

(2) A Balance sheet of Jupiter Ltd. showing the position immediately after amalgamation.

Question 16 : X Ltd. and Y Ltd.

X Ltd. and Y Ltd. give the following information of assets, equity and liabilities as on 31st March, 2018:

Particulars	X Ltd. (Rs.)	Y Ltd. (Rs.)
Equity and Liabilities		
Equity Shares of Rs.10 each	30,00,000	9,00,000
9% Preference Shares of Rs.100 each	3,00,000	-
10% Preference Shares of Rs.100 each	-	3,00,000

General Reserve	2,10,000	2,10,000
Retirement Gratuity Fund (long term)	1,50,000	60,000
Trade Payables	3,90,000	2,40,000
Total	**40,50,000**	**17,10,000**
Assets		
Goodwill	1,50,000	75,000
Land & Buildings	9,00,000	3,00,000
Plant & Machinery	15,00,000	4,50,000
Inventories	7,50,000	5,25,000
Trade Receivables	6,00,000	3,00,000
Cash and Bank	1,50,000	60,000
Total	**40,50,000**	**17,10,000**

X Ltd. absorbs Y Ltd. on the following terms:

(i) 10% Preference Shareholders are to be paid at 10% premium by issue of 9% Preference Shares of X Ltd.

(ii) Goodwill of Y Ltd. on absorption is to be computed based on two times of average profits of preceding three financial years (2016-17 : Rs. 90,000; 2015-16 : Rs. 78,000 and 2014-15: Rs. 72,000). The profits of 2014 -15 included credit of an insurance claim of Rs. 25,000 (fire occurred in 2013-14 and loss by fire Rs. 30,000 was booked in Profit and Loss Account of that year). In the year 2015 -16, there was an embezzlement of cash by an employee amounting to Rs. 10,000.

(iii) Land & Buildings are valued at Rs. 5,00,000 and the Plant & Machinery at Rs.4,00,000.

(iv) Inventories are to be taken over at 10% less value and Provision for Doubtful Debts is to be created @ 2.5%.

(v) There was an unrecorded current asset in the books of Y Ltd. whose fair value amounted to Rs. 15,000 and such asset was also taken over by X Ltd.

(vi) The trade payables of Y Ltd. included Rs. 20,000 payable to X Ltd.

(vii) Equity Shareholders of Y Ltd. will be issued Equity Shares @ 5% premium.

You are required to:

(i) Prepare Realisation A/c in the books of Y Ltd.

(ii) Show journal entries in the books of X Ltd.

(iii) Prepare the Balance Sheet of X Ltd. after absorption as at 31st March,2018.

Question 17 : Tina Ltd.

On 1st April, 2018, Tina Ltd. take over the business of Rina Ltd. and discharged purchase consideration as follows:

(i) Issued 50,000 fully paid Equity shares of Rs. 10 each at a premium of Rs. 5 per share to the equity shareholders of Rina Ltd.

(ii) Cash payment of Rs. 50,000 was made to equity shareholders of Rina Ltd.

(iii) Issued 2,000 fully paid 12% Preference shares of Rs. 100 each at par to discharge the preference shareholders of Rina Ltd.

(iv) Debentures of Rina Ltd. (Rs. 1,20,000) will be converted into equal number and amount of 10% debentures of Tina Ltd.

Calculate the amount of Purchase consideration as per AS-14 and pass Journal Entry relating to discharge of purchase consideration in the books of Tina Ltd.

Question 18 : A Ltd.

The following is the summarized Balance Sheet of A Ltd. as at 31st March, 2019:

Liabilities	Rs.	Assets	Rs.
8,000 Equity shares of Rs.100 each	8,00,000	Building	3,40,000
10% Debentures	4,00,000	Machinery	6,40,000
Loans	1,60,000	Inventory	2,20,000
Trade payables	3,20,000	Trade receivables	2,60,000
General Reserve	80,000	Bank	1,36,000
		Patent	1,30,000
		Share issue Expenses	34,000
	17,60,000		**17,60,000**

B Ltd. agreed to absorb A Ltd. on the following terms and conditions:

(1) B Ltd. would take over all assets, except bank balance and Patent at their book values less 10%. Goodwill is to be valued at 4 year's purchase of super profits, assuming that the normal rate of return be 8% on the combined amount of share capital and general reserve.

(2) B Ltd. is to take over trade payables at book value.

(3) The purchase consideration is to be paid in cash to the extent of Rs.6,00,000 and the balance in fully paid equity shares of Rs.100 each at Rs.125 per share.

The average profit is Rs. 1,24,400. The liquidation expenses amounted to Rs. 16,000. B Ltd. sold prior to 31st March, 2018 goods costing Rs. 1,20,000 to A Ltd. for Rs. 1,60,000. Rs. 1,00,000 worth of goods are still in Inventory of A Ltd. on 31st March, 2018. Trade payables of A Ltd. include Rs. 40,000 still due to B Ltd.

Show the necessary Ledger Accounts to close the books of A Ltd. and prepare the Balance Sheet of B Ltd. as at 1st April, 2019 after the takeover.

2. MCQs :

1. In case of amalgamation, the entry for elimination of unrealized profit or loss on stock is made
   - (a) By the vendor company
   - (b) By the purchasing company
   - (c) By the third party
   - (d) By the court
2. If expenses of liquidation of the vendor company are paid by the purchasing company then, in purchasing company's book, the account debited is
   - (a) Goodwill account.
   - (b) Liquidation expense account.
   - (c) Vendor company account.
   - (d) General reserve.
3. Amalgamation adjustment reserve is opened in the books of the amalgamated company to incorporate
   - (a) Assets of the amalgamating company.
   - (b) Non- Statutory reserves of the amalgamating company.
   - (c) Statutory reserves of the amalgamating company.
   - (d) General reserve of the amalgamating company.
4. Amalgamation Adjustment Reserve is presented in the financial statements of the transferee company as
   - (a) Other current asset.
   - (b) Separate line item with a negative sign under the head 'Reserves and Surplus'.
   - (c) Other non-current assets.
   - (d) Investment of the company
5. A company into which the vendor company is merged is called
   - (a) Transferee company.
   - (b) Transferor company.
   - (c) Selling company.
   - (d) Acquiree company.
6. If the purchase consideration is more than net assets (at agreed values) of the transferor company, difference shall be recorded as ___________ in the books of the transferee company.
   - (a) Goodwill.
   - (b) Capital Reserve.
   - (c) Profit.
   - (d) Loss.

Thanks ....

Rahul Malkan

Chapter 32

CASH FLOW STATEMENTS

CHAPTER DESIGN

1. INTRODUCTION
2. ELEMENTS OF CASH
3. FORMAT OF CASH FLOWS

1. INTRODUCTION :

Cash Flow Statement is prepared to explain the cash movement between 2 point of times. It provides changes in cash and cash equivalent of an enterprise. It is classified into

1. Cash from trading Activities
2. Cash from Investing Activities and
3. Cash from Financing Activities

2. ELEMENTS OF CASH :

AS per AS 3, cash includes

1. Cash
2. Demand deposits with Bank
3. Cash Equivalent
   (a) Security with short term maturity period, say 3 months
   (b) Highly liquid and which are subject to an insignificant risk of changes in value

3. FORMAT OF CASH FLOWS :

	Particulars	Rs.	Total Rs.
1.	CASH FROM OPERATING ACTIVITY		
	Cash generated from operation	XX	
	(Direct Method or Indirect Method)		
	Less Income Tax Paid	(XX)	XX (1)
2.	CASH FROM INVESTING ACTIVITY		
	Sale of Fixed Assets / Investments	XX	
	Purchase of Fixed Assets / Investments	(XX)	
	Interest Received	XX	
	Dividend Received	XX	XX (2)
3.	CASH FROM FINANCING ACTIVITY		
	Issue of Shares	XX	
	Issue of Debentures	XX	
	Loans Taken	XX	
	Redemption of Preference Shares / Debentures	(XX)	
	Buy back of Shares	XX	
	Loans Repaid	XX	
	Interest Paid	(XX)	
	Dividend Paid	(XX)	XX (3)
4.	Net Cash or Equivalent Generated (1 + 2 + 3)		XX
5.	Add Opening Cash or Equivalent (Cash/Bank/Short Term Investments)		XX
6.	Closing Cash or Equivalent (Cash/Bank/Short Term Investments)		XX

Cash generated from Operations (Direct Method) :

Particulars	Rs.
Cash receipts From Sale of Goods	XX
Cash Receipts from Rendering Services	XX
Cash Payments to Suppliers of Goods	(XX)
Cash Paid to Employees	(XX)
Net Cash Generated from Operations	XX

Cash Generated from Operations (Indirect Method) :

	Particulars	Rs.	Total Rs.
	CASH FROM OPERATING ACTIVITY		
	Cash generated from operation		
1.	Closing Balance Profit and Loss A/c		XX
	Less Opening Balance of Profit and Loss A/c		XX
			XX
2.	Add Appropriations		
	Proposed Dividend	XX	
	Interim Dividend	XX	
	Transfer to Reserves	XX	XX
			XX
3.	Add Non Cash Non Operating Expenses		
	Depreciation on Fixed Assets	XX	
	Loss on sale of Assets	XX	
	Provision for Tax	XX	
	Amortisations (Goodwill w/o)	XX	XX
			XX
4.	Less Non Cash Non Operating Income		
	Profit on sale of Assets	XX	
	Interest Income	XX	
	Dividend Income	XX	XX
	Funds from Operations		XX
5.	Add Decrease in Working Capital (CA CL)		
	Decrease in Stock	XX	
	Decrease in Debtors	XX	

	Increase in Creditors	XX	XX
			XX
6.	Less Increase in Working Capital (CA CL)		
	Increase in Bills Receivable	XX	
	Increase in Prepaid Expenses	XX	
	Decrease in Bills Payable	XX	XX
	Cash From Operations		XX

PRACTICAL QUESTIONS :

Question 1 : AB Ltd.

From the following financial statements prepare Cash Flow Statement of AB Ltd for the year ended 31st Dec 2014.

Balance Sheet as on

Liabilities	31.03.13	31.03.14	Assets	31.03.13	31.03.14
Share Capital	1,35,000	1,40,000	Goodwill	13,950	4,950
Profit And Loss A/c	30,000	35,000	Land &	32,400	45,000
General Reserve	10,500	19,000	Building	1,13,400	85,050
Debentures	45,000	22,000	Plant &		40,500
Loans	67,950	62,010	Machinery		49,500
Creditors	71,650	43,940	Furniture	40,500	1,14,120
Proposed Dividend	13,500	16,200	Investments	94,500	
Provision for Taxation	10,800	12,600	Debtors	89,650	11,630
			Bank Balance		
Total	**3,84,400**	**3,50,750**	**Total**	**3,84,400**	**3,50,750**

Question 2 : Ryan Ltd.

The following data were provided by the accounting records of Ryan Ltd. at year-end, March 31, 2012:

Income Statement

		Rs.
Sales		6,98,000
Cost of Goods Sold		(5,20,000)
Gross Margin		1,78,000

Operating Expenses		
(including Depreciation Expense of Rs. 37,000)		(1,70,000)
		8,000
Other Income (Expenses)		
Dividend received	6,000	
Gain on Sale of Investments	12,000	
Loss on Sale of Plant	(3,000)	15,000
		23,000
Income tax		(7,000)
		16,000

Comparative Balance Sheets

Assets	31st March 12	31st March 11
Plants	7,15,000	5,05,000
Less: Accumulated Depreciation	(1,03,000)	-68,000
	6,12,000	4,37,000
Investments (Long term)	1,15,000	1,27,000
Current Assets :		
Inventory	1,44,000	1,10,000
Accounts Receivable	47,000	55,000
Cash	46,000	15,000
Prepaid Expenses	1,000	5,000
	9,65,000	7,49,000
Liabilities		
Share Capital	4,65,000	3,15,000
Reserves and Surplus	1,40,000	1,32,000
Bonds	2,95,000	2,45,000
Current Liabilities:		
Accounts Payable	50,000	43,000
Accrued Liabilities	12,000	9,000
Income Taxes Payable	3,000	5,000
	9,65,000	7,49,000

Analysis of selected accounts and transactions during 2011-2012

1. Purchased investments for Rs. 78,000.

2. Sold investments for Rs. 1,02,000. Theso investments cost Rs. 90,000.
3. Purchased plant assets for Rs. 1,20,000.
4. Sold plant assets that cost Rs. 10,000 with accumulated depreciation of Rs. 2,000 for Rs.5,000.
5. Issued Rs. 1,00,000 of bonds at face value in an exchange for plant assets on 31st March, 2012.
6. Repaid Rs. 50,000 of bonds at face value at maturity.
7. Issued 15,000 shares of Rs. 10 each.
8. Paid cash dividends Rs. 8,000.

Prepare Cash Flow Statement as per AS-3 (Revised), using indirect method.

Question 3 : Sun Ltd.

The balance sheets of Sun Ltd. as at 31st March 20X1 and 20X0 were as:

Particulars	Notes	20X1 Rs.	20X0 Rs.
Equity and Liabilities			
1 Shareholder's funds			
(a) Share capital	1	60,000	50,000
(b) Reserve & surplus	2	5,000	4,000
2 Current liabilities			
(a) Trade Payables		4,000	2,5000
(b) Other current liabilities	3	-	1,000
(c) Short term provision (provision for tax)		1,500	1,000
Total		**70,500**	**58,500**
Assets			
1 Non-current assets			
(a) Property, Plant & Equipment	4	39,500	29,000
2 Current assets			
(a) Current investments		2,000	1,000
(b) Inventories		17,000	14,000
(c) Trade receivables		8,000	6,000
(d) Cash & cash equivalents	5	4,000	8,500
		70,500	**58,500**

Notes to accounts :

		20X1 Rs.	20X0 Rs.
1	**Share Capital**		
	Equity Shares of Rs. 10 each	60,000	50,000
2	**Reserve & surplus**		
	Profit and Loss Account	5,000	4,000
3	**Other current liabilities**		
	Dividend Payable	-	1,000
4	**Property, plant and equipment (at WDV)**		
	Building	10,000	10,000
	Fixtures	17,000	11,000
	Vehicles	12,500	8,000
	Total	39,500	29,000
5	**Cash and cash equivalents**		
	Cash and Bank	4,000	8,500

The profit and loss statement for the year ended 31st March, 20X1 disclosed:

Particulars	Rs.
Profit before tax	4,500
Tax expense: Current tax	(1,500)
Profit for the year	3,000
Declared dividend	(2,000)
Retained Profit	1000

Further information is available :

	Fixtures Rs.	Vehicles Rs.
Depreciation for the year	1,000	2,500
Disposals		
Proceeds on disposal of vehicles	--	1,700
Written down value	--	(1,000)
Profit on disposal		700

Prepare a Cash Flow Statement for the year ended 31st March, 20X1.

Question 4 : More Ltd.

From the following details relating to the Accounts of Grow More Ltd. prepare Cash Flow Statement:

Liabilities	31.03.2012 (Rs.)	31.03.2011 (Rs.)
Share Capital	10,00,000	8,00,000
Reserve	2,00,000	1,50,000
Profit and Loss Account	1,00,000	60,000
Debentures	2,00,000	-
Provision for taxation	1,00,000	70,000
Proposed dividend	2,00,000	1,00,000
Sundry Creditors	7,00,000	8,20,000
	25,00,000	20,00,000
Assets		
Plant and Machinery	7,00,000	5,00,000
Land and Building	6,00,000	4,00,000
Investments	1,00,000	-
Sundry Debtors	5,00,000	7,00,000
Stock	4,00,000	2,00,000
Cash on hand / Bank	2,00,000	2,00,000
	25,00,000	**20,00,000**

(i) Depreciation @ 25% was charged on the opening value of Plant and Machinery,

(ii) During the year one old machine costing 50,000 (WDV 20,000) was sold for Rs.35,000.

(iii) Rs.50,000/- was paid towards income tax during the year.

(iv) Building under construction was not subject to any depreciation.

Prepare Cash flow Statement.

Question 5 : Danish Ltd.

The following are the summarized balance sheets of Danish Ltd. as on March 31, 2013 and 2014 :

Liabilities	As on 31.3.13	As on 31.3.14
	(Rs.)	**(Rs.)**
Equity share capital	10,00,000	12,50,000
Capital Reserve	-	10,000
General Reserve	2,50,000	3,00,000
Profit and Loss A/c	1,50,000	1,80,000

Long-term loan from the Bank	5,00,000	4,00,000
Sundry Creditors	5,00,000	4,00,000
Provision for Taxation	50,000	60,000
Proposed Dividends	1,00,000	1,25,000
	25,50,000	**27,25,000**
Assets		
Land and Building	5,00,000	4,80,000
Machinery	7,50,000	9,20,000
Investment	1,00,000	50,000
Stock	3,00,000	2,80,000
Sundry Debtors	4,00,000	4,20,000
Cash in Hand	2,00,000	1,65,000
Cash at Bank	3,00,000	4,10,000
	25,50,000	**27,25,000**

(i) Dividend of Rs.1,00,000 was paid during the year ended March 31, 2014.

(ii) Machinery during the year purchased for Rs.1,25,000.

(iii) Machinery of another company was purchased for a consideration of Rs.1,00,000 payable in equity shares.

(iv) Income-tax provided during the year Rs.55,000.

(v) Company sold some investment at a profit of Rs.10,000, which was credited to Capital reserve.

(vi) There was no sale of machinery during the year.

(vii) Depreciation written off on Land and Building Rs.20,000.

From the above particulars, prepare a cash flow statement for the year ended March, 2013 as per AS 3 (Indirect method).

Question 6 : Global Ltd.

The balance sheet of Global Ltd. as on 31st March, 2011 and 2012 are as under :

Liabilities	31.3. 11	31.3. 12	Assets	31.3. 11	31.3. 12
Share Capital			Fixed Assets:		
Equity	1,50,000	2,50,000	Goodwill	60,000	47,000
8% Redeemable Preference Share Capital	1,50,000	1,00,000	Land & Bldg.	1,00,000	75,000
Reserves & Surplus :			Plant & Mach.	90,000	1,91,000

General Reserves	20,000	30,000	Trade Invest.	10,000	35,000
Capital Reserves	-	25,000	Current Assets		
Profit & Loss A/c.	18,000	27,000	Loans & Advances		
Current Liab. & Provisions			Stock	85,000	78,000
Sundry Crs.	26,000	53,000	Sundry Drs.	60,000	90,000
Bills Payable	18,000	12,000	Bills Receivable	15,000	18,000
Prov. for Tax	28,000	32,000	Cash at Bank	10,000	22,000
Prop. Dividend	27,000	33,000	Cash in Hand	7,000	6,000
	4,37,000	**5,62,000**		**4,37,000**	**5,62,000**

The following further particulars are given :

i) In 2012 Rs.18,000 depreciation has been written off plant and machinery and no depreciation has been charged on Land & Bldg.

ii) A piece of land has been sold out and the balance has been revalued, profit on such sale and revaluation being transferred to capital Reserve. There is no other entry in capital reserve account. Profit on revaluation amounted to Rs. 12,500

iii) A plant was sold for Rs.12,000 (WDV Rs.15,000).

iv) Dividend received amounted to Rs.2,100 which includes pre acquisition dividend of Rs.600.

iv) An interim dividend of Rs.10,000 has been paid in 2012.

Prepare a statement of Cash Flow as per AS (3) for the year ended 31.3.2012.

Question 7 : JK Limited

The Balance Sheet of JK Limited as on 31st March, 2012 and 31st March, 2013 are given below Balance Sheet as on

Liabilities	31.03.12	31.03.13	Assets	31.03.12	31.03.13
Share Capital	1,440	1,920	Fixed Assets	3,840	4,560
Capital Reserve	-	48	Less : Depreciation	1,104	1,392
General Reserve	816	960		2,736	3,168
Profit and Loss A/c	288	360	Investment	480	384
9% Debentures	960	672	Cash	210	312
Current Liabilities	576	624	Other Current Assets		
Proposed Dividend	144	174	(including Stock)	1,134	1,272
Provision for Tax	432	408	Preliminary Exp.	96	48
Unpaid Dividend	-	18			

	4,656	5,184		4,656	5,84

Additional Information :

(i) During the year 2012-2013, Fixed Assets with a book values of Rs.2,40,000 (accumulated depreciation Rs.84,000) was sold for Rs.1,20,000

(ii) Provided Rs.4,20,000 as depreciation.

(iii) Some investment are sold at a profit of Rs.48,000 and Profit was credited to capital reserve.

(iv) It decided that stock be valued at cost, whereas previously the practice was to value stock at cost less 10 per cent. The stock was Rs.2, 59,200 as on 31.03.12. The stock as on 31.03.13 was correctly valued at Rs.3, 60,000.

(v) It decided to write off Fixed Assets costing Rs.60,000 on which depreciation amounting to Rs.48,000 has been provided.

(vi) Debentures are redeemed at Rs.105

Prepare a Cash Flow Statement.

Question 8 : X Limited

The following figures have been extracted from the Books of X Limited for the year ended on 31.3.2012. You are required to prepare a cash flow statement.

(i) Net profit before taking into account income tax and income from law suits but after taking into account the following items was Rs. 20 lakhs:

(a) Depreciation on Fixed Assets Rs. 5 lakhs.

(b) Discount on issue of Debentures written off Rs. 30,000.

(c) Interest on Debentures paid Rs. 3,50,000.

(d) Book value of investments Rs.3 lakhs (Sale of Investments for Rs.3,20,000).

(e) Interest received on investriients Rs. 60,000.

(f) Compensation received Rs. 90,000 by the company in a suit filed.

(ii) Income tax paid during the year Rs. 10,50,000.

(iii) 15,000, 10% preference shares of Rs. 100 each were redeemed on 31-3-2012 at a premium of 5%. Further the company issued 50,000 equity shares of Rs.10 each at a premium of 20% on 2.4.2011. Dividend on preference shares were paid at the time of redemption.

(iv) Dividends paid for the year 2010-2011 Rs. 5 lakhs and interim dividend paid Rs. 3 lakhs for the year 2011-2012.

(v) Land was purchased on 2.4.2011 for Rs. 2,40,000 for which the company issued 20,000 equity shares of Rs. 10 each at a premium of 20% to the land owner as consideration.

(vi) Current assets and current liabilities in the beginning and at the end of the years were as detailed below:

	As on 31.3.2011	As on 31.3.2012
	Rs.	Rs.
Stock	12,00,000	13,18,000
Sundry Debtors	2,08,000	2,13,100
Cash in hand	1,96,300	35,300
Bills receivable	50,000	40,000
Bills payable	45,000	40,000
Sundry Creditors	1,66,000	1,71,300
Outstanding expenses	75,000	81,800

Question 9 : Patiat Oils Limited

Patiat Oils Limited has collected the following information for the preparation of Cash Flow Statement for the year 2012.

	(Rs. in 000)
Net Profit after tax	25,000
Dividend (including CDT)	8,535
Provision for Tax	5,000
Tax paid	4,248
Loss on sale of assets	40
Book Value of assets sold	185
Depreciation	20,000
Amortisation of Capital Grants	6
Profit on sale of investments	100
Carrying amount of investments sold	27,765
Interest income on investments	2,506
Interest expenses	10,000
Interest paid	10,520
Increase in Working Capital (excluding Cash & Bank)	56,075
Purchase of Fixed Assets	14,560
Investments in joint Ventures	3,850
Expenditure on Construction in W-I-P.	34,740
Proceeds from calls in Arrears	2
Receipt of grant for capital projects	12
Proceeds from Long term borrowings	25,980
Proceeds from Short term borrowings	20,575
Opening balance of Cash and Bank	5,003

Closing balance of Cash and Bank	6,988

Required to prepare Cash Flow statement as per AS - 3 issued by ICAI.

Question 10 :

The Balance Sheets of a Company as on 31st March, 2008 and 2009 are given below:

Liabilities	31.3.08	31.3.09	Assets	31.3.08	31.3.09
	Rs.	Rs.		Rs.	Rs.
Equity Share Capital	14,40,00	19,20,00	Fixed Assets	38,40,000	45,60,000
Capital Reserve	-	48,000	Less: Depreciation	11,04,000	13,92,000
General Reserve	8,16,000	9,60,000		27,36,000	31,68,000
Profit & Loss A/c	2,88,000	3,60,000	Investment	4,80,000	3,84,000
9% debentures	9,60,000	6,72,000	Sundry Debtors	12,00,000	14,00,000
Sundry Creditors	5,50,000	5,90,000	Stock	1,40,000	1,84,000
Bills Payables	26,000	34,000	Cash in Hand	4,000	-
Proposed dividend	1,44,000	1,72,000	Preliminary Expenses		
Provision for Tax	4,32,000	4,08,000		96,000	48,000
Unpaid dividend	-	19,200			
	46,56,000	**51,84,000**		**46,56,000**	**51,84,000**

Additional Information:

During the year ended 31st March, 2009 the company.

(1) Sold a Machine for Rs. 1,20,000; the cost of machine was Rs. 2,40,000 and depreciation provided on it was Rs. 84,000.

(2) Provided Rs. 4,20,000 as depreciation on fixed assets.

(3) Sold some investment and profit credited to capital reserve.

(4) Redeemed 30% of the debentures @ 105.

(5) Decide to write off fixed assets costing Rs. 60,000 on which depreciation amounting to Rs 48,000 has been provided.

You are required to prepare cash flow statements as per AS – 3.

Question 11 : X Ltd.

From the following Summary Cash Account of X Ltd. Prepare Cash Flow Statement for the year ended 31st March, 2012 in accordance with AS 3 (Revised) using the direct method. The company does not have any cash equivalents.

Summary Cash Account for the year ended 31.3.2014

	Rs. '000		Rs. '000
Balance on 1.4.2013	50	Payment to Suppliers	2,000
Issue of Equity Shares	300	Purchase of Fixed Assets	200

Receipts from Customers	2,800	Overhead expenses	200
Sale of Fixed Assets	100	Wages and Salaries	100
		Taxation	250
		Dividend	50
		Repayment of Bank Loan	300
		Balance on 31.3.2014	150
	3,250		**3,250**

Question 12 : Raj Ltd.

Raj Ltd. gives you the following information for the year ended 31st March, 2014:

(i) Sales for the year Rs.48,00,000. The Company sold goods for cash only.

(ii) Cost of goods sold was 75% of sales.

(iii) Closing inventory was higher than opening inventory by Rs. 50,000

(iv) Trade creditors on 31.3.2012 exceed the outstanding on 31.3.2011 by Rs.1,00,000.

(v) Tax paid during the year amounts to Rs.1,50,000.

(vi) Amounts paid to Trade creditors during the year Rs.35,50,000.

(vi) Administrative and Selling expenses paid Rs.3,60,000.

(vii) One new machinery was acquired in December, 2006 for Rs.6,00,000.

(viii) Dividend paid during the year Rs.1,20,000.

(ix) Cash in hand and at Bank on 31.3.2012 Rs. 70,000.

(x) Cash in hand and at Bank on 1.4.2011 Rs. 50,000.

Prepare Cash Flow Statement for the year ended 31.3.2012 as per the prescribed Accounting standard.

Question 13 : Mr.Zen

From the following information of Mr. Zen, prepare a Cash flow statement as per AS-3 for the year ended 31.3.20X1:

Ledger Balances of Mr. Zen as of 20X0 and 20X1

	As on 1.4.20X0	As on 1.4.20X1
	Rs.	Rs.
Zen's Capital A/c	1000000	1224000
Trade payables	320000	352000
Mrs. Zen's loan	200000	--
Loan from Bank	320000	400000
Land	600000	880000
Plant and Machinery (net block)	640000	440000
Inventories	280000	200000

Trade receivables	240000	400000
Cash	80000	56000

A machine costing Rs 80,000 (accumulated depreciation there on Rs 24,000) was sold for Rs. 40,000. The provision for depreciation on 1.4.20X0 was Rs. 2,00,000 and 31.3.20X1 was Rs. 3,20,000. The net profit for the year ended on 31.3.20X1 was Rs. 3,60,000.

Question 14 : Gamma Ltd.

Prepare Cash flow for Gamma Ltd., for the year ending 31.3.20X1 from the following information:

(1) Sales for the year amounted to Rs. 135 crores out of which 60% was cash sales.

(2) Purchases for the year amounted to Rs. 55 crores out of which credit purchase was 80%.

(3) Administrative and selling expenses amounted to Rs. 18 crores and salary paid amounted to Rs. 22 crores.

(4) The Company redeemed debentures of Rs. 20 crores at a premium of 10%. Debenture holders were issued equity shares of Rs. 15 crores towards redemption and the balance was paid in cash. Debenture interest paid during the year was Rs. 1.5 crores.

(5) Dividend paid during the year amounted to Rs. 11.7 crores.

(6) Investment costing Rs. 12 crores were sold at a profit of Rs. 2.4 crores.

(7) Rs. 8 crores was paid towards income tax during the year.

(8) A new plant costing Rs. 21 crores was purchased in part exchange of an old plant. The book value of the old plant was Rs. 12 crores but the vendor took over the old plant at a value of Rs. 10 crores only. The balance was paid in cash to the vendor

(9) The following balances are also provided :

	Rs. in crores	Rs. in crores
	1.4.20X0	**31.3.20X1**
Debtors	45	50
Creditors	21	23
Bank	6	18.2

MCQs :

1. While preparing cash flow statement, conversion of debt to equity
   (a) Should be shown as a financing activity.
   (b) Should be shown as an investing activity.
   (c) Should not be shown as it is a non-cash transaction
   (d) Should not be shown as operating activity.
2. Which of the following would be considered a ‘cash-flow item from an “investing" activity’?

(a) Cash outflow to the government for payment of taxes.
(b) Cash outflow to purchase bonds issued by another company.
(c) Cash outflow to shareholders as dividends
(d) Cash outflow to make payment to trade payables.

3. All of the following would be included in a company's operating activities except:
(a) Income tax payments
(b) Collections from customers or Cash payments to suppliers
(c) Dividend payments
(d) Office and selling expenses.

4. Hari Uttam, a stock broking firm, received Rs. 1,50,000 as premium for forward contracts entered for purchase of equity shares. How will you classify this amount in the cash flow statement of the firm?
(a) Operating Activities. (b) Investing Activities.
(c) Financing Activities. (d) Non-cash transaction

5. As per AS 3 on Cash Flow Statements, cash received by a manufacturing company from sale of shares of ABC Company Ltd. should be classified as
(a) Operating activity. (b) Financing activity.
(c) Investing activity. (d) Non-cash transaction

Thanks ....

Chapter 33

BUY-BACK OF SECURITIES

CHAPTER DESIGN

1. PROVISION OF BUY BACK
2. PRACTICAL QUESTIONS
3. MCQ'S

1. PROVISIONS OF BUY BACK :

1. all the shares or other specified securities for buy-back are fully paid-up
2. The Companies Act, 2013 under Section 68 (1) permits companies to buy-back their own shares and other specified securities out of:
   (i) its free reserves; or
   (ii) the securities premium account; or
   (iii) the proceeds of the issue of any shares or other specified securities.
3. Section 69 (1) states that where a company purchases its own shares out of the free reserves or securities premium account, a sum equal to the nominal value of shares so purchased shall be transferred to the Capital Redemption Reserve Account and details of such account shall be disclosed in the Balance Sheet.
4. Premium (excess of buy-back price over the par value) paid on buy-back should be adjusted against free reserves and/or securities premium account. Revaluation reserve represents unrealized profit and hence it cannot be used for buy-back of securities.
5. Share Outstanding Test : The buy-back of shares in any financial year must not exceed 25% of its existing number.
6. Resource Test : The buy-back must be equal or less than twenty-five per cent of the total paid-up capital and free reserves of the company.
7. Debt-Equity Ratio Test : The ratio of the debt owed by the company (both secured and unsecured) after such buy-back is not more than twice the total of its paid-up capital and its free reserves.

2. PRACTICAL QUESTIONS :

Question 1 : M Ltd.

M Ltd. furnishes the following Balance Sheet as at 31st March, 20X1:

Particulars	Notes	Rs (000's)
Equity and Liabilities :		
1. Shareholders' funds		
A. Share capital	1	5,000
B. Reserves and Surplus	2	6,310
2. Non Current Liabilities		
A. Long Term Borrowings	3	400
3. Current Liabilities		
A. Trade Payables		40
Total		**11,750**
Assets :		
1. Non Current Asset		

A. Property Plant and Equipment	4	2,750
B. Non Current Investments		5,000
2. Current Assets		
A. Inventories		1,000
B. Trade Receivables		2,000
C. Cash and Cash Equivalents		1,000
Total		**11,750**

Notes to Accounts :

Sr. No.	Particulars	Rs in (000's)
1	**Share Capital :**	
	Authorized, Issued and Subscribed Capital:	
	3,00,000 Equity shares of Rs 10 each fully paid up	3,000
	20,000 9% Preference Shares of 100 each	2,000
	Total	**5,000**
2	**Reserves and Surplus :**	
	Capital Reserve	10
	Revenue reserve	4,000
	Securities premium	500
	Profit and Loss account	1,800
	Total	**6,310**
3	**Long term borrowings :**	
	10% Debentures	400
4	**Property, Plant and Equipment (PPE) PPE :**	
	Cost	3,000
	Less: Provision for depreciation	(250)
	Net carrying value	2,750

The company passed a resolution to buy-back 20% of its equity capital @ Rs 15 per share. For this purpose, it sold its investments of Rs 30 lakhs for Rs 25 lakhs.

You are required to pass necessary Journal entries.

Question 2 :Anu Ltd.

Anu Ltd. (a non-listed company) furnishes you with the following balance sheet as at 31st March, 20X1:

Particulars	Notes	Rs (crores's)
Equity and Liabilities		
1. Shareholders' funds		

	A. Share capital	1	100
	B. Reserves and Surplus	2	200
2.	Current Liabilities		
	A. Trade Payables		40
Total			**440**
Assets			
1.	Non Current Asset		
	A. Property Plant and Equipment	3	-
	B. Non Current Investments		100
2.	Current Assets		
	A. Trade Receivables		140
	B. Cash and Cash Equivalents		200
Total			**440**

Notes to Accounts :

Sr No.	Particulars	Rs in (000's)
1	**Share Capital :**	
	Authorized, Issued and Subscribed Capital:	
	Equity shares of Rs 10 each fully paid up	75
	12% Preference Shares of 100 each	25
	Total	100
2	**Reserves and Surplus :**	
	Capital Reserve	15
	Revenue reserve	260
	Securities premium	25
	Total	300
3	**Property, Plant and Equipment (PPE) PPE:**	
	Cost	100
	Less: Provision for depreciation	100
	Net carrying value	Nil
4	**Non current Investments :**	
	Non-current investments at cost (Market value Rs 400 Cr.)	100

The company redeemed preference shares on 1st April, 20X1. It also bought back 50 lakhs equity shares of Rs 10 each at Rs 50 per share. The payments for the above were made out of the huge bank balances, which appeared as a part of current assets.

You are asked to:

1) Pass journal entries to record the above.

2) Prepare balance sheet as at 1.4.20X1.

Question 3 : Dee Limited

Dee Limited (a non-listed company) furnishes the following Balance Sheet as at 31st March, 20X1:

Particulars	Notes	Rs (000's)
Equity and Liabilities		
1. Shareholders' funds		
A. Share capital	1	2,700
B. Reserves and Surplus	2	9,700
2. Current Liabilities		
A. Trade Payables		1,400
Total		13,800
Assets		
1. Non Current Asset		
A. Property Plant and Equipment		9,300
B. Non Current Investments		3,000
2. Current Assets		
A. Inventories		500
B. Trade Receivables		200
C. Cash and Cash Equivalents		800
Total		13,800

Notes to Accounts :

Sr. No.	Particulars	Rs in (000's)
1	Share Capital	
	Authorized, Issued and Subscribed Capital:	
	2,50,000 Equity shares of Rs 10 each fully paid up	2500
	2,000, 10% Preference Shares of 100 each	200
	(Issued two months back for the purpose of buy-back)	
	Total	2,700
2	Reserves and Surplus	
	Capital Reserve	1,000
	Revenue reserve	3,000
	Securities premium	2,200
	Profit and Loss Account	2,500
	Total	9,700

The company passed a resolution to buy-back 20% of its equity capital @ Rs 50 per share. For this purpose, it sold all of its investment for Rs 22,00,000.

You are required to pass necessary journal entries and prepare the Balance Sheet.

Question 4 : Extra Ltd.

Extra Ltd. (a non-listed company) furnishes you with the following Balance Sheet as at 31st March, 20X1:

Particulars	Notes	Rs (lakhs's)
Equity and Liabilities		
1. Shareholders' funds		
A. Share capital	1	120
B. Reserves and Surplus	2	118
2. Non Current Liabilities		
A. Long Term Borrowings	3	4
3. Current Liabilities		
A. Trade Payables		70
Total		312
Assets		
1. Non Current Asset		
A. Property Plant and Equipment	4	50
B. Non Current Investments		120
2. Current Assets		
A. Cash and Cash Equivalents		142
Total		312

Notes to Accounts :

Sr.No.	Particulars	Rs in (000's)
1	Share Capital	
	Authorized, Issued and Subscribed Capital:	
	Equity shares of Rs 10 each fully paid up	100
	9% Preference Shares of 100 each	20
	Total	120
2	Reserves and Surplus	
	Capital Reserve	8
	Revenue reserve	50
	Securities premium	60
	Total	118
3	Long term borrowings	
	10% Debentures	4

1. The company redeemed the preference shares at a premium of 10% on 1st April, 20X1.
2. It also bought back 3 lakhs equity shares of Rs 10 each at Rs 30 per share. The payment for the above was made out of huge bank balances.
3. Included in its investment were "investments in own debentures" costing Rs 2 lakhs (face value Rs 2.20 lakhs). These debentures were cancelled on 1st April, 20X1.
4. The company had 1,00,000 equity stock options outstanding on the above-mentioned date, to the employees at Rs 20 when the market price was Rs 30 (This was included under current liabilities) On 1.04.20X1 employees exercised their options for 50,000 shares.

Pass the journal entries to record the above.

Prepare Balance Sheet as at 01.04.20X1.

Question 5 : KG Limited

KG Limited furnishes the following Balance Sheet as at 31st March, 20X1:

Particulars	Notes	Rs (000's)
Equity and Liabilities		
1. Shareholders' funds		
A. Share capital	1	1200
B. Reserves and Surplus	2	810
2. Non Current Liabilities		
A. Long Term Borrowings	3	750
3. Current Liabilities		
A. Trade Payables		745
B. Other Current Liability		195
Total		3700
Assets		
1. Non Current Asset		
A. Property Plant and Equipment	4	2026
B. Non Current Investments		74
2. Current Assets		
A. Inventories		600
B. Trade Receivables		260
C. Cash and Cash Equivalents		740
Total		3700

Notes to Accounts :

Sr No.	Particulars	Rs in (000's)
1	Share Capital	
	Authorized, Issued and Subscribed Capital:	
	3,00,000 Equity shares of Rs 10 each fully paid up	1200
2	Reserves and Surplus	
	General Reserve	175
	Securities premium	265
	Capital Redemption Reserve	200
	Profit and Loss account	170
	Total	810
3	Long term borrowings	
	12% Debentures	750
4	Property, Plant and Equipment (PPE) PPE:	
	Land and Building	1800
	Plant and Machinery	226
		2,026

On 1st April, 20X1, the company announced the buy-back of 25% of its equity shares @ Rs 15 per share. For this purpose, it sold all of its investments for Rs 75 lakhs.

On 5th April, 20X1, the company achieved the target of buy-back. On 30th April, 20X1 the company issued one fully paid up equity share of Rs 10 by way of bonus for every four equity shares held by the equity shareholders.

You are required to:

(1) Pass necessary journal entries for the above transactions.

(2) Prepare Balance Sheet of KG Limited after bonus issue of the shares.

Question 6 : Competent Limited

Following is the Balance Sheet of Competent Limited as at 31st March, 20X1:

Particulars	Notes	Rs (000's)
Equity and Liabilities		
1. Shareholders' funds		
A. Share capital	1	12,50,000
B. Reserves and Surplus	2	18,75,000
2. Non Current Liabilities		
A. Long Term Borrowings	3	18,75,000
3. Current Liabilities		
A. Trade Payables		-

B. Other Current Liability		16,50,000
Total		76,50,000
Assets		
1. Non Current Asset		
A. Property Plant and Equipment	4	46,50,000
B. Non Current Investments		
2. Current Assets		
A. Other current Assets		30,00,000
Total		76,50,000

Notes to Accounts :

Sr. No.	Particulars	Rs in (000's)
1	Share Capital	
	Authorized, Issued and Subscribed Capital:	
	Equity shares of Rs 10 each fully paid up	12,50,000
2	Reserves and Surplus	
	Securities premium	2,50,000
	Profit and Loss account	1,25,000
	Revenue Reserve	15,00,000
	Total	18,75,000
3	Long term borrowings	
	14% Debentures	18,75,000
	Unsecured Loan	10,00,000
		28,75,000
4	Property, Plant and Equipment (PPE) PPE:	
	Land and Building	19,30,000
	Plant and Machinery	18,00,000
	Furniture and fitting	9,20,000
		46,50,000

The company wants to buy-back 25,000 equity shares of Rs 10 each, on 1st April, 20X1 at Rs 20 per share. Buy-back of shares is duly authorized by its articles and necessary resolution has been passed by the company towards this. The payment for buy-back of shares will be made by the company out of sufficient bank balance available shown as part of Current Assets.

Comment with your calculations, whether buy-back of shares by company is within the provisions of the Companies Act, 2013. If yes, pass necessary journal entries towards buy-back of shares and prepare the Balance Sheet after buy-back of shares.

Question 7 : Pratham Ltd.

Pratham Ltd. (a non-listed company) has the following Capital structure as on 31st March, 20X1:

Particulars	Rs .	Rs .
Equity Share Capital (shares of Rs 10 each fully paid)		30,00,000
Reserves & Surplus		
General Reserve	32,50,000	
Security Premium Account	6,00,000	
Profit & Loss Account	4,30,000	
Revaluation Reserve	6,20,000	49,00,000
Loan Funds		42,00,000

You are required to compute by Debt Equity Ratio Test, the maximum number of shares that can be bought back in the light of above information, when the offer price for buy-back is Rs 30 per share.

Question 8 : Perrotte Ltd.

Perrotte Ltd. (a non-listed company) has the following Capital Structure as on 31.03.20X1:

	Particulars	Rs in crores	Rs in crores
1.	Equity Share Capital (shares of Rs 10 each fully paid)		330
2.	Reserves & Surplus		
	General Reserve	240	
	Security Premium Account	90	
	Profit & Loss Account	90	
	Infrastructure Development Reserve	180	600
3.	Loan Funds		1,800

The Shareholders of Perrotte Ltd., on the recommendation of their Board of Directors, have approved on 12.09.20X1 a proposal to buy-back the maximum permissible number of Equity shares considering the large surplus funds available at the disposal of the company.

The prevailing market value of the company's shares is Rs 25 per share and in order to induce the existing shareholders to offer their shares for buy-back, it was decided to offer a price of 20% over market.

You are also informed that the Infrastructure Development Reserve is created to satisfy Income-tax Act requirements.

You are required to compute the maximum number of shares that can be bought back in the light of the above information and also under a situation where the loan funds of the company were either Rs 1,200 crores or Rs 1,500 crores.

Assuming that the entire buy-back is completed by 09.12.20X1, show the accounting entries in the company's books in each situation.

Question 9 : SMM Ltd.

SMM Ltd. has the following capital structure as on 31st March, 20X1:

Particulars		Situation 1	Situation 2
1.	Equity Share Capital (shares of Rs 10 each fully paid)	1200	1200
2.	Reserves & Surplus		
	General Reserve	1080	1080
	Security Premium Account	400	400
	Profit & Loss Account	200	200
	Infrastructure Development Reserve	320	320
3.	Loan Funds	3200	6000

The company has offered buy-back price of Rs 30 per equity share. You are required to calculate maximum permissible number of equity shares that can be bought back in both situations and also required to pass necessary Journal Entries.

3. MCQs :

1. As per section 68(1) of the Companies Act, buy-back of own shares by the company, shall not exceed
   (a) 25% of the total paid-up capital and free reserves of the company.
   (b) 20% of the total paid-up capital and free reserves of the company.
   (c) 15% of the total paid-up capital and free reserves of the company.
   (d) 10% of the total paid-up capital and free reserves of the company.
2. The companies are permitted to buy-back their own shares out of
   (a) Free reserves and Securities premium
   (b) Proceeds of the issue of any shares.
   (c) Both (a) and (b)
   (d) Neither (a) nor (b).
3. When a company purchases its own shares out of free reserves; a sum equal to nominal value of shares so purchased shall be transferred to
   (a) Revenue redemption reserve.
   (b) Capital redemption reserve.
   (c) Buy-back reserve
   (d) Special reserve

4. State which of the following statements is true?
   (a) Buy-back is for more than twenty-five per cent of the total paid-up capital and free reserves of the company.
   (b) Partly paid shares cannot be bought back by a company.
   (c) Buy-back of equity shares in any financial year shall exceed twenty-five per cent of its total paid-up equity capital in that financial year.
   (d) Partly paid shares can be bought back by a company.
5. Premium (excess of buy-back price over the par value) paid on buy-back should be adjusted against
   (a) Free reserves.
   (b) Securities premium.
   (c) Both (a) and (b).
   (d) Neither (a) nor (b).
6. Advantages of Buy-back of shares include to
   (a) Encourage others to make hostile bid to take over the company.
   (b) Decrease promoters holding as the shares which are bought back are cancelled.
   (c) Discourage others to make hostile bid to take over the company as the buy-back will increase the promoters holding.
   (d) All of the above.

Thanks ....

Chapter 34

INTERNAL RECONSTRUCTION

CHAPTER DESIGN

1. PRACTICAL QUESTIONS
2. MCQ'S
3. THEORETICAL QUESTIONS
4. EXTRA QUESTIONS

1. PRACTICAL QUESTIONS :

Question 1 : B Ltd.

On 31-12-20X1, B Ltd. had 20,000, Rs. 10 Equity Shares as authorized capital and the shares were all issued on which Rs. 8 was paid up. In June, 20X2 the company in general meeting decided to sub-divide each share into two shares of Rs. 5 with Rs. 4 paid up. In June, 20X3 the company in general meeting resolved to consolidate 20 shares of Rs. 5, Rs. 4 per share paid up into one share of Rs. 100 each, Rs. 80 paid up. Pass entries and show how share capital will appear in notes to Balance Sheet as on 31-12-20X1, 31-12-20X2 and 31-12-20X3.

Question 2 : C Ltd.

C Ltd. had Rs. 5,00,000 authorized capital on 31-12-20X1 divided into shares of Rs. 100 each out of which 4,000 shares were issued and fully paid up. In June 20X2 the Company decided to convert the issued shares into stock. But in June, 20X3 the Company re-converted the stock into shares of Rs. 10 each, fully paid up. Pass entries and show how Share Capital will appear in Notes to Balance Sheet as on 31-12-20X1, 31-12-20X2 and 31-12-20X3.

Question 3 : A & Co. Ltd.

The Balance Sheet of A & Co. Ltd. as at 31-3-20X2 is as follows:

		Particulars	Notes	Rs.
		Equity and Liabilities		
1		**Shareholders' funds**		
	A	Share capital	1	11,50,000
	B	Reserves and Surplus	2	(5,35,000)
2		**Non-current liabilities**		
	A	Long-term borrowings	3	3,75,000
3		**Current liabilities**		
	A	Trade Payables		3,00,000
	B	Short term borrowings - Bank Overdraft		1,95,000
	C	Other current liabilities	4	1,22,500
		Total		16,07,500
		Assets		
1		**Non-current assets**		
	A	Property, plant and equipment	5	4,75,000
	B	Intangible assets	6	1,67,500

	C	Non-current investments	7	55,000
2		**Current assets**		
	A	Inventories		4,25,000
	B	Trade receivables		4,85,000
		Total		16,07,500

Notes to accounts :

		Rs.
1	**Share Capital**	
	Equity share capital:	
	75,000 Equity Shares of Rs. 10 each	7,50,000
	Preference share capital:	
	4,000 6% Cumulative Preference Shares of Rs. 100 each	4,00,000
		11,50,000
2	**Reserves and Surplus**	
	Debit balance of Profit and loss Account	(5,35,000)
		(5,35,000)
3	**Long-term borrowings**	
	Secured	
	6% Debentures (secured on the freehold property)	3,75,000
		3,75,000
4	**Other current liabilities**	
	Loan from directors	1,00,000
	Interest payable on 6% debentures	22,500
		1,22,500
5	**Property plant and Equipment**	
	Freehold property	4,25,000
	Plant	50,000
		4,75,000
6	**Intangible assets**	
	Goodwill	1,30,000
	Patents	37,500
		1,67,500
7	**Non-current investments**	
	Investments at cost	55,000
		55,000

The Court approved a Scheme of re-organization to take effect on 1-4-20X2, whereby:

(i) The Preference shares to be written down to Rs. 75 each and Equity Shares to Rs. 2 each.

(ii) Of the Preference Share dividends which are in arrears for four years, three fourths to be waived and Equity Shares of Rs. 2 each to be allotted for the remaining quarter.

(iii) Interest payable on debentures to be paid in cash.

(iv) Debenture-holders agreed to take over freehold property, book value Rs. 1,00,000 at a valuation of Rs. 1,20,000 in part repayment of their holdings and to provide additional cash of Rs. 1,30,000 secured by a floating charge on company's assets at an interest rate of 8% p.a.

(v) Patents and Goodwill to be written off.

(vi) Inventory to be written off by Rs. 65,000.

(vii) Amount of Rs. 68,500 to be provided for bad debts.

(viii) Remaining freehold property after giving to debenture holders, to be revalued at Rs. 3,87,500.

(ix) Investments be sold for Rs. 1,40,000.

(x) Directors to accept settlement of their loans as to 90% thereof by allotment of equity shares of Rs. 2 each and as to 5% in cash, and balance 5% being waived.

(xi) There were capital commitments totalling Rs. 2,50,000. These contracts are to be cancelled on payment of 5% of the contract price as a penalty.

(xii) Ignore taxation and cost of the scheme.

You are requested to show Journal entries reflecting the above transactions (including cash transactions) and prepare the Balance Sheet of the company after completion of the Scheme.

Question 4 : Rebuilt Ltd.

Given below is the Balance sheet of Rebuilt Ltd. as at 31.3.20X1:

		Particulars	Notes	Rs.
		Equity and Liabilities		
1		**Shareholders' funds**		
	A	Share capital	1	13,50,000
	B	Reserves and Surplus	2	(4,51,000)
2		**Non-current liabilities**		
	A	Long-term borrowings (Loan)	3	5,73,000
3		**Current liabilities**		
	A	Trade Payables		2,07,000
	B	Other current liabilities		35,000
		Total		17,14,000

		Assets		
1		**Non-current assets**		
	A	Property, plant and equipment	4	6,68,000
	B	Intangible assets	5	3,18,000
2		**Current assets**		
	A	Inventories		4,00,000
	B	Trade receivables		3,28,000
		Total		17,14,000

Notes to account :

		Rs.
1	**Share Capital**	
	Equity share capital	7,50,000
	15,000 Equity Shares of Rs. 50 each	
	Preference share capital	
	12,000, 7% Cumulative Preference Shares of Rs. 50 each	
	(Preference dividend is in arrears for five years)	6,00,000
	Total	13,50,000
2	**Reserves and Surplus**	
	Debit balance of Profit and loss Account	(4,51,000)
		(4,51,000)
3	**Long-term borrowings**	
	Loan	5,73,000
		5,73,000
4	**Property, plant and Equipment**	
	Building at cost less depreciation	4,00,000
	Plant at cost less depreciation	2,68,000
		6,68,000
5	**Intangible Assets**	
	Trademarks and Goodwill at cost	3,18,000
		3,18,000

The Company is not earning profits, short of working capital and a scheme of reconstruction has been approved by both the classes of shareholders. A summary of the scheme is as follows:

(a) The equity shareholders have agreed that their Rs. 50 shares should be reduced to Rs. 2.50 by cancellation of Rs. 47.50 per share. They have also agreed to subscribe for three new equity shares of Rs. 2.50 each for each equity share held.

(b) The preference shareholders have agreed to cancel the arrears of dividends and to accept for each Rs. 50 share, 4 new 5% preference shares of Rs. 10 each, plus 6 new equity shares of Rs. 2.50 each, all credited as fully paid.

(c) Lenders to the company for Rs. 1,50,000 have agreed to convert their loan into share and for this purpose they will be allotted 12,000 new preference shares of Rs. 10 each and 12,000 new equity shares of Rs. 2.50 each.

(d) The directors have agreed to subscribe in cash for 40,000, new equity shares of Rs. 2.50 each in addition to any shares to be subscribed by them under (a) above.

(e) Of the cash received by the issue of new shares, Rs. 2,00,000 is to be used to reduce the loan due by the company.

(f) The equity share capital cancelled is to be applied:

i. to write off the debit balance in the profit and loss A/c; and

ii. to write off Rs. 35,000 from the value of plant.

Any balance remaining is to be used to write down the value of trademarks and goodwill. Show by journal entries how the financial books are affected by the scheme and prepare the balance sheet of the company after reconstruction. The nominal capital as reduced is to be increased to Rs. 6,50,000 for preference share capital and Rs. 7,50,000 for equity share capital.

Question 5 : Vaibhav Ltd.

Vaibhav Ltd. gives the following ledger balances as at 31st March 20X1:

	Rs.
Property, Plant and Equipment	2,50,00,000
Investments (Market-value Rs. 19,00,000)	20,00,000
Current Assets	2,00,00,000
P & L A/c (Dr. balance)	12,00,000
Share Capital: Equity Shares of Rs. 100 each	2,00,00,000
6%, Cumulative Preference Shares of Rs. 100 each	1,00,00,000
5% Debentures of Rs. 100 each	80,00,000
Creditors	1,00,00,000
Provision for taxation	2,00,000

The following scheme of Internal Reconstruction is sanctioned:

(i) All the existing equity shares are reduced to Rs. 40 each.

(ii) All preference shares are reduced to Rs. 60 each.

(iii) The rate of Interest on Debentures increased to 6%. The Debenture holders surrender their existing debentures of Rs. 100 each and exchange the same for fresh debentures of Rs. 70 each for every debenture held by them.

(iv) Property, Plant and Equipment is to be written down by 20%.

(v) Current assets are to be revalued at Rs. 90,00,000.

(vi) Investments are to be brought to their market value.

(vii) One of the creditors of the company to whom the company owes Rs. 40,00,000 decides to forgo 40% of his claim. The creditor is allotted with 60000 equity shares of Rs. 40 each in full and final settlement of his claim.

(viii) The taxation liability is to be settled at Rs. 3,00,000.

(ix) It is decided to write off the debit balance of Profit & Loss A/c.

Pass journal entries and show the Balance Sheet of the company after giving effect to the above.

Question 6

Following is the Balance Sheet of ABC Ltd. as at 31st March, 20X1:

		Particulars	Notes	Rs.
		Equity and Liabilities		
1		**Shareholders' funds**		
	A	Share Capital	1	26,00,000
	B	Reserves and Surplus	2	(4,05,000)
2		**Non-current liabilities**		
	A	**Long-term borrowings**	3	12,00,000
3		**Current liabilities**		
	A	Trade Payables		5,92,000
	B	Short term borrowings - Bank overdraft		1,50,000
		Total		41,37,000
		Assets		
1		**Non-current assets**		
	A	Property, plant and equipment	4	11,50,000
	B	Intangible assets	5	70,000
	C	Non-current investment	6	68,000
2		**Current assets**		
	A	Inventory		14,00,000
	B	Trade receivables		14,39,000
	C	Cash and cash equivalents		10,000
		Total		41,37,000

Notes to accounts :

		Rs.
1	**Share Capital**	

	Equity share capital:	20,00,000
	2,00,000 Equity Shares of Rs 10 each	6,00,000
	6,000, 8% Preference shares of Rs. 100 each	26,00,000
2	**Reserves and Surplus**	
	Debit balance of Profit and loss A/c	(4,05,000)
		(4,05,000)
3	**Long-term borrowings**	
	9% debentures	12,00,000
		12,00,000
4	**Property, Plant and Equipment**	
	Plant and machinery	9,00,000
	Furniture and fixtures	2,50,000
		11,50,000
5	**Intangible assets**	
	Patents and copyrights	70,000
		70,000
6	**Non-current investments**	
	Investments (market value of Rs. 55,000)	68,000
		68,000

The following scheme of reconstruction was finalized:

(i) Preference shareholders would give up 30% of their capital in exchange for allotment of 11% Debentures to them.

(ii) Debenture holders having charge on plant and machinery would accept plant and machinery in full settlement of their dues.

(iii) Inventory equal to Rs. 5,00,000 in book value will be taken over by trade payables in full settlement of their dues.

(iv) Investment value to be reduced to market price.

(v) The company would issue 11% Debentures for Rs. 3,00,000 and augment its working capital requirement after settlement of bank overdraft.

Pass necessary Journal Entries in the books of the company. Prepare Capital Reduction account and Balance Sheet of the company after internal reconstruction.

Question 7 : Revise Limited

The Balance Sheet of Revise Limited as at 31st March, 20X1 was as follows :

		Particulars	Notes	Rs.
		Equity and Liabilities		
1		**Shareholders' funds**		

	A	Share capital	1	10,00,000
	B	Reserves and surplus	2	(6,00,000)
2		**Non-current liabilities**		
	A	Long-term borrowings	3	2,00,000
3		**Current liabilities**		
	A	Trade Payables		72,000
	B	Other current liabilities	4	24,000
	C	Short term provisions	5	24,000
				7,20,000
		Assets		
1		**Non-current assets**		
	A	Property, Plant and Equipment	6	1,00,000
2		**Current assets**		
	A	Inventory		3,20,000
	B	Trade receivables		2,70,000
	C	Cash and cash equivalents		30,000
		Total		7,20,000

Notes to accounts :

			Rs.
1	**Share Capital**		
	Equity share capital		
	10,000 Equity Shares of Rs. 100 each		10,00,000
			10,00,000
2	**Reserves and Surplus**		
	Debit balance of Profit and loss Account		(6,00,000)
			(6,00,000)
3	**Long-term borrowings**		
	12% debentures		2,00,000
			2,00,000
4	**Other current liabilities**		
	Interest payable on debentures		24,000
			24,000
5	**Property, Plant and Equipment**		
	Machinery		1,00,000
			1,00,000

It was decided to reconstruct the company for which necessary resolution was passed and sanctions were obtained from appropriate authorities. Accordingly, it was decided that:

(a) Each share is sub-divided into ten fully paid up equity shares of Rs. 10 each.

(b) After sub-division, each shareholder shall surrender to the company 50% of his holding, for the purpose of re-issue to debenture holders and trade payables as necessary.

(c) Out of shares surrendered, 10,000 shares of Rs. 10 each shall be converted into 12% preference shares of Rs. 10 each, fully paid up.

(d) The claims of the debenture-holders shall be reduced by 75 per cent. In consideration of the reduction, the debenture holders shall receive preference shares of Rs. 1,00,000 which are converted out of shares surrendered.

(e) Trade payables claim shall be reduced to 50 per cent, it is to be settled by the issue of equity shares of Rs. 10 each out of shares surrendered.

(f) Balance of profit and loss account to be written off.

(g) The shares surrendered and not re-issued shall be cancelled.

You are required to show the journal entries giving effect to the above and the resultant Balance Sheet

Question 8 : Recover Ltd.

Recover Ltd. decided to reorganize its capital structure owing to accumulated losses and adverse market condition. The Balance Sheet of the company as on 31st March 20X1 is as follows

		Particulars	Notes	Rs.
		Equity and Liabilities		
1		**Shareholders' funds**		
	A	Share capital	1	3,50,000
	B	Reserves and surplus	2	(70,000)
2		**Non-current liabilities**		
		Long-term borrowings	3	50,000
3		**Current liabilities**		
	A	Trade Payables		80,000
	B	Short term Borrowings – Bank overdraft		90,000
	C	Other Current Liabilities (Interest payable on Debentures)		5,000
				5,05,000
		Assets		
1		**Non-current assets**		

	A	Property, Plant Equipment	4	
	B	Intangible assets	5	
	C	Non-current investments	6	
2		**Current assets**		
	A	Inventories		30,000
	B	Trade receivables		50,000
				5,05,000

Notes to accounts :

			Rs.
1	**Share Capital**		
	Equity share capital:		
	20,000 Equity Shares of Rs. 10 each		2,00,000
	Preference share capital:		
	15,000 8% Cumulative Preference Shares of Rs. 10 each (preference dividend has been in arrears for 4 years)		1,50,000
			3,50,000
2	**Reserves and surplus**		
	Profit and loss account (debit balance)		(70,000)
			(70,000)
3	**Long-term borrowings**		
	Secured		
	(10% Debentures (secured on the freehold property)		50,000
			50,000
4	**Property, Plant and Equipment**		
	Freehold property		1,20,000
	Leasehold property		85,000
	Plant and machinery		1,30,000
			3,35,000
5	**Intangible assets**		
	Goodwill		50,000
			50,000
6	**Non-current investments**		
	Non-Trade investments at cost		40,000
			40,000

Subsequent to approval by court of a scheme for the reduction of capital, the following steps were taken:

(i) The preference shares were reduced to Rs. 2.5 per share, and the equity shares to Rs. 1 per share.

(ii) One new equity share of Rs. 1 was issued for the arrears of preferred dividend for past 4 years.

(iii) The debenture holders took over the freehold property at an agreed figure of Rs. 75,000 and paid the balance to the company after deducting the amount due to them.

(iv) Plant and Machinery was written down to Rs. 1,00,000.

(v) Non-trade Investments were sold for Rs. 32,000.

(vi) Goodwill and obsolete stock (included in the value of inventories) of Rs. 10,000 were written off.

(vii) A contingent liability of which no provision had been made was settled at Rs. 7,000 and of this amount, Rs. 6,300 was recovered from the insurance

You are required (a) to show the Journal Entries, necessary to record the above transactions in the company's books and (b) to prepare the Balance Sheet, after completion of the scheme.

2. MCQs :

1. When the object of reconstruction is usually to re-organise capital or to compound with creditors or to effect economies then such type of reconstruction is called
   (a) Internal reconstruction with liquidation
   (b) Internal reconstruction without liquidation of the company
   (c) External reconstruction
   (d) None of the above.
2. The accumulated losses under scheme of internal reconstruction are written off against
   (a) Capital Reduction account
   (b) Share Capital account
   (c) Shareholders' account
   (d) Reserve and surplus
3. A process of reconstruction, which is carried out without liquidating the company and forming a new one is called
   (a) Internal reconstruction.
   (b) External reconstruction.
   (c) Amalgamation in the nature of merger.
   (d) Amalgamation in the nature of purchase.
4. Reconstruction is a process by which affairs of a company are reorganized by
   (a) Revaluation of assets and Reassessment of liabilities.

(b) Writing off the losses already suffered by reducing the paid up value of shares and/or varying the rights attached to different classes of shares.

(c) Both (a) and (b).

(d) None of the above.

5. For reduction of the share capital, the permission has to be sought from

(a) Court. (b) Controller.

(c) State government. (d) Shareholders.

6. In case of internal reconstruction

(a) Only one company is liquidated. (b) Two or more companies are liquidated.

(c) No company is liquidated. (d) Two companies amalgamated

3. THEORETICAL QUESTIONS :

1. What are the methods of internal reconstruction generally followed by companies?

4. EXTRA QUESTIONS :

Question 9 : Parth Ltd.

Parth Ltd., had laid down the following terms upon the sanction of the reconstruction plan by the court

1. Furniture and Fixtures which stood at the books at Rs. 1,50,000 to be written down to Rs. 95,000. The freehold premises which was valued at Rs. 7,00,000 showed an appreciation of Rs. 55,000.
2. Plant and machinery showed fall in value of Rs. 89,000, to be recorded in the books. Investment at Rs. 2,00,000 was brought down to the existing market value at Rs. 1,05,000.
3. Debenture holders accepted to receive the following in lieu of their present 9% debentures of Rs.2,50,000-
   a. 1/5th of the total to be paid in cash to them.
   b. To take over the land and buildings of value Rs. 72,000.
   c. To forgo the remaining unpaid portion as a policy of reconstruction.

Write off the profit and loss A/c debit balance at Rs. 70,000 which had been accumulated over the years. In case of any shortfall, the balance of the General reserve of Rs. 1,50,000 can be utilized to write off the losses under reconstruction scheme.

Show the necessary journal entries as part of the reconstruction process considering that balance in general reserve utilized to write off the losses as per reconstruction scheme

Questions 10 : Win Limited

The following scheme of reconstruction has been approved for Win Limited:

(i) The shareholders to receive in lieu of their present holding at 1,00,000 shares of Rs.10 each, the following:

(a) New fully paid Rs. 10 Equity shares equal to 3/5th of their holding.

(b) 10% Preference shares fully paid to the extent of 1/5th of the above new equity shares.

(c) Rs. 40,000, 8% Debentures.

(ii) An issue of Rs. 1 lakh 10% first debentures was made and allotted, payment for the same being received in cash forthwith.

(iii) Goodwill which stood at Rs. 1,40,000 was completely written off.

(iv) Plant and machinery which stood at Rs. 2,00,000 was written down to Rs. 1,50,000

(v) Freehold property which stood at Rs. 1,50,000 was written down by Rs. 50,000.

You are required to draw up the necessary Journal entries in the Books of Win Limited for the above reconstruction. Suitable narrations to Journal entries should form part of your answer.

Question 11 : Green Limited

Green Limited had decided to reconstruct the Balance Sheet since it has accumulated huge losses. The following is the Balance Sheet of the Company as at 31.3.20X1 before reconstruction:

		Particulars	Notes	Rs.
		Equity and Liabilities		
1		**Shareholders' fund**		
	A	Share capital	1	65,00,000
	B	Reserves and Surplus	2	(20,00,000)
2		**Non-current liabilities**		
	A	Long-term borrowings	3	15,00,000
3		**Current liabilities**		
	A	Trade Payables		5,00,000
		Total		65,00,000
		Assets		
1		**Non-current assets**		
	A	Property, plant and equipment	4	45,00,000
	B	Intangible assets	5	20,00,000
2		**Current assets**		NIL
		Total		65,00,000

Notes to accounts :

		Rs.
1	**Share Capital**	
	Equity share capital	
	Authorized share capital	
	1,50,000 Equity shares of Rs. 50 each	75,00,000
	Issued, subscribed and paid up capital	
	50,000 Equity Shares of Rs. 50 each	25,00,000
	1,00,000 Equity shares of Rs. 50 each, Rs. 40 paid up	40,00,000
		65,00,000
2	**Reserves and Surplus**	
	Debit balance of Profit and loss Account	(20,00,000)
3	**Long-term borrowings**	
	Secured: 12% First debentures	5,00,000
	12% Second debentures	10,00,000
		15,00,000
4	**Property, Plant and Equipment**	
	Building	10,00,000
	Plant	10,00,000
	Computers	25,00,000
		45,00,000
5	**Intangible assets**	
	Goodwill	20,00,000
		20,00,000

The following is the interest of Mr. X and Mr. Y in Green Limited

	Mr. X Rs.	**Mr. Y Rs.**
12% First Debentures	3,00,000	2,00,000
12% Second Debentures	7,00,000	3,00,000
Trade payables	2,00,000	1,00,000
	12,00,000	6,00,000
Fully paid up Rs. 50 shares	3,00,000	2,00,000
Partly paid up shares (Rs. 40 paid up)	5,00,000	5,0,0000

The following Scheme of Reconstruction is approved by all parties interested and also by the Court:

(a) Uncalled capital is to be called up in full and such shares and the other fully paid up shares be converted into equity shares of Rs. 20 each.

(b) Mr. X is to cancel Rs. 7,00,000 of his total debt (other than share amount) and to pay Rs. 2 lakhs to the company and to receive new 14% First Debentures for the balance amount.

(c) Mr. Y is to cancel Rs. 3,00,000 of his total debt (other than equity shares) and to accept new 14% First Debentures for the balance.

(d) The amount thus rendered available by the scheme shall be utilised in writing off of Goodwill, Profit and Loss A/c Loss and the balance to write off the value of computers

You are required to draw the Journal Entries to record the same and also show the Balance Sheet of the reconstructed company.

Question 12 : Weak Ltd.

The following is the Balance Sheet of Weak Ltd. as at 31.3.20X1:

		Particulars	Notes	Rs.
		Equity and Liabilities		
1		**Shareholders' funds**		
	A	Share capital	1	1,50,00,000
	B	Reserves and Surplus	2	(6,00,000)
2		**Non-current liabilities**		
	A	Long-term borrowings	3	40,00,000
3		**Current liabilities**		
	A	Trade Payables		50,00,000
	B	Short term provisions	4	1,00,000
		Total		2,35,00,000
		Assets		
1		**Non-current assets**		
	A	Property, plant and equipment		1,25,00,000
	B	Non-current investment	5	10,00,000
2		**Current assets**		1,00,00,000
		Total		2,35,00,000

Notes to accounts :

		Rs.
1	**Share Capital**	
	Equity share capital	
	1,00,000 Equity Shares of Rs. 100 each	1,00,00,000

	50,000, 12% Cumulative Preference shares of Rs. 100 each	50,00,000
		1,50,00,000
2	**Reserves and Surplus**	
	Debit balance of Profit and loss Account	(6,00,000)
		(6,00,000)
3	**Long-term borrowings**	
	40,000, 10% debentures of Rs. 100 each	40,00,000
		40,00,000
4	**Short term provisions**	
	Provision for taxation	1,00,000
		1,00,000
5	**Non-current investments**	
	Investments (market value of Rs. 9,50,000)	10,00,000
		10,00,000

The following scheme of reorganization is sanctioned:

(i) All the existing equity shares are reduced to Rs. 40 each.

(ii) All preference shares are reduced to Rs. 60 each.

(iii) The rate of interest on debentures is increased to 12%. The debenture holders surrender their existing debentures of Rs. 100 each and exchange the same for fresh debentures of Rs. 70 each for every debenture held by them.

(iv) One of the creditors of the company to whom the company owes Rs. 20,00,000 decides to forgo 40% of his claim. He is allotted 30,000 equity shares of Rs. 40 each in full satisfaction of his claim.

(v) Property, plant and equipment are to be written down by 30%.

(vi) Current assets are to be revalued at Rs. 45,00,000.

(vii) The taxation liability of the company is settled at Rs. 1,50,000.

(viii) Investments to be brought to their market value.

(ix) It is decided to write off the debit balance of Profit and Loss account.

Pass Journal entries and show the Balance sheet of the company after giving effect to the above.

Questions 13 : X Ltd.

The following is the Balance Sheet of X Ltd. as at 31st March, 20X1:

		Particulars	Notes	Rs.
		Equity and Liabilities		
1		**Shareholders' funds**		
	A	Share capital	1	36,00,000

	B	Reserves and Surplus	2	(14,40,000)
2		**Non-current liabilities**		
	A	Long-term borrowings	3	6,00,000
3		**Current liabilities**		
	A	Trade Payables		3,00,000
	B	Short term borrowings – Bank Overdraft		6,00,000
		Total		36,60,000
		Assets		
1		**Non-current assets**		
	A	Property, plant and equipment	4	30,00,000
	B	Intangible assets	5	90,000
2		**Current assets**		
	a	Inventories		2,60,000
	b	Trade receivables		2,80,000
	c	Cash and cash equivalents		30,000
		Total		36,60,000

Notes to accounts :

		Rs.
1	**Share Capital**	
	Equity share capital	
	24,000 Equity Shares of Rs. 100 each	24,00,000
	12,000 10% Preference shares of Rs. 100 each	12,00,000
	Total	36,00,000
2	**Reserves and Surplus**	
	Debit balance of Profit and loss Account	(14,40,000)
		(14,40,000)
3	**Long-term borrowings**	
	10% debentures	6,00,000
		6,00,000
4	**Property, plant and Equipment**	
	Land and Building	12,00,000
	Plant and Machinery	18,00,000
		30,00,000
5	**Intangible assets**	
	Goodwill	90,000
		90,000

On the above date, the company adopted the following scheme of reconstruction:

(i) The equity shares are to be reduced to shares of Rs. 40 each fully paid and the preference shares to be reduced to fully paid shares of Rs. 75 each.

(ii) The debenture holders took over Inventories and Trade receivables in full satisfaction of their claims.

(iii) The Land and Building to be appreciated by 30% and Plant and machinery to be depreciated by 30%.

(iv) The debit balance of profit and loss account and intangible assets are to be eliminated.

(v) Expenses of reconstruction amounted to Rs. 5,000.

Give journal entries incorporating the above scheme of reconstruction and prepare the reconstructed Balance Sheet.

Thanks ....

Chapter 35

ACCOUNTING FOR BRANCHES INCLUDING FOREIGN BRANCHES

CHAPTER DESIGN

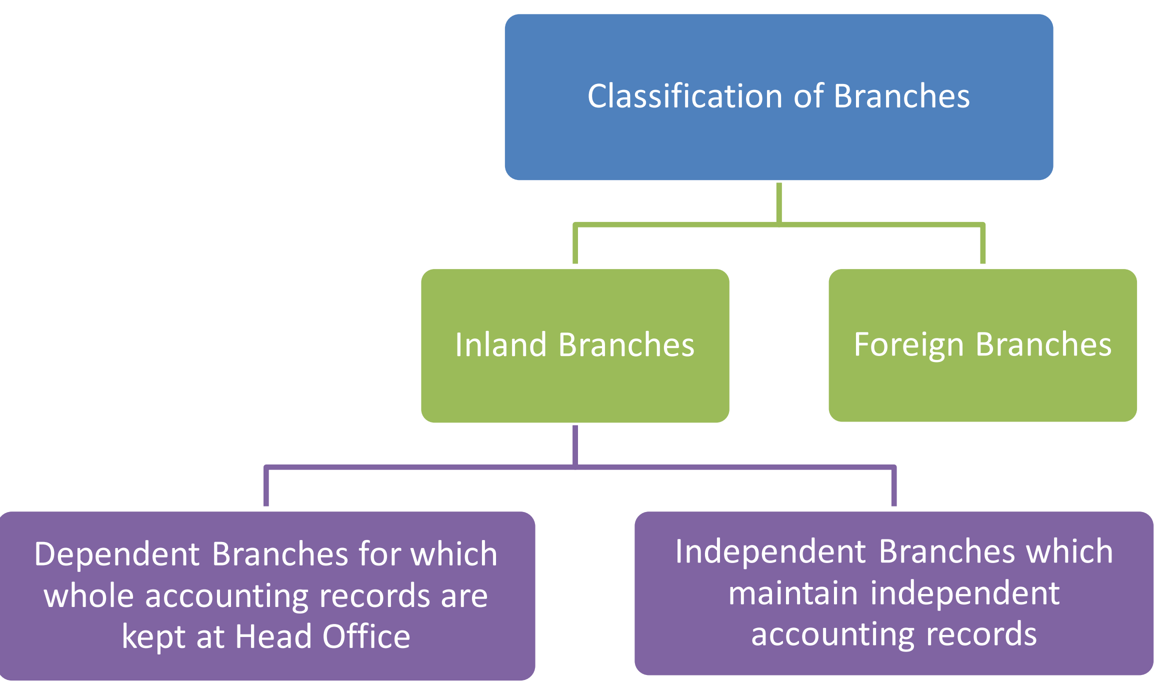
1. INTRODUCTION
2. CLASSIFICATION OF BRANCHES
3. ACCOUNTING FOR DEPENDENT BRANCHES
4. ACCOUNTING FOR INDEPENDENT BRANCHES
5. FOREIGN BRANCHES

1. INTRODUCTION :

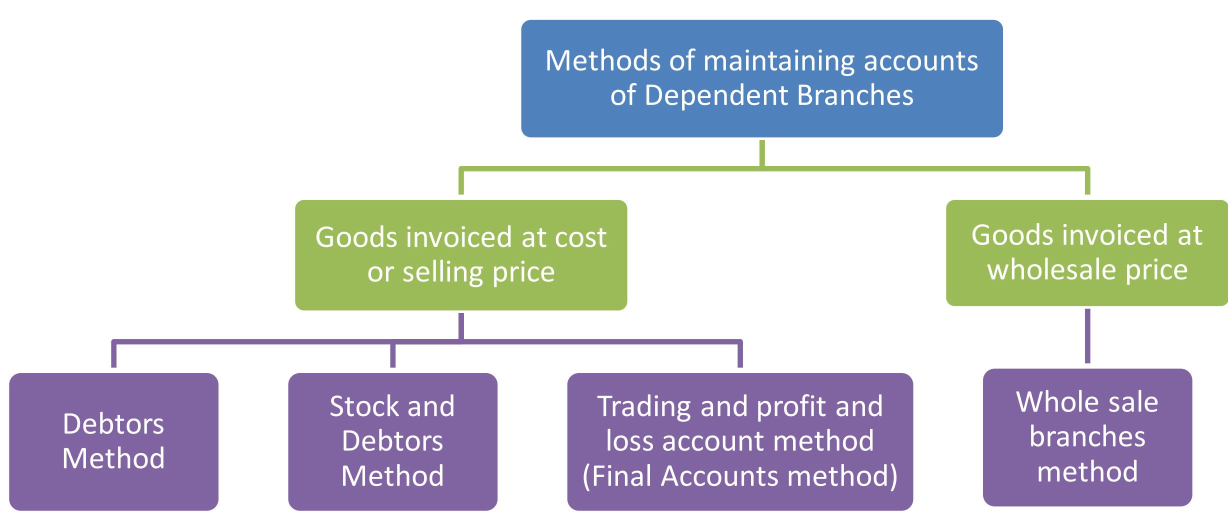
A branch can be described as any establishment carrying on either the same or substantially the same activity as that carried on by head office of the company. It must also be noted that the concept of a branch means existence of a head office; for there can be no branch without a head office - the principal place of business.

2. CLASSIFICATION OF BRANCHES :

From the accounting point of view, branches may be classified as follows:



3. ACCOUNTING FOR DEPENDENT BRANCHES :



3.1 Debtors Method :

This method of accounting is suitable for small sized branches. Under this method, separate branch account is maintained for each branch to compute profit or loss made by each branch.

Proforma Branch Account

Particulars	Amount	Particulars	Amount
To Balance b/d (opening Assets)		By Balance b/d (Opening Liabilities)	
Cash	XXX	Liabilities	XXX
Stock	XXX	By Goods returned to HO	XXX
Debtors	XXX	By Bank A/c (Cash Remitted)	XXX
Petty cash	XXX	By Balance c/d (Closing Assets)	
Fixed Assets	XXX	Cash	XXX
Prepaid Expenses	XXX	Stock	XXX
To Goods sent to branch	XXX	Debtors	XXX
To Bank A/c		Petty cash	XXX
Salaries	XXX	Fixed Assets	XXX
Rent	XXX	Prepaid Expenses	XXX
Sundry expenses	XXX	By Profit and Loss A/c	XXX
To Balance c/d (Closing Liabilities)		(Balancing figure – Loss)	
Liabilities	XXX		
To Profit and Loss A/c	XXX		
(Balancing figure – Profit)			
Total	XXX	Total	XXX

Note:

1. Only transaction between HO and Branch and HO and others in relation to branch are recorded
2. Transaction between branch and others in are not recorded.

Question 1 : Buckingham Bros, Bombay

Buckingham Bros, Bombay have a branch at Nagpur. They send goods at cost to their branch at Nagpur. However, direct purchases are also made by the branch for which payments are made at head office. All the daily collections are transferred from the branch to the head office.

From the following, prepare Nagpur branch account in the books of head office by Debtors method:

	Rs.		Rs.
Opening balance (1-1-20X1) Imprest Cash	2,000	Bad Debts	1,000
Sundry Debtors	25,000	Discount to Customers	2,000
Stock: Transferred from H.O.	24,000	Remittances to H.O. (recd. by H.O.)	1,65,000
Direct Purchases	16,000	Remittances to H.O. not recd. by H.O. so far)	5,000
Cash Sales	45,000	Branch Exp. directly paid by H.O.	30,000
Credit Sales	1,30,000	Closing Balance (31-12-20X1)	
Direct Purchases	45,000	Stock: Direct Purchase	10,000
Returns from Customers	3,000	Transfer from H.O.	15,000
Goods sent to branch from H.O.	60,000	Debtors	?
Transfer from H.O. for Petty Cash expenses	4,000	Imprest Cash	?
		Petty Cash expenses	4,000

3.2 Stock and Debtors Method :

If it is desired to exercise a more detailed control over the working of a branch, the accounts of the branch are maintained under the Stock and Debtors Method. According to this method, the following accounts are maintained by the Head Office:

1. Brach Stock A/c - To ascertain shortage or surplus
2. Goods sent to Branch A/c - Ascertainment of cost of goods sent to branch
3. Branch Adjustment A/c - To ascertain trading profit
4. Branch Debtors A/c - Ascertainment of closing balance of debtors
5. Branch Cash/Bank A/c - To ascertain closing balance of cash/bank at branch
6. Branch Asset A/c - To Maintain branch Assets
7. Branch Expenses A/c - Ascertainment of total expenses incurred
8. Branch profit and Loss A/c - Calculation of net profit or loss

Journal Entries :

1. H.O sends goods to branch

   (A) AT IP Branch Stock A/c Dr.

   To Goods sent to Branch A/c

(B) Loading Goods sent to branch A/c Dr.
To Branch Adjustment A/c

2. Brach returns goods to H.O

(A) At IP Goods sent to Branch A/c Dr.
To Branch Stock A/c

(B) Loading Branch Adjustment A/c Dr.
To Goods sent to Branch A/c

3. Remittance for expenses

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

4. Cash Sales at Branch

Branch Cash A/c Dr.
To Branch Stock A/c

5. Credit sales at Branch

Branch Debtors A/c Dr.
To Branch Stock A/c

6. Return of goods by debtors

Branch Stock A/c Dr.
To Branch Debtors A/c

7. Cash paid by debtors

Brach Cash A/c Dr.
To Branch Debtors A/c

8. Discount Allowed / Bad Debts

Branch Expenses A/c Dr.
To Branch Debtors A/c

9. Expenses of Branch paid by HO

Branch Expenses A/c Dr.
To Cash A/c

10. Expenses of Branch paid by Branch

Branch Expenses A/c Dr.

To Branch Cash A/c

11. Remittance to HO

Cash A/c Dr.

To Branch Cash A/c

3.3 Branch Trading and Profit and Loss Account :

In this method, Trading and Profit and Loss accounts are prepared considering each branch as a separate entity. The main advantage of this method is that, it is easy to prepare and understand. It also gives complete information of all transactions which are ignored in the other methods. It should be noted that Branch Trading and Profit and Loss account is merely a memorandum account and therefore, the entries made there in do not have double entry effect.

Question 2 : Buckingham Bros, Bombay

Buckingham Bros, Bombay have a branch at Nagpur. They send goods at cost to their branch at Nagpur. However, direct purchases are also made by the branch for which payments are made at head office. All the daily collections are transferred from the branch to the head office.

From following, prepare Nagpur Branch Trading and Profit and Loss Account in the books of head office.

	Rs.		Rs.
Opening balance (1-1-20X1) Imprest Cash	2,000	Bad Debts	1,000
Sundry Debtors	25,000	Discount to Customers	2,000
Stock: Transferred from H.O.	24,000	Remittances to H.O. (recd. by H.O.)	1,65,000
Direct Purchases	16,000	Remittances to H.O. not recd. by H.O. so far)	5,000
Cash Sales	45,000	Branch Exp. directly paid by H.O.	30,000
Credit Sales	1,30,000	Closing Balance (31-12-20X1)	
Direct Purchases	45,000	Stock: Direct Purchase	10,000

Returns from Customers	3,000	Transfer from H.O.	15,000
Goods sent to branch from H.O.	60,000	Debtors	?
Transfer from H.O. for Petty Cash expenses	4,000	Imprest Cash	?
		Petty Cash expenses	4,000

Question 3 : The Bombay Traders

The Bombay Traders invoiced goods to its Delhi branch at cost. Head Office paid all the branch expenses from its bank account, except petty cash expenses which were met by the Branch. All the cash collected by the branch was banked on the same day to the credit of the Head Office. The following is a summary of the transactions entered into at the branch during the year ended December 31, 20X1.

	Rs.		Rs.
Balances as on 1.1.20X1:		Bad Debts	600
Stock	7,000	Goods returned by customers	500
Debtors	12,600	Salaries & Wages	6,200
Petty Cash,	200	Rent & Rates	1,200
Goods sent from H.O.	26,000	Sundry Expenses	800
Goods returned to H.O.	1,000	Cash received from Sundry Debtors	28,500
Cash Sales	17,500	Balances as on 31.12.20X1:	
Credit Sales	28,400	Stock	6,500
Allowances to customers	200	Debtors	9,800
Discount to customers	1,400	Petty Cash	100

Prepare: (a) Branch Account (Debtors Method), (b) Branch Stock Account, Branch Profit & Loss Account, Branch Debtors and Branch Expenses Account by adopting the Stock and Debtors Method and (c) Branch Trading and Profit & Loss Account to prove the results as disclosed by the Branch Account.

Question 4 : Harrison of Chennai

Harrison of Chennai has a branch at New Delhi to which goods are sent @ 20% above cost. The branch makes both cash and credit sales. Branch expenses are met partly from H.O. and partly by the branch. The statement of expenses incurred by the branch every month is sent to head office for recording.

Following further details are given for the year ended 31st December, 20X1 :

		Rs.
Cost of goods sent to Branch at cost		2,00,000
Goods received by Branch till 31-12-20X1 at invoice price		2,20,000
Credit Sales for the year @ invoice price		1,65,000
Cash Sales for the year @ invoice price		59,000
Cash Remitted to head office		2,22,500
Expenses paid by H.O.		12,000
Bad Debts written off		750
Balance as on		
	Rs.	Rs.
Stock	25,000 (Cost)	28,000 (invoice price)
Debtors	32,750	26,000
Cash in Hand	5,000	2,500

Show necessary ledger accounts in the books of the head office and determine the Profit and Loss of the Branch for the year ended 31st December, 20X1.

Question 5 :

Take figures from Illustration 4 and prepare branch account following debtors' method.

Question 6 : Jammu branch of Best New Delhi

Following is the information of the Jammu branch of Best New Delhi for the year ending 31st March, 20X2 from the following:

(1) Goods are invoiced to the branch at cost plus 20%.

(2) The sale price is cost plus 50%.

(3) Other information:

	Rs.
Stock as on 01.04.20X1(invoice price)	2,20,000
Goods sent during the year(invoice price)	11,00,000
Sales during the year	12,00,000
Expenses incurred at the branch	45,000

Ascertain

(i) the profit earned by the branch during the year.

(ii) branch stock reserve in respect of unrealized profit.

Question 7 : Sell Well

Sell Well who carried on a retail business opened a branch X on January 1st, 20X1 where all sales were on credit basis. All goods required by the branch were supplied from the Head Office and were invoiced to the branch at 10% above cost.

The following were the transactions:

	Jan. 20X1	Feb. 20X1	March 20X1
	Rs.	Rs.	Rs.
Goods sent to Branch (Purchase Price)	40,000	50,000	60,000
Sales as shown by the branch monthly report	38,000	42,000	55,000
Cash received from Debtors and remitted to H.O.	20,000	51,000	35,000
Returns to H.O. (Invoice price to Branch)	1,200	600	2,400

The stock of goods held by the branch on March 31, 20X1 amounted to Rs. 53,400 at invoice to branch.

Record these transactions in the Head Office books, showing balances as on 31st March, 20X1 and the branch gross profit for the three months ended on that date.

All workings should form part of your solution.

Question 8 : Hindustan Industries Mumbai

Hindustan Industries Mumbai has a branch in Cochin to which office goods are invoiced at cost plus 25%. The branch sells both for cash and on credit. Branch Expenses are paid direct from head office, and the Branch has to remit all cash received into the Head Office Bank Account.

From the following details, relating to calendar year 20X1, prepare the accounts in the Head Office Ledger and ascertain the Branch Profit. Branch does not maintain any books of account, but sends weekly returns to the Head Office :

	Rs.
Goods received from Head Office at invoice price	6,00,000
Returns to Head Office at invoice price	12,000
Stock at Cochin as on 1st Jan., 20X1	60,000
Sales in the year - Cash	2,00,000
Credit	3,60,000
Sundry Debtors at Cochin as on 1st Jan. 20X1	72,000
Cash received from Debtors	3,20,000
Discount allowed to Debtors	6,000
Bad debts in the year	4,000

Sales returns at Cochin Branch	8,000
Rent, Rates, Taxes at Branch	18,000
Salaries, Wages, Bonus at Branch	60,000
Office Expenses	6,000
Stock at Branch on 31st Dec. 20X1 at invoice price	1,20,000

Prepare Branch accounts in books of head office by Stock and debtors method.

Question 9 : Arnold of Delhi

Arnold of Delhi, trades in Ghee and Oil. It has a branch at Lucknow. He dispatches 25 tins of Oil @ Rs.1,000 per tin and 15 tins of Ghee @ Rs.1,500 per tin on 1st of every month. The branch incurs some expenditure which is met out of its collections; this is in addition to expenditure directly paid by Head Office.

Following are the other details :

		Rs.	Rs.
Purchases	Ghee	14,75,000	-
	Oil	29,32,000	-
Direct expenses		3,83,275	-
Expenses paid by H.O.		-	14,250
Sales	Ghee	18,46,350	3,42,750
	Oil	27,41,250	3,15,730
Collection during the year (including Cash Sales)		-	6,47,330
Remittance by Branch to Head Office		-	6,13,250

	(Delhi)	
Balance as on:	1-1-20X1	31-12-20X1
Stock : Ghee	1,50,000	3,12,500
Oil	3,50,000	4,17,250
Debtors	7,32,750	-
Cash on Hand	70,520	55,250
Furniture & Fittings	21,500	19,350
Plant/Machinery	3,07,250	7,73,500

	(Lucknow)	
Balance as on:	1-1-20X1	31-12-20X1
Stock : Ghee	17,000	13,250
Oil	27,000	44,750
Debtors	75,750	?
Cash on Hand	7,540	12,350

Furniture & Fittings	6,250	5,625
Plant/Machinery	-	-

Addition to Plant/Machinery on 1-1-20X1 Rs.6,02,750.

Rate of Depreciation: Furniture / Fittings @ 10% and Plant / Machinery @ 15% (already adjusted in the above figures).

The Branch Manager is entitled to 10% commission after charging such commission whereas, the General Manager is entitled to 10% commission on overall company profits after charging such commission. General Manager is also entitled to a salary of Rs.2,000 p.m. General expenses incurred by H.O. Rs.24,000.

Prepare Branch Account in the head office books and also prepare the Arnold's Trading and Profit and Loss A/c (excluding branch transactions).

Question 10 : M/s Rahul

M/s Rahul operates a number of retail outlets to which goods are invoiced at wholesale price which is cost plus 25%. These outlets sell the goods at the retail price which is wholesale price plus 20%.

Following is the information regarding one of the outlets for the year ended 31.3.20X2:

	Rs.
Stock at the outlet 1.4.20X1	30,000
Goods invoiced to the outlet during the year	3,24,000
Gross profit made by the outlet	60,000
Goods lost by fire	?
Expenses of the outlet for the year	20,000
Stock at the outlet 31.3.20X2	36,000

You are required to prepare the following accounts in the books of Rahul Limited for the year ended 31.3.20X2 :

(a) Outlet Stock Account.

(b) Outlet Profit & Loss Account.

(c) Stock Reserve Account.

4. ACCOUNTING FOR INDEPENDENT BRANCHES :

When the size of the business is big, it is desirable that the branch maintains complete records of its transactions. These branches are called independent branches and each independent branch maintains comprehensive account books for recording their transactions; therefore a separate trial balance of each branch can be prepared. The head office maintains one ledger account for each such branch, wherein all transactions between the head office and the branches are recorded.

Question 11 : Messrs Ramchand & Co.

Messrs Ramchand & Co., Hyderabad have a branch in Delhi. The Delhi Branch deals not only in the goods from Head Office but also buys some auxiliary goods and deals in them. They, however, do not prepare any Profit & Loss Account but close all accounts to the Head Office at the end of the year and open them afresh on the basis of advice from their Head Office. The fixed assets accounts are also maintained at the Head Office.

The goods from the Head Office are invoiced at selling prices to give a profit of 20 per cent on the sale price. The goods sent from the branch to Head Office are at cost. From the following prepare Branch Trading and Profit & Loss Account and Branch Assets Account in the Head Office Books.

Trial Balance of the Delhi Branch as on 31-12-20X1

Debit	Rs.	Credit	Rs.
Head office opening balance on 1-1-20X1	15,000	Sales	1,00,000
Goods from H.O.	50,000	Goods to H.O.	3,000
Purchases	20,000	Head Office Current A/c	15,000
Opening Stock		Sundry Creditors	3,000
(H.O. supplies goods at invoice prices)	4,000		
Opening Stock of other goods	500		
Salaries	7,000		
Rent	3,000		
Office expenditure	2,000		
Cash on Hand	500		
Cash at Bank	4,000		
Sundry Debtors	15,000		
	1,21,000		**1,21,000**

The Branch balances as on 1st January, 20X1, were as under: Furniture Rs.5,000; Sundry Debtors Rs.9,500; Cash Rs.1,000, Creditors Rs.30,000. The closing stock at branch of the head office goods at invoice price is Rs.3,000 and that of purchased goods at cost is Rs.1,000. Depreciation is to be provided at 10 per cent on branch assets.

Question 12 : Ring Bell Ltd.

Ring Bell Ltd. Delhi has a Branch at Bombay where a separate set of books is used. The following is the trial balance extracted on 31st December, 20X1.

Head Office Trial Balance

	Rs.	Rs.
Share Capital (Authorised: 10,000 Equity Shares of Rs.100 each):		
Issued: 8,000 Equity Shares		8,00,000
Profit & Loss Account - 1-1-20X1		25,310
General Reserve		1,00,000
Fixed Assets	5,30,000	
Stock	2,22,470	
Debtors and Creditors	50,500	21,900
Profit for 20X1		52,200
Cash Balance	62,730	
Branch Current Account	1,33,710	
	9,99,410	**9,99,410**

Branch Trial Balance

	Rs.	Rs.
Fixed Assets	95,000	
Profit for 20X1		31,700
Stock	50,460	
Debtors and Creditors	19,100	10,400
Cash Balance	6,550	
Head Office Current Account		1,29,010
	1,71,110	**1,71,110**

The difference between the balances of the Current Account in the two sets of books is accounted for as follows:

(a) Cash remitted by the Branch on 31st December, 20X1, but received by the Head Office on 1st January 20X2 – Rs.3,000.

(b) Stock stolen in transit from Head Office and charged to Branch by the Head Office, but not credited to Head Office in the Branch books as the Branch Manager declined to admit any liability (not covered by insurance) – Rs.1,700.

Give the Branch Current Account in Head Office books after incorporating Branch Trial Balance through journal.

Question 13 : KP manufactures

KP manufactures a range of goods which it sells to wholesale customers only from its head office. In addition, the H.O. transfers goods to a newly opened branch at factory cost plus 15%. The branch then sells these goods to the general public on only cash basis.

The selling price to wholesale customers is designed to give a factory profit which amounts to 30% of the sales value. The selling price to the general public is designed to give a gross margin (i.e., selling price less cost of goods from H.O.) of 30% of the sales value.

KP operates from rented premises and leases all other types of fixed assets. The rent and hire charges for these are included in the overhead costs shown in the trial balances.

From the information given below, you are required to prepare for the year ended 31st Dec., 20X1 in columnar form.

(a) A Profit & Loss account for (i) H.O. (ii) the branch (iii) the entire business.

(b) Balance Sheet as on 31st Dec., 20X1 for the entire business.

	HO		Branch	
	Rs.	**Rs.**	**Rs.**	**Rs.**
Raw materials purchased	35,000			
Direct wages	1,08,500			
Factory overheads	39,000			
Stock on 1-1-20X1				
Raw materials	1,800			
Finished goods	13,000		9,200	
Debtors	37,000			
Cash	22,000		1,000	
Administrative Salaries	13,900		4,000	
Salesmen Salaries	22,500		6,200	
Other administrative & selling overheads	12,500		2,300	
Inter-unit accounts	5,000			2,000
Capital		50,000		
Sundry Creditors		13,000		
Provision for unrealized profit in stock		1,200		
Sales		2,00,000		65,200
Goods sent to Branch		46,000		
Goods received from H.O.			44,500	
	3,10,200	**3,10,200**	**67,200**	**67,200**

Notes:

(1) On 28th Dec., 20X1 the branch remitted Rs.1,500 to the H.O. and this has not yet been recorded in the H.O. books. Also on the same date, the H.O. dispatched goods to the branch invoiced at Rs.1,500 and these too have not yet been entered into the branch books. It is the company's policy to adjust items in transit in the books of the recipient.

(2) The stock of raw materials held at the H.O. on 31st Dec., 20X1 was valued at Rs.2,300.

(3) You are advised that:

- there were no stock losses incurred at the H.O. or at the branch.
- it is KP's practice to value finished goods stock at the H.O. at factory cost.
- there were no opening or closing stock of work-in-progress.

(4) Branch employees are entitled to a bonus of Rs. 156 under a bilateral agreement.

Question 14 : AFFIX of Kolkata

AFFIX of Kolkata has a branch at Delhi to which the goods are supplied from Kolkata but the cost thereof is not recorded in the Head Office books. On 31st March, 20X1 the Branch Balance Sheet was as follows :

Liabilities	Rs.	Assets	Rs.
Creditors Balance	40,000	Debtors Balance	2,00,000
Head Office	1,68,000	Building Extension A/c closed by transfer to H.O. A/c	—
		Cash at Bank	8,000
	2,08,000		**2,08,000**

During the six months ending on 30-9-20X1, the following transactions took place at Delhi.

	Rs.		Rs.
Sales	2,40,000	Manager's Salary	4,800
Purchases	48,000	Collections from Debtors	1,60,000
Wages paid	20,000	Discounts allowed	8,000
Salaries (inclusive of advance of Rs.2,000)	6,400	Discount earned	1,200
General Expenses	1,600	Cash paid to Creditors	60,000
Fire Insurance (paid for one year)	3,200	Building Account (further payment)	4,000
Remittance to H.O.	38,400	Cash in Hand	1,600
		Cash at Bank	28,000

Set out the Head Office Account in Delhi books and the Branch Balance Sheet as on 30-9-20X1. Also give journal entries in the Delhi books.

Question 15 :

The following Trial balances as at 31st December, 20X1 have been extracted from the books of Major Ltd. and its branch at a stage where the only adjustments requiring to be made prior to the preparation of a Balance Sheet for the undertaking as a whole.

	HO		Branch	
	Dr. (Rs.)	**Cr. (Rs.)**	**Dr. (Rs.)**	**Cr. (Rs.)**
Share Capital		1,50,000		
Fixed Assets	75,125		18,901	
Current Assets	1,21,809		23,715	(Note 3)
Current Liabilities		34,567		9,721
Stock Reserve, 1st Jan., 20X1 (Note 2)		693		
Revenue Account		43,210		10,250
Branch Account	31,536			
Head Office Account				22,645
	2,28,470	**2,28,470**	**42,616**	**42,616**

You are required to record the following in the appropriate ledger accounts in both sets of books:

Notes:

1. Goods transferred from Head Office to the Branch are invoiced at cost plus 10% and both Revenue Accounts have been prepared on the basis of the prices charged.
2. Relating to the Head Office goods held by the Branch on 1st January, 20X1.
3. Includes goods received from Head Office at invoice price Rs. 4,565.
4. Goods invoiced by Head Office to Branch at Rs. 3,641 were in transit at 31st December, 20X1, as was also a remittance of Rs. 3,500 from the Branch.
5. At 31st December, 20X1, the following transactions were reflected in the Head Office books but unrecorded in the Branch books.

The purchase price of lorry, Rs. 2,500, which reached the Branch on December 25th; a sum received on December 30, 20X1 from one of the Branch debtors, Rs. 750.

5. FOREIGN BRANCHES :

For the purpose of accounting, AS 11 (revised 2003) classifies the foreign branches may be classified into two types:

- Integral Foreign Operation;
- Non- Integral Foreign Operation.

Integral Foreign Operation (IFO)

It is a foreign operation, the activities of which are an integral part of those of the reporting enterprise. The business of IFO is carried on as if it were an extension of the reporting enterprise's operations. For example, sale of goods imported from the reporting enterprise and remittance of proceeds to the reporting enterprise.

Non-Integral Foreign Operation (NFO)

The following are the indicators of Non- Integral Foreign Operation-

- Control by reporting enterprises - While the reporting enterprise may control the foreign operation, the activities of foreign operation are carried independently without much dependence on reporting enterprise.
- Transactions with the reporting enterprises are not a high proportion of the foreign operation's activities.
- Activities of foreign operation are mainly financed by its operations or from local borrowings. In other words, it raises finance independently and is in no way dependent on reporting enterprises.
- Foreign operation sales are mainly in currencies other than reporting currency.
- All the expenses by foreign operations are primarily paid in local currency, not in the reporting currency.
- Day-to-day cash flow of the reporting enterprises is independent of the foreign enterprises cash flows.
- Sales prices of the foreign enterprises are not affected by the day-to-day changes in exchange rate of the reporting currency of the foreign operation.
- There is an active sales market for the foreign operation product.

Techniques for foreign currency translation

Integral Foreign Operation (IFO) :

Following are the standard recommendations for foreign currency translation:

(1) All transactions of IFO be translated at the rate prevailing on the date of transaction. This will require date wise details of the transaction entered by that operation together with the rates. Weekly or monthly average rate is permitted if there are no significant variations in the rate.

(2) Translation at the balance sheet date-
- (i) Monetary items at closing rate;
- (ii) Non-monetary items: The cost and depreciation of the tangible fixed assets is translated using the exchange rate at the date of purchase of the asset if asset is carried at cost. If tangible fixed asset is carried at fair value, translation should be done using the rate existed on the date of the valuation.
- (iii) The cost of inventories is translated at the exchange rates that existed when the cost of inventory was incurred and realizable value is translated applying exchange rate when realizable value is determined which is generally closing rate.
- (iv) Exchange difference arising on the translation of the financial statement of integral foreign operation should be charged to profit and loss account

Non-Integral Foreign Operation :

Accounts of non-integral foreign operation are translated using the following principles:

- Balance sheet items i.e. Assets and Liabilities both monetary and nonmonetary – apply closing exchange rate.
- Items of income and expenses – At actual exchange rates on the date of transactions. However, accounting standard allows average rate subject to materiality.
- Resulting exchange rate difference should be accumulated in a "foreign currency translation reserve" until the disposal of "net investment in nonintegral foreign operation".

Question 16 : Books of Chennai Branch

On 31st December, 20X2 the following balances appeared in the books of Chennai Branch of an English firm having its HO office in New York:

	Rs.	Rs.
Stock on 1st Jan., 20X2	2,34,000	-
Purchases and Sales	15,62,500	23,43,750
Debtors and Creditors	7,65,000	5,10,000
Bills Receivable and Payable	2,04,000	1,78,500
Salaries and Wages	1,00,000	-
Rent, Rates and Taxes	1,06,250	-
Furniture	91,000	-
Bank A/c	5,68,650	-
New York Account	-	5,99,150
	36,31,400	**36,31,400**

Stock on 31st December, 20X2 was Rs.6,37,500.

Branch account in New York books showed a debit balance of $ 13,400 on 31st December, 20X2 and Furniture appeared in the Head Office books at $ 1,750.

The rate of exchange for 1 $ on 31st December, 20X1 was Rs.52 and on 31st December, 20X2 was Rs.51. The average rate for the year was Rs.50.

Prepare in the Head Office books the Profit and Loss a/c and the Balance Sheet of the Branch assuming integral foreign operation.

Question 17 : S & M Ltd.

S & M Ltd., Bombay, have a branch in Sydney, Australia. Sydney branch is an integral foreign operation of S & M Ltd.

At the end of 31st March, 20X2, the following ledger balances have been extracted from the books of the Bombay Office and the Sydney Office:

	Bombay		Sydney	
	(Rs. thousands)		(Austr dollars thousands)	
	Debit	**Credit**	**Debit**	**Credit**
Share Capital	–	2,000	–	–
Reserves & Surplus	–	1,000	–	–
Land	500	–	–	–
Buildings (Cost)	1,000	–	–	–
Buildings Dep. Reserve	–	200	–	–
Plant & Machinery (Cost)	2,500	–	200	–
Plant & Machinery Dep. Reserve	–	600	–	130
Debtors / Creditors	280	200	60	30
Stock (1.4.20X1)	100	–	20	–
Branch Stock Reserve	–	4	–	–
Cash & Bank Balances	10	–	10	–
Purchases / Sales	240	520	20	123
Goods sent to Branch	–	100	5	–
Managing Director's salary	30	–	–	–
Wages & Salaries	75	–	45	–
Rent	–	–	12	–
Office Expenses	25	–	18	–
Commission Receipts	–	256	–	100
Branch / H.O. Current A/c	120	–	–	7
	4,880	**4,880**	**390**	**390**

The following information is also available:

(1) Stock as at 31.3.20X2:

Bombay Rs.1,50,000

Sydney A $ 3,125

You are required to convert the Sydney Branch Trial Balance into rupees;

(use the following rates of exchange :

Opening rate A $ =Rs.20

Closing rate A $ = Rs.24

Average rate A $ = Rs.22

For Fixed Assets A $ = Rs.18).

Question 18 : M/s Carlin

M/s Carlin has head office at New York (U.S.A.) and branch at Mumbai (India). Mumbai branch is an integral foreign operation of Carlin & Co.

Mumbai branch furnishes you with its trial balance as on 31st March, 20X2 and the additional information given thereafter:

	Dr.	Cr.
	Rupees in thousands	
Stock on 1st April, 20X1	300	–
Purchases and sales	800	1,200
Sundry Debtors and creditors	400	300
Bills of exchange	120	240
Wages and salaries	560	–
Rent, rates and taxes	360	–
Sundry charges	160	–
Computers	240	–
Bank balance	420	–
New York office a/c	–	1,620
	3,360	**3,360**

Additional information:

(a) Computers were acquired from a remittance of US $ 6,000 received from New York head office and paid to the suppliers. Depreciate computers at 60% for the year.

(b) Unsold stock of Mumbai branch was worth Rs. 4,20,000 on 31st March, 20X2.

(c) The rates of exchange may be taken as follows:

- on 1.4.20X1 @ Rs. 40 per US $
- on 31.3.20X2 @ Rs. 42 per US $
- average exchange rate for the year @ Rs. 41 per US $
- conversion in $ shall be made upto two decimal accuracy.

You are asked to prepare in US dollars the revenue statement for the year ended 31st March, 20X2 and the balance sheet as on that date of Mumbai branch as would appear in the books of New York head office of Carlin & Co. You are informed that Mumbai branch account showed a debit balance of US $ 39609.18 on 31.3.20X2 in New York books and there were no items pending reconciliation.

PRACTICAL QUESTIONS :

Question 19 :

Goods worth Rs. 50,000 sent by head office but the branch has received till the closing date goods for worth Rs. 40,000 only. Give journal entry in the books of H.O. and branch for goods in transit.

Question 20 : Alphs

Alphs having head office in Mumbai has a branch in Nagpur. The branch at Nagpur is an independent branch maintaining separate books of account. On 31.3.20X1, it was found that the goods dispatched by head office for Rs. 2,00,000 was received by the branch only to the extent of Rs. 1,50,000. The balance goods are in transit. What is the accounting entry to be passed by the branch for recording the goods in transit, in its books?

Question 21 :

Show adjustment journal entry in the books of head office at the end of April, 20X1 for incorporation of inter-branch transactions assuming that only head office maintains different branch accounts in its books.

A. Delhi branch:
- (1) Received goods from Mumbai – Rs.35,000 and Rs.15,000 from Kolkata.
- (2) Sent goods to Chennai – Rs.25,000, Kolkata – Rs.20,000.
- (3) Bill Receivable received – Rs.20,000 from Chennai.
- (4) Acceptances sent to Mumbai – Rs.25,000, Kolkata – Rs.10,000.

B. Mumbai Branch (apart from the above) :
- (5) Received goods from Kolkata – Rs.15,000, Delhi – Rs.20,000.
- (6) Cash sent to Delhi – Rs.15,000, Kolkata – Rs.7,000.

C. Chennai Branch (apart from the above) :
- (7) Received goods from Kolkata – Rs.30,000.
- (8) Acceptances and Cash sent to Kolkata – Rs.20,000 and Rs.10,000 respectively.

D. Kolkata Branch (apart from the above) :
- (9) Sent goods to Chennai – Rs.35,000.
- (10) Paid cash to Chennai – Rs.15,000.
- (11) Acceptances sent to Chennai – Rs.15,000.

Question 22 : Branch A

Give Journal Entries in the books of Branch A to rectify or adjust the following:

- (i) Head Office expenses Rs.3,500 allocated to the Branch, but not recorded in the Branch Books.
- (ii) Depreciation of branch assets, whose accounts are kept by the Head Office not provided earlier for Rs.1,500.
- (iii) Branch paid Rs.2,000 as salary to a H.O. Inspector, but the amount paid has been debited by the Branch to Salaries account.
- (iv) H.O. collected Rs.10,000 directly from a customer on behalf of the Branch, but no intimation to this effect has been received by the Branch.

(v) A remittance of Rs.15,000 sent by the Branch has not yet been received by the Head Office.

(vi) Branch A incurred advertisement expenses of Rs.3,000 on behalf of Branch B.

Question 23 : Widespread

Widespread invoices goods to its branch at cost plus 20%. The branch sells goods for cash as well as on credit. The branch meets its expenses out of cash collected from its debtors and cash sales and remits the balance of cash to head office after withholding Rs.10,000 necessary for meeting immediate requirements of cash. On 31st March, 20X1 the assets at the branch were as follows:

	Rs. ('000)
Cash in Hand	10
Trade Debtors	384
Stock, at Invoice Price	1,080
Furniture and Fittings	500

During the accounting year ended 31st March, 20X2 the invoice price of goods dispatched by the head office to the branch amounted to Rs.1 crore 32 lakhs. Out of the goods received by it, the branch sent back to head office goods invoiced at Rs.72,000. Other transactions at the branch during the year were as follows:

	Rs. ('000)
Cash Sales	9,700
Credit Sales	3,140
Cash collected by Branch from Credit Customers	2,842
Cash Discount allowed to Debtors	58
Returns by Customers	102
Bad Debts written off	37
Expenses paid by Branch	842

On 1st January, 20X2 the branch purchased new furniture for Rs. 1 lakh for which payment was made by head office through a cheque.

On 31st March, 20X2 branch expenses amounting to Rs. 6,000 were outstanding and cash in hand was again Rs. 10,000. Furniture is subject to depreciation @ 16% per annum on diminishing balance method.

Prepare Branch Account in the books of head office for the year ended 31st March, 20X2.

Question 24 : Kanpur Branch

On 31st March, 20X2 Kanpur Branch submits the following Trial Balance to its Head Office at Lucknow :

Debit Balances	Rs. In lacs
Furniture and Equipment	18
Depreciation on furniture	2
Salaries	25
Rent	10
Advertising	6
Telephone, Postage and Stationery	3
Sundry Office Expenses	1
Stock on 1st April, 20X1	60
Goods Received from Head Office	288
Debtors	20
Cash at bank and in hand	8
Carriage Inwards	7
	448
Credit Balances	
Outstanding Expenses	3
Goods Returned to Head Office	5
Sales	360
Head Office	80
	448

Additional Information:

Stock on 31st March, 20X2 was valued at Rs. 62 lacs. On 29th March, 20X2 the Head Office dispatched goods costing Rs. 10 lacs to its branch. Branch did not receive these goods before 1st April, 20X2. Hence, the figure of goods received from Head Office does not include these goods. Also the head office has charged the branch Rs. 1 lac for centralized services for which the branch has not passed the entry.

You are required to:

(i) Pass Journal Entries in the books of the Branch to make the necessary adjustments

(ii) Prepare Final Accounts of the Branch including Balance Sheet, and

(iii) Pass Journal Entries in the books of the Head Office to incorporate the whole of the Branch Trial Balance.

Question 25 : The Washington branch of XYZ

The Washington branch of XYZ Mumbai sent the following trial balance as on 31st December, 20X1:

	$	$
Head office A/c	-	22,800

Sales	-	84,000
Debtors and creditors	4,800	3,400
Machinery	24,000	-
Cash at bank	1,200	-
Stock, 1 January, 20X1	11,200	-
Goods from H.O.	64,000	-
Expenses	5,000	-
	1,10,200	**1,10,200**

In the books of head office, the Branch A/c stood as follows:

Washington Branch A/c

	Rs.		Rs.
To Balance b/d	8,10,000	By Cash	28,76,000
To Goods sent to branch	29,26,000	By Balance c/d	8,60,000
	37,36,000		**37,36,000**

Goods are sent to the branch at cost plus 10% and the branch sells goods at invoice price plus 25%. Machinery was acquired on 31st January, 2007, when $ 1.00 = Rs. 40.

Rates of exchange were:

1st January, 20X1	$1.00	=	Rs.46
31st December, 20X1	$1.00	=	Rs.48
Average	$1.00	=	Rs.47

Machinery is depreciated @ 10% and the branch manager is entitled to a commission of 5% on the profits of the branch.

You are required to:

(i) Prepare the Branch Trading & Profit & Loss A/c in dollars.

(ii) Convert the Trial Balance of branch into Indian currency and prepare Branch Trading & Profit and Loss A/c and the Branch A/c in the books of head office.

MCQs :

1. If goods are invoiced to branches at cost, trading results of branch can be ascertained by
   (a) Debtors method. (b) Stock and debtors method.
   (c) Either (a) or (b). (d) Both (a) and (b).

2. Under branch trading and profit loss account method
   (a) H.O prepares profit and loss account.
   (b) Each branch is treated separate entity.
   (c) Both (a) and (b).
   (d) Either (a) or (b).

3. Goods may be invoiced to branch at
   (a) Cost or Selling price. (b) Wholesale price.
   (c) Both (a) and (b). (d) Either (a) or (b).
4. Under debtors method, opening balance of debtors is
   (a) Debited to branch account. (b) Credited to branch account.
   (c) Debited to H.O account. (d) Credited to H.O account.
5. Cost of goods returned by branch will have the following effect
   (a) Goods sent to branch account will be debited.
   (b) Branch stock account will be credited.
   (c) Both (a) and (b).
   (d) Either (a) or (b).

Thanks ....

About The Author

Rahul Malkan is a proficient faculty of Financial Reporting and Strategic Financial Management at CA Final level. He is an MBA in business financial. He has 20 years of experience in teaching industry and has authored 20 books in academics.

A good mentor for students and guides them to the path of success by assisting in other subjects as well.

: Follow us on :

rahulmalkan

: Address :

215, Ghanshyam Enclave, Off.Kandivali Link Road, Kandivali (West), Mumbai - 400 067.