

CA INTER

ADVANCED ACCOUNTING

“MUST DO QUESTIONS”

BEFORE EXAM

Total No. of Questions - 192

Compiled by CA. Jai Chawwla

Telegram Channel	
Download All Free Resources (From VSmart App) • Handwritten Concepts Notes • MCQs • Additional Questions and Amendements • Study Planner • 3 Mints Revision Shorts	<u>Android</u>  <u>Ios</u> 

INDEX

Sr. No.	Chapter Name	Page No.	No. of Questions
1.	FRAMEWORK	4	5
2.	FINANCIAL STATEMENTS	8	4
3.	CASH FLOW STATEMENT (AS 3)	20	6
4.	BUYBACK OF SECURITIES	32	4
5.	RECONSTRUCTION OF COMPANIES	43	5
6.	AMALGAMATION OF COMPANIES (AS 14)	56	12
7.	CONSOLIDATION (AS 21)	92	9
8.	BRANCH ACCOUNTS	112	11
9.	Introduction and Applicability of AS	128	1
10.	AS 1 – DISCLOSURE OF ACCOUNTING POLICIES	129	3
11.	AS 2 - Valuation of Inventory	132	5
12.	AS 10 - Property, Plant & Equipment	137	9
13.	AS 13 - Accounting for Investments	146	6
14.	AS 16 - Borrowing Costs	157	7
15.	AS 19 – Leases	163	6
16.	AS 26 - Intangible Assets	168	5
17.	AS 28 - Impairment of Assets	172	6
18.	AS 5 – NP for the Period, Prior Period Items & Changes in Accounting Policies	178	8
19.	AS 9 - Revenue Recognition	183	8
20.	AS 4 - Contingencies & Events Occurring after the Balance Sheet Date	189	5
21.	AS 7 - Construction Contracts	193	4
22.	AS 11 - Effects Of Changes in Foreign Exchange Rates	196	5
23.	AS 12 - Accounting for Government Grants	200	6
24.	AS 15 – Employee Benefits	206	7
25.	AS 17 – Segment Reporting	212	5
26.	AS 18 - Related Party Disclosures	215	8
27.	AS 20 – Earnings Per Share	218	8
28.	AS 22 - Accounting For Taxes on Income	224	3

CA Intermediate**Advanced Accounts**

29.	AS 23 – Investment in Associates	233	3
30.	AS 24 – Discontinuing Operations	238	4
31.	AS 25 – Interim Financial Reporting	241	4
32.	AS 27 - Joint Ventures	244	3
33.	AS 29 – Provisions, Contingent Liabilities & Contingent Assets	250	9

1. FRAMEWORK

QUESTION 1: (Q.FRW.RMP.06(A) RTP Nov22; EXAM May19; EXAM Nov'20, EXAM JAN'25)

Summarised Balance Sheet of Cloth Trader as on 31.03.2017 is given below:

Liabilities	Amount (Rs.)	Assets	Amount (Rs.)
Proprietor's Capital	3,00,000	Fixed Assets	3,60,000
Profit & Loss Account	1,25,000	Closing Stock	1,50,000
10% Loan Account	2,10,000	Sundry Debtors	1,00,000
Sundry Creditors	50,000	Deferred Expenses	50,000
		Cash & Bank	25,000
	6,85,000		6,85,000

Additional Information is as follows:

- (1) The remaining life of fixed assets is 8 years. The pattern of use of the asset is even. The net realisable value of fixed assets on 31.03.2018 was Rs.3,25,000.
- (2) Purchases and Sales in 2017-18 amounted to Rs.22,50,000 and Rs.27,50,000 respectively.
- (3) The cost and net realizable value of stock on 31.03.2018 were Rs.2,00,000 and Rs.2,50,000 respectively.
- (4) Expenses for the year amounted to Rs.78,000.
- (5) Deferred Expenses are amortized equally over 5 years.
- (6) Sundry Debtors on 31.03.2018 are Rs.1,50,000 of which Rs.5,000 is doubtful. Collection of another Rs.25,000 depends on successful re-installation of certain product supplied to the customer;
- (7) Closing Sundry Creditors are Rs.75,000, likely to be settled at 10% discount.
- (8) Cash balance as on 31.03.2018 is Rs.4,22,000.
- (9) There is an early repayment penalty for the loan of Rs.25,000.

You are required to prepare: (Not assuming going concern)

- (1) Profit & Loss Account for the year 2017-18.
- (2) Balance Sheet as on 31st March, 2018.

SOLUTION:

Profit and Loss Account for the year ended 2017-18(not assuming going concern)

Particulars	Amount	Particulars	Amount
To Opening Stock	1,50,000	By Sales	27,50,000
To Purchases	22,50,000	By Closing Stock	2,50,000
To Expenses*	78,000	By Trade payables	7,500
To Depreciation	35,000		
To Provision for doubtful debts	30,000		
To Deferred cost	50,000		
To Loan penalty	25,000		
To Net Profit (b.f.)	3,89,500		
	30,07,500		30,07,500

Balance Sheet as at 31st March, 2018 (not assuming going concern)

Liabilities	Amount Rs.	Assets	Amount Rs.
Capital	3,00,000	Fixed Assets	3,25,000
Profit & Loss A/c	5,14,500	Stock	2,50,000
10% Loan	2,35,000	Trade receivables (less provision)	1,20,000
Trade payables	67,500	Deferred costs	Nil
		Bank	4,22,000
	11,17,000		11,17,000

*Assumed that Rs.78,000 includes interest on 10% loan amount for the year.

QUESTION 2: –**Historical Cost Capital Maintenance**

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. Thus:

Opening Equity = Rs. 12,000 represented by 6,000 units at Rs. 2 per unit.

Closing Equity = Rs. 12,000 (Rs. 18,000 – Rs. 6,000) represented entirely by cash.

Retained Profit = Rs. 12,000 – Rs. 12,000 = Nil

The trader can start year 20X3 by purchasing 6,000 units at Rs. 2 per unit once again for selling them at Rs. 3 per unit. The whole process can repeat endlessly if there is no change in purchase price of the product.

QUESTION 3: –**Financial Capital Maintenance**

In the above question, suppose that the average price indices at the beginning and at the end of year are 100 and 120 respectively.

Opening Equity = Rs. 12,000 represented by 6,000 units at Rs. 2 per unit.

Opening equity at closing price = (Rs. 12,000 / 100) x 120 = Rs. 14,400 (6,000 x Rs. 2.40)

Closing Equity at closing price = Rs. 12,000 (Rs. 18,000 – Rs. 6,000) represented entirely by cash.

Retained Profit = Rs. 12,000 – Rs. 14,400 = (-) Rs. 2,400

The negative retained profit indicates that the trader has failed to maintain his capital. The available fund Rs. 12,000 is not sufficient to buy 6,000 units again at increased price Rs. 2.40 per unit. In fact, he should have restricted his drawings to Rs. 3,600 (Rs. 6,000 – Rs. 2,400).

Had the trader withdrawn Rs. 3,600 instead of Rs. 6,000, he would have left with Rs. 14,400, the fund required to buy 6,000 units at Rs. 2.40 per unit.

QUESTION 4: –**Physical Capital Maintenance**

In the above Question 2, suppose that the price of the product at the end of year is 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 Rs. 12,000 is not sufficient to buy 6,000 units again at increased price 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.

Capital maintenance can be computed under all three bases as shown below:

Financial Capital Maintenance at historical costs

	Rs	Rs
Closing capital (At historical cost)		12,000
Less: Capital to be maintained		
Opening capital (At historical cost)	12,000	
Introduction (At historical cost)	Nil	(12,000)
Retained profit		Nil

Financial Capital Maintenance at current purchasing power

	Rs	Rs
Closing capital (At closing price)		12,000
Less: Capital to be maintained		
Opening capital (At closing price)	14,400	
Introduction (At closing price)	Nil	(14,400)
Retained profit		(2,400)

Physical Capital Maintenance

	Rs	Rs
Closing capital (At current cost)		12,000
Less: Capital to be maintained		
Opening capital (At current cost)	15,000	
Introduction (At current cost)	Nil	(15,000)
Retained profit		(3,000)

QUESTION 5: (Q.FR.W.RMP.08A) (RTP MAY'26)

Giant Ltd. has entered into a binding agreement with Tiny Ltd. to buy a custom-made machine of ₹ 1,00,000 at the end of 2024-25, before delivery of the machine, Giant Ltd. had to change its method of production. The new method will not require the machine ordered and it will be scrapped after delivery. The expected scrap value is nil.

You are required to advise the accounting treatment and give necessary journal entry in the year 2024-25.

SOLUTION:

A liability is recognized when outflow of economic resources in settlement of a present obligation can be anticipated and the value of outflow can be reliably measured.

When flow of economic benefit to the enterprise beyond the current accounting period is considered improbable, the expenditure incurred is recognised as an expense rather than as an asset.

In the given case, Giant Ltd. should recognise a liability of ₹1,00,000 to Tiny Ltd.

Also, the flow of future economic benefit from the machine to the enterprise is improbable.

Thus, the entire amount of purchase price of the machine should be recognised as an expense.

Journal Entries

Loss on Change in Production Method	Dr	1,00,000	
To Tiny Ltd.			1,00,000
(Being loss due to change in production method)			
Profit & Loss A/c	Dr	1,00,000	
To Loss on Change in Production Method			1,00,000
(Being loss transferred to P&L)			

2. PREPARATION OF FINANCIAL STATEMENTS

QUESTION 6: – (Q.FS.RMP.01(A) (Exam May'24) (Dividend Declaration)

Following information are available in respect of Z Limited as on 31st March, 2024

- | | |
|--|---------------|
| 1. Equity shares of Rs. 100 each | Rs. 500 lakhs |
| 2. General reserve | Rs. 100 lakhs |
| 3. Loss for the year ending 31 st March, 2024 | Rs. 5 lakhs |

Due to absence of profits during the year 2023 – 24, the management recommends to declare dividend of 10% on equity share capital out of general reserve.

The rates of equity dividend for the last 5 years immediately preceding the year 2023 – 24 are as following:

2022-23	2021-22	2020-21	2019-20	2018-19
12%	14%	10%	10%	7%

As an accountant of the company, you are required to suggest whether the recommendation of the management is justified? If, you do not agree, then suggest the rate of dividend.

SOLUTION

In case of declaration of dividend out of free reserves, there are 3 conditions:

- (1) Dividend Rate < Average Rate of last 3 years $10\% < 12\% [(12+14+10)/3]$
Condition is Satisfied
- (2) Dividend Distributed < 10% of PUSC + Reserve and Surplus $50,00,000 < 59,50,000$
 $[(5,00,00,000 + 1,00,00,000 - 5,00,000) \times 10\%]$
Condition is Satisfied
- (3) Reserves after dividend > 15% of PUSC $45,00,000$ not > $75,00,000$ ($5,00,00,000 \times 15\%$)
Condition is Not Satisfied
- (4) The closing balance of reserves after payment of dividend and set off of loss = ₹ $75,00,000$

Therefore, can be utilized = $20,00,000$ ($1,00,00,000 - 5,00,000 - 75,00,000$) Thus, rate of dividend = $(20,00,000 / 5,00,00,000) = 4\%$

Alternatively

To judge the recommendation of management, the satisfaction of all three conditions is to be checked:

- (1) Condition I
The proposed dividend of 10% is less than the average rate of dividend being 12% (i.e.) $(12+14+10) / 5 = 12\%$.
Hence, this condition is satisfied.
- (2) Condition II
Amount to be withdrawn.

10% dividend on Equity share capital	50,00,000
+ Loss of Current year	5,00,000
Amount to be drawn from General Reserve	55,00,000

Maximum amount that can be withdrawn should not exceed 10% of paid-up share capital + free reserves.

$$= 10\% \text{ of } [₹ 500 \text{ lakhs} + ₹ 100 \text{ lakhs}] = ₹ 60,00,000$$

As the amount to be withdrawn is within the maximum limit, hence, this condition is also satisfied.

(3) Condition III

Balance of reserves after withdrawal (100-55) ₹ 45,00,000 15% of paid-up capital ₹ 75,00,000

As the balance of reserves should not be less than 15% of its paid-up share capital, but here the balance of reserves after withdrawal is less than 15% of paid-up share capital, hence this condition is not satisfied, hence, 10% dividend cannot be declared.

Maximum withdrawal of Reserve if condition II is satisfied.

Opening balance of Reserves in the beginning of the year = ₹ 1,00,00,000

- Closing balance of reserves being 15% of paid-up capital = ₹ 75,00,000

Reserves available = ₹ 25,00,000

Maximum permissible Divisible Profits

Permissible withdrawal as above = ₹ 25,00,000

Less: Current Year's Loss = ₹ 5,00,000

Maximum permissible Divisible profit = ₹ 20,00,000

Actual permissible rate of Dividend =

$$(₹ 20,00,000 / ₹ 5,00,00,000) \times 100 = 4\%$$

Therefore, the recommendation of management is not justified and a dividend only up to a rate of 4% can be declared.

QUESTION 7: – (Q.FS.SM.07(A))

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.	Cr.
	Rs	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

CA Intermediate**Advanced Accounts**

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	2,72,300	
Goodwill at cost	5,00,000	
General Reserve		<u>2,00,000</u>
	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.

SOLUTION

**Statement of Profit and Loss of International Hotels Ltd.
for the year ended 31st March, 20X2**

	Particulars	Notes	Amount
I.	Revenue from operations	9	1,79,700
II.	Other income	10	6,800
III.	Total Revenue (I + II)		1,86,500
IV.	Expenses:		
	Cost of materials consumed	11	25,060
	Purchases of Inventory-in-Trade	12	45,800
	Changes in inventories of finished goods work-in-progress and Inventory-in-Trade	13	(9,700)
	Employee benefits expense	14	29,580
	Other operating expenses	15	18,000
	Selling and administrative expenses	16	14,200
	Finance costs	17	12,000
	Depreciation and amortisation expense	18	21,315
	Other expense (preliminary expenses written off)		8,000
	Total expenses		1,64,255
V.	Profit (Loss) for the period (III - IV)		22,245

Balance Sheet of International Hotels Ltd. as on 31st March, 20X2

Particulars		Note No	Rs
EQUITY AND LIABILITIES			
1	Shareholders' funds		
	a Share capital	1	13,00,000
	b Reserves and Surplus	2	2,68,745
2	Non-current liabilities		
	a Long-term borrowings	3	2,00,000
3	Current liabilities		
	a Trade Receivables	4	42,000
	b Other current liabilities	5	13,280
Total			18,24,025
ASSETS			
1	Non-current assets		
	a PPE		
	I Tangible assets	6	9,14,985
	II Intangible assets (Goodwill)		5,00,000
	B Non-current investments		2,72,300
2	Current assets		
	A Inventories	7	38,900
	B Trade receivables		19,260
	C Cash and bank balances	8	78,580
Total			18,24,025

Notes to accounts

		Rs
1	Share Capital	
	Equity share capital	
	Authorised	
	10,000 Equity shares of Rs 100 each	10,00,000
	Issued & subscribed	
	8,000 Equity Shares of Rs 100 each	8,00,000
	Preference share capital	
	Authorised	
	5,000 6% Preference shares of Rs 100 each	5,00,000
	Issued & subscribed	
	5,000 6% Preference shares of Rs 100 each	5,00,000
	Total	13,00,000
2	Reserves and Surplus	
	Capital reserve [100 x (90 – 40)]	5,000
	General reserve	2,00,000
	Surplus (Profit & Loss A/c)	22,245
	Add: Balance from previous year	41,500
		63,745
	Total	2,68,745
3	Long-term borrowings	
	Secured	
	6% Debentures	2,00,000
	Total	2,00,000
4	Trade Receivables	42,000

5	Other current liabilities		
	Wages and Salaries Outstanding	1,280	
	Interest on debentures	12,000	13,280
	Total		13,280
6	Tangible assets		
	Freehold land & Buildings	8,50,000	
	Less: Depreciation	(17,000)	8,33,000
	Furniture and Fittings	86,300	
	Less: Depreciation	(4,315)	81,985
	Total		9,14,985
7	Inventories		
	Wines, Cigarettes & Cigars, etc.		22,500
	Foodstuffs		16,400
	Total		38,900
8	Cash and cash equivalents		
	Cash at bank		76,380
	Cash in hand		2,200
	Other bank balances		Nil
	Total		78,580
9	Revenue from operations		
	Sale of products		
	Wines, Cigarettes, Cigars etc.	68,400	
	Food	57,600	1,26,000
	Sale of services		
	Room Rent	48,000	
	Billiards	5,700	53,700
	Total		1,79,700
10	Other income		
	Transfer fees	700	
	Miscellaneous Receipts	2,800	
	Discount received	3,300	
	Total		6,800
11	Cost of materials consumed		
	Opening Inventory	5,260	
	Add: Purchases during the year	36,200	
	Less: Closing Inventory	(16,400)	25,060
	Total		25,060
12	Purchases of Inventory-in-Trade		
	Wines, Cigarettes etc.		45,800
	Total		45,800
13	Changes in inventories of finished goods work-in-progress and Inventory-in-Trade		
	Wines, Cigarettes etc.		
	Opening Inventory	12,800	
	Less: Closing Inventory	(22,500)	(9,700)
	Total		(9,700)
14	Employee benefits expense		
	Wages and Salaries	28,300	
	Add: Wages and Salaries Outstanding	1,280	29,580
	Total		29,580
15	Other operating expenses		
	Rent, Rates and Taxes		8,900
	Coal and Firewood		3,290

	Laundry		750
	Carriage and Cooliage		810
	Repairs		4,250
	Total		18,000
16	Selling and administrative expenses		
	Advertising		8,360
	Sundry Expenses		5,840
	Total		14,200
17	Finance costs		
	Interest on Debentures (2,00,000 x 6%)	12,000	
	Total		12,000
18	Depreciation and amortisation expense		
	Land and Buildings (8,50,000 x 2%)	17,000	
	Furniture & Fittings (86,300 x 5%)	4,315	
	Total		21,315

QUESTION 8: – (Q.FS.RMP.09(A) RTP May'18 & May'24, MTP Nov'20 & May'22)

Kapil Ltd. has authorized capital of Rs. 50 lakhs divided into 5,00,000 equity shares of Rs. 10 each. Their books show the following balances as on 31st March, 2017:

	Rs		Rs
Inventory 1.4.2016	6,65,000	Bank Current Account	20,000
Discounts & Rebates allowed	30,000	Cash in hand	8,000
Carriage Inwards	57,500	Interest (bank overdraft)	1,11,000
Patterns (Tangible Asset)	3,75,000	Calls in Arrear @ Rs 2 per share	10,000
Rate, Taxes and Insurance	55,000	Equity shares capital	20,00,000
Furniture & Fixtures	1,50,000	(2,00,000 shares of Rs. 10 each)	
Purchases	12,32,500	Bank Overdraft	12,67,000
Wages	13,68,000	Trade Payables (for goods)	2,40,500
Freehold Land	16,25,000	Sales	36,17,000
Plant & Machinery	7,50,000	Rent (Cr.)	30,000
Engineering Tools	1,50,000	Transfer fees received	6,500
Trade Receivables	4,00,500	Profit & Loss A/c (Cr.)	67,000
Advertisement	15,000	Repairs to Building	56,500
Commission & Brokerage	67,500	Bad debts	25,500
Business Expenses	56,000		

The inventory (valued at cost or market value, which is lower) as on 31st March, 2017 was Rs. 7,08,000. Outstanding liabilities for wages Rs. 25,000 and business expenses Rs. 36,000. Dividend declared @ 12% on paid-up capital and it was decided to transfer to reserve @ 2.5% of profits.

Charge depreciation on closing written down amount of Plant & Machinery @ 5%, Engineering Tools @ 20%; Patterns @ 10%; and Furniture & Fixtures @ 10%. Provide 25,000 as doubtful debts after writing off Rs. 16,000 as bad debts. Provide for income tax @ 30%.

You are required to prepare Statement of Profit & Loss for the year ended 31st March, 2017 and Balance Sheet as on that date.

SOLUTION

Kapil Ltd. Balance Sheet as at 31st March, 2017

Particulars		Note No.	(Rs)
I	Equity and Liabilities		
(1)	Shareholders' Funds		
(a) Share Capital		1	19,90,000

(b) Reserves and Surplus	2	3,47,000
(2) Current Liabilities		
(a) Trade Payables		2,40,500
(b) Short Term Borrowings	3	12,67,000
(b) Other Current Liabilities	4	61,000
(c) Short-Term Provisions	5	1,20,000
Total		40,25,500
II ASSETS		
(1) Non-Current Assets		
(a) Fixed Assets		
(i) Tangible Assets	5	29,30,000
(2) Current Assets		
(a) Inventories		7,08,000
(b) Trade Receivables	6	3,59,500
(c) Cash and Cash Equivalents	7	28,000
Total		40,25,500

Kapil Ltd. Statement of Profit and Loss for the year ended 31st March, 2017

	Particulars	Note No.	(Rs)
I	Revenue from Operations		36,17,000
II	Other Income	8	36,500
III	Total Revenue [I + II]		36,53,500
IV Expenses:			
	Cost of purchases		12,32,500
	Changes in Inventories [6,65,000-7,08,000]		(43,000)
	Employee Benefits Expenses	9	13,93,000
	Finance Costs	10	1,11,000
	Depreciation and Amortization Expenses		1,20,000
	Other Expenses	11	4,40,000
	Total Expenses		32,53,500
V	Profit before Tax (III-IV)		4,00,000
VI	Tax Expenses @ 30%		(1,20,000)
VII	Profit for the period		2,80,000

Notes to Accounts:**1. Share Capital**

Authorized Capital	
5,00,000 Equity Shares of Rs. 10 each	50,00,000
Issued Capital	
2,00,000 Equity Shares of Rs. 10 each	20,00,000
Subscribed Capital and fully paid	
1,95,000 Equity Shares of Rs. 10 each	19,50,000
Subscribed Capital but not fully paid	
5,000 Equity Shares of Rs. 10 each Rs. 8 paid	40,000
(Call unpaid Rs. 10,000)	19,90,000

2. Reserves and Surplus

General Reserve		7,000
Surplus i.e., Balance in Statement of Profit & Loss:		
Opening Balance	67,000	
Add: Profit for the period	2,80,000	
Less: Transfer to Reserve @ 2.5%	(7,000)	3,40,000
		3,47,000

3. Short Term Borrowings

Bank Overdraft	12,67,000
	12,67,000

4. Other Current Liabilities

Outstanding Expenses [25,000+36,000]	61,000
	61,000

5. Short-term Provisions

Provision for Tax	1,20,000
	1,20,000

6. Tangible Assets

Particulars	Value given (Rs)	Depreciation rate	Depreciation Charged (Rs)	Written down value at the end (Rs)
Land	16,25,000		-	16,25,000
Plant & Machinery	7,50,000	5%	37,500	7,12,500
Furniture & Fixtures	1,50,000	10%	15,000	1,35,000
Patterns	3,75,000	10%	37,500	3,37,500
Engineering Tools	1,50,000	20%	30,000	1,20,000
	30,50,000		1,20,000	29,30,000

7. Trade Receivables

Trade receivables (4,00,500-16,000)	3,84,500
Less: Provision for doubtful debts	(25,000)
	3,59,500

8. Cash & Cash Equivalent

Cash Balance	8,000
Bank Balance in current A/c	20,000
	28,000

9. Other Income

Miscellaneous Income (Transfer fees)	6,500
Rental Income	30,000
	36,500

10. Employee benefits expenses

Wages	13,68,000
Add: Outstanding wages	25,000
	13,93,000

11. Finance Cost

Interest on Bank overdraft	1,11,000
----------------------------	----------

12. Other Expenses

Carriage Inward	57,500
Discount & Rebates	30,000
Advertisement	15,000
Rate, Taxes and Insurance	55,000
Repairs to Buildings	56,500
Commission & Brokerage	67,500
Miscellaneous Expenses [56,000+36,000] (Business Expenses)	92,000
Bad Debts [25,500+16,000]	41,500
Provision for Doubtful Debts	<u>25,000</u>
	4,40,000

QUESTION 9: – (Q.FS.RMP 13(A) EXAM July'21)

The following is the Trial Balance of H Ltd., as on 31st March, 2021:

	Dr.	Cr.
Equity Capital (Shares of Rs. 100 each)		8,05,000
5,000, 6% preference shares of Rs. 100 each		5,00,000
9% Debentures		4,00,000
General Reserve		40,00,000
Profit & Loss A/c (of previous year)		72,000
Sales		60,00,000
Trade Payables		10,40,000
Provision for Depreciation on Plant & Machinery		1,72,000
Suspense Account		40,000
Land at cost	24,00,000	
Plant & Machinery at cost	7,70,000	
Trade Receivables	19,60,000	
Inventories (31-03-2021)	9,50,000	
Bank	2,30,900	
Adjusted Purchases	22,32,100	
Factory Expenses	15,00,000	
Administration Expenses	3,00,000	
Selling Expenses	14,00,000	
Debenture Interest	36,000	
Goodwill	12,50,000	
	1,30,29,000	1,30,29,000

Additional Information:

- (i) The authorised share capital of the company is: Rs.
5,000, 6% preference shares of Rs. 100 each 5,00,000
10,000, equity shares of Rs. 100 each 10,00,000

Issued equity capital as on 1st April 2020 stood at Rs. 7,20,000, that is 6,000 shares fully paid and 2,000 shares of Rs. 60 paid. The directors made a call of Rs. 40 per share on 1st October 2020. 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.

- (ii) On 31st March 2021, the Directors declared a dividend of 5% on equity shares, transferring any amount that may be required from General Reserve. Ignore Taxation.

- (iii) The company on the advice of independent valuer wishes to revalue the land at Rs. 36,00,000.

*This should have been given as 31.3.2021.

- (iv) Suspense account of Rs. 40,000 represents amount received for the sale of some of the

machinery on 1-4-2020. The cost of the machinery was Rs. 1,00,000 and the accumulated depreciation thereon being Rs. 30,000.

(v) Depreciation is to be provided on plant and machinery at 10% on cost.

(vi) Amortize 1/5th of Goodwill.

You are required to prepare H Limited's Balance Sheet as on 31-3-2021 and Statement of Profit and Loss with notes to accounts for the year ended 31-3-2021 as per Schedule III of the Companies Act, 2013. Ignore previous years' figures & taxation.

SOLUTION

H Ltd

Balance Sheet as at 31st March 2021

Particulars	Note No	Amount in Rs.
Equity and Liabilities		
I. Shareholders' Funds		
a. Share Capital	1	13,00,000
b. Reserves and Surplus	2	53,91,900
II. Non-Current Liabilities		
a. Long Term Borrowings	3	4,00,000
III. Current Liabilities		
a. Trade Payables	4	10,40,000
b. Other Current Liabilities	5	70,000
Total		82,01,900
Assets		
I. Non-Current Assets		
a. Property, Plant and Equipment	6	40,61,000
b. Intangible Assets	7	10,00,000
II. Current Assets		
a. Inventories		9,50,000
b. Trade Receivables		19,60,000
c. Cash and Cash equivalents		2,30,900
Total		82,01,900

Statement of Profit and Loss for the year ended 31st March 2021

Particulars	Note No	Amount in Rs.
I. Revenue from operations		
Total Revenue		60,00,000
II. Expenses		
Purchases (adjusted)		22,32,100
Finance Costs	8	36,000
Depreciation and Amortization	9	3,17,000
Other Expenses	10	32,30,000
Total Expenses		58,15,100
III. Profit/(Loss) for the period		1,84,900

Notes to Accounts**(Amount in Rs.)**

1	Share Capital		
	a. Authorized Capital		
	5,000, 6% Preference shares of Rs. 100/- each		5,00,000
	10,000 Equity Shares of Rs. 100/- each		10,00,000
	b. Issued & Subscribed Capital		15,00,000
	5,000, 6% Preference shares of Rs. 100/- each		5,00,000
	8,000, Equity shares of Rs. 100/- each		8,00,000
	Total		13,00,000
2	Reserves & Surplus		
	Capital Reserve (100 X (90-40))		5,000
	Revaluation Reserve (36,00,000-24,00,000)		12,00,000
	General Reserve		40,00,000
	Surplus	1,84,900	
	Add: Balance from previous year	72,000	
	Less: Dividends declared	(70,000)	
	Profit/(Loss) carried forward to Balance Sheet		1,86,900
	Total		53,91,900
3	Long-Term Borrowings		
	Secured		
	9% Debentures		4,00,000
4	Trade Payables		10,40,000
5	Other Current Liabilities		
	Dividend Payable		
	Preference Dividend		30,000
	Equity Dividend		40,000
	Total		70,000
6	Property, Plant and Equipment		
	Land		
	Opening balance		24,00,000
	Add: Revaluation Adjustment		12,00,000
	Closing Balance		36,00,000
	Plant and Machinery		
	Opening Balance		7,70,000
	Less: Disposed off		(1,00,000)
	Depreciation		(2,09,000)
	Closing Balance		4,61,000
	Total		40,61,000
7	Intangible Assets		
	Goodwill		12,50,000
	Less: Amortized (1/5th)		(2,50,000)
	Total		10,00,000
8	Finance Costs		

	Debenture Interest		36,000
9	Depreciation and Amortization		
	Plant and Machinery		67,000
	Goodwill		2,50,000
	Total		3,17,000
10	Other Expenses		
	Factory Expenses		15,00,000
	Selling Expenses		14,00,000
	Administrative Expenses		3,00,000
	Loss on sale of Plant and Machinery		
	Book Value (1,00,000-30,000)	70,000	
	Less: Sale Value	(40,000)	30,000
	Total		32,30,000

Note:

1. The inventories (31.3.20) amounting Rs. 9,50,000 (given in the trial balance of the question) should have been as closing inventory i.e., as on 31.3.21. In the above solution, this inventory has been considered as closing inventory i.e., for 31.3.21. If this is considered as inventory of 31.3.20, the closing inventory (as on 31.3.21) will not be available for the balance sheet as on 31.3.21 and in that case, the balance sheet will not tally without using suspense account amounting Rs. 9,50,000.
2. The financial statements given in the above answer include adjustment for dividend declared on 31st March, 2021, strictly, as per the information given in the question. However, practically dividends are declared in the annual general meetings which take place after the reporting date.

3. CASH FLOW STATEMENT (AS 3)

QUESTION 10: (Q.CFS.SM.202(A))

Prepare Cash flow for Gamma Ltd., for the year ending 31.3.20X1 from the following information:

- (1) Sales for the year amounted to Rs135 crores out of which 60% was cash sales.
- (2) Purchases for the year amounted to Rs55 crores out of which credit purchase was 80%.
- (3) Administrative and selling expenses amounted to Rs18 crores and salary paid amounted to Rs 22 crores.
- (4) The Company redeemed debentures of Rs20 crores at a premium of 10%. Debenture holders were issued equity shares of Rs15 crores towards redemption and the balance was paid in cash. Debenture interest paid during the year was Rs1.5 crores.
- (5) Dividend paid during the year amounted to Rs11.7 crores (including Dividend distribution tax) was also paid.
- (6) Investment costing Rs12 crores were sold at a profit of Rs2.4 crores.
- (7) Rs8 crores was paid towards income tax during the year.
- (8) A new plant costing Rs21 crores was purchased in part exchange of an old plant. The book value of the old plant was Rs12 crores but the vendor took over the old plant at a value of Rs10 crores only. The balance was paid in cash to the vendor.
- (9) The following balances are also provided:

	Rs in crores 1.4.20X0	Rs in crores 31.3.20X1
Debtors	45	50
Creditors	21	23
Bank	6	

SOLUTION

Gamma Ltd.

Cash Flow Statement for the year ended 31st March, 20X1 (Using direct method)

Particulars	Rs in crores	Rs in crores
<u>CASH FLOWS FROM OPERATING ACTIVITIES</u>		
Cash sales (60% of 135)	81	
Cash receipts from Debtors [45+ (135x40%) - 50]	49	
Cash purchases (20% of 55)	(11)	
Cash payments to suppliers [21+(55x80%)23]	(42)	
Cash paid to employees	(22)	
Cash payments for overheads (Adm. and selling)	(18)	
Cash generated from operations	37	
Income tax paid	(8)	
Net cash generated from operating activities		29
<u>CASH FLOWS FROM INVESTING ACTIVITIES</u>		
Sale of investments (12+ 2.40)	14.4	
Payments for purchase of fixed assets (21 - 10)	(11)	
Net cash used in investing activities		3.4
<u>CASH FLOWS FROM FINANCING ACTIVITIES</u>		
Redemption of debentures (22-15)	(7)	
Interest paid	(1.5)	
Dividend paid	(11.7)	

Net cash used in financing activities		(20.2)
Net increase in cash		12.2
Cash at beginning of the period		6.0
Cash at end of the period		18.2

QUESTION 11: (Q.CFS.SM.306(A))

From the following Balance Sheet & information, prepare Cash Flow Statement of Ryan Ltd. by Indirect method for the year ended 31st March, 20X1:

Balance Sheet

	31stMarch, 20X1	31stMarch, 20X0
Liabilities		
Equity Share Capital	6,00,000	5,00,000
10% Redeemable Preference Share Capital	–	2,00,000
Capital Redemption Reserve	1,00,000	–
Capital Reserve	1,00,000	–
General Reserve	1,00,000	2,50,000
Profit and Loss Account	70,000	50,000
9% Debentures	2,00,000	–
Trade payables	1,15,000	1,10,000
Liabilities for Expenses	30,000	20,000
Provision for Taxation	95,000	60,000
Dividend payable	90,000	60,000
	15,00,000	12,50,000
	31st March,20X1	31st March,20X0
Assets		
Land and Building	1,50,000	2,00,000
Plant and Machinery	7,65,000	5,00,000
Investments	50,000	80,000
Inventory	95,000	90,000
Trade receivables	2,50,000	2,25,000
Cash and Bank	65,000	90,000
Voluntary Separation Payments	1,25,000	65,000
	15,00,000	12,50,000

Additional Information:

- A piece of land has been sold out for Rs 1,50,000 (Cost – Rs 1,20,000) and the balance land was revalued. Capital Reserve consisted of profit on sale and profit on revaluation.
 - On 1st April, 20X0 a plant was sold for Rs 90,000 (Original Cost – Rs 70,000 and W.D.V. – Rs 50,000) and Debentures worth Rs1 lakh was issued at par as part consideration for plant of Rs4.5 lakhs acquired.
 - Part of the investments (Cost – Rs 50,000) was sold for Rs 70,000.
 - Pre-acquisition dividend received Rs 5,000 was adjusted against cost of investment.
 - Directors have declared 15% dividend for the current year.
 - Voluntary separation cost of Rs 50,000 was adjusted against General Reserve.
 - Income-tax liability for the current year was estimated at Rs 1,35,000.
- Depreciation @ 15% has been written off from Plant account but no depreciation has been charged on Land and Building.

SOLUTION

Cash Flow Statement of Ryan Limited
For the year ended 31st March, 20X1

Particulars	Rs	
<u>CASH FLOW FROM OPERATING ACTIVITIES</u>		
Net Profit before taxation (W.N.1)	2,45,000	
Adjustment for		
Depreciation (W.N.3)	1,35,000	
Profit on sale of plant (W.N.3)	(40,000)	
Profit on sale of investments (W.N.3)	(20,000)	
Interest on debentures (W.N.4)	18,000	
Operating profit before working capital changes	3,38,000	
Increase in inventory	(5,000)	
Increase in trade receivables	(25,000)	
Increase in Trade payables	5,000	
Increase in accrued liabilities	10,000	
Extraordinary items	(1,10,000)	
Income taxes paid (W.N.8)	(1,00,000)	
Net cash generated from operating activities		1,13,000
<u>CASH FLOW FROM INVESTING ACTIVITIES</u>		
Proceeds from sale of land (W.N.2)	1,50,000	
Proceeds from sale of plant (W.N.3)	90,000	
Proceeds from sale of investments (W.N.4)	70,000	
Purchase of plant (W.N.3)	(3,50,000)	
Purchase of investments (W.N.4)	(25,000)	
Pre-acquisition dividend received (W.N.4)	5,000	
Net cash used in investing activities		(60,000)
<u>CASH FLOW FROM FINANCING ACTIVITIES</u>		
Proceeds from issue of equity shares (6,00,000 – 5,00,000)	1,00,000	
Proceeds from issue of debentures (2,00,000 – 1,00,000)	1,00,000	
Redemption of preference shares	(2,00,000)	
Dividends paid	(60,000)	
Interest paid on debentures	(18,000)	
Net cash used in financing activities		(78,000)
Net decrease in cash and cash equivalents		(25,000)
Cash and cash equivalents at the beginning of the year		90,000
Cash and Cash equivalents at the end of the year		65,000

Working Notes:

1. Net Profit before taxation

Particulars	Rs
Net profit before taxation	
Retained profit	1,00,000
Less: Balance as on 31.3.20X0	(50,000)
	20,000
Provision for taxation	1,35,000
Dividend payable	90,000
Net Profit before taxation	2,75,000

2. Land and Building Account

Particulars		Rs	Particulars		Rs
To	Balance b/d	2,00,000	By	Cash (Sale)	1,50,000
To	Capital reserve (Profit on sale)	30,000	By	Balance c/d	1,50,000
To	Capital reserve (Revaluation profit)	70,000			
		3,00,000			3,00,000

3. Plant and Machinery Account

Particulars		Rs	Particulars		Rs
To	Balance b/d	5,00,000	By	Cash (Sale)	90,000
To	Profit and loss account	40,000	By	Depreciation	1,35,000
To	Debentures	1,00,000	By	Balance c/d	7,65,000
To	Bank	3,50,000			
		9,90,000			9,90,000

4. Investments Account

Particulars		Rs	Particulars		Rs
To	Balance b/d	80,000	By	Cash (Sale)	70,000
To	Profit and loss account	20,000	By	Dividend (Pre acquisition)	5,000
To	Bank (Balancing figure)	25,000	To	Balance C/d	50,000
		125,000			125,000

5. Capital Reserve Account

Particulars		Rs	Particulars		Rs
To	Balance c/d	70,000	By	Profit on revaluation of land	70,000
		70,000			700,000

6. General Reserve Account

Particulars		Rs	Particulars		Rs
To	Capital redemption reserve	1,00,000	By	Balance b/d	2,50,000
To	Balance c/d	1,50,000			
		2,50,000			2,50,000

7. Dividend payable Account

Particulars		Rs	Particulars		Rs
To	Bank (Balancing figure)	1,50,000	By	Balance b/d	60,000
To	Balance c/d	-	By	Profit & loss account	90,000
		1,50,000			1,50,000

8. Provision for Taxation Account

Particulars		Rs	Particulars		Rs
To	Bank (Balancing figure)	1,00,000	By	balance b/d	60,000
To	Balance c/d	95,000	By	Profit & loss account	1,35,000
		1,95,000			1,95,000

9. Other Current Assets Account

Particulars		Rs	Particulars		Rs
To	Balance b/d	65,000	By	Balance c/d	1,00,000
To	Bank (Balancing figure)	35,000			
		1,00,000			1,00,000

QUESTION 12: (Q.CFS.SM.308(A))

The Balance Sheet of New Light Ltd. for the years ended 31st March, 20X0 and 20X1 are as follows:

			Notes	31 st March, 20X0 (Rs.)	31 st March, 20X1 (Rs.)
		Equity and liabilities			
1		Shareholders' funds			
	A	Share capital	1	16,00,000	18,80,000
	B	Reserves and Surplus	2	8,40,000	11,00,000
2		Non-current liabilities			
	A	Long term borrowings	3	4,00,000	2,80,000
3		Current liabilities			
	A	Other current liabilities	4	6,00,000	5,20,000
	B	Short term provision (Provision for tax)		3,60,000	3,40,000
		Total		38,00,000	41,20,000
		Assets			
1		non-current assets			
	A	Property, plant and Equipment	5	22,80,000	26,40,000
	B	Non-Current investment		4,00,000	3,20,000
2		Current assets			
	A	Cash and Cash equivalents		10,000	10,000
	B	Inventory		2,16,000	3,00,000
	C	Other current assets		8,94,000	8,50,000
		Total		38,00,000	41,20,000

Notes to accounts

No.	Particular	31 st March, 20X0	31 st March, 20X1
1	Share capital		
	Equity share capital	12,00,000	16,00,000
	10% Preference share capital	4,00,000	2,80,000
	Total	16,00,000	18,80,000
2	Reserves and Surplus		
	General reserve	6,00,000	7,60,000
	Profit and Loss account	2,40,000	3,40,000
	Total	8,40,000	11,00,000
3	Long term borrowings		
	9% Debentures	4,00,000	2,80,000
	Total	4,00,000	2,80,000
4	Other current liabilities		
	Dividend payable	1,20,000	-
	Current Liabilities	4,80,000	5,20,000
	Total	6,00,000	5,20,000
5	Property, plant and equipment		
	Property, plant and equipment	32,00,000	38,00,000
	Less: Depreciation	(9,20,000)	(11,60,000)
	Net carrying value	22,80,000	26,40,000

Additional information:

- The company sold one fixed asset for Rs 1,00,000, the cost of which was Rs 2,00,000 and the depreciation provided on it was Rs 80,000.
- The company also decided to write off another fixed asset costing Rs 56,000 on which depreciation amounting to Rs 40,000 has been provided.

- (iii) Depreciation on fixed assets provided Rs 3,60,000.
- (iv) Company sold some investment at a profit of Rs 40,000.
- (v) Debentures and preference share capital redeemed at 5% premium. Debentures were redeemed at the year end.
- (vi) Company decided to value inventory at cost, whereas previously the practice was to value inventory at cost less 10%. The inventory according to books on 31.3.20X0 was Rs 2,16,000. The inventory on 31.3.20X1 was correctly valued at Rs. 3,00,000.

Prepare Cash Flow Statement as per revised Accounting Standard 3 by indirect method.

SOLUTION

New Light Ltd.

Cash Flow Statement for the year ended 31st March, 20X1

A. Cash Flow from operating activities	Rs.
Profit after appropriation	
Increase in profit and loss A/c after inventory adjustment [Rs. 3,40,000 – (Rs. 2,40,000 + Rs. 24,000)]	76,000
Transfer to general reserve	1,60,000
Dividend payable	1,60,000
Provision for tax	3,40,000
Net profit before taxation and extraordinary Item	5,76,000
Adjustments for:	
Depreciation	3,60,000
Loss on sale of fixed assets	20,000
Decrease in value of fixed assets	16,000
Profit on sale of investment	(40,000)
Premium on redemption of preference share capital	6,000
Interest on debentures	36,000
Premium on redemption of debentures	6,000
Operating profit before working capital changes	9,80,000
Increase in current liabilities (Rs. 5,20,000 – Rs. 4,80,000)	40,000
Increase in other current assets [Rs. 11,50,000 – (Rs. 11,10,000 + Rs. 24,000)]	(16,000)
Cash generated from operations	10,04,000
Income taxes paid	(3,60,000)
Net Cash generated from operating activities	6,44,000
B. CASH FLOW FROM INVESTING ACTIVITIES	
Purchase of fixed assets (W.N.3)	(8,56,000)
Proceeds from sale of fixed assets (W.N.3)	1,00,000
Proceeds from sale of investments (W.N.2)	1,20,000
Net Cash from investing activities	(6,36,000)
C. CASH FLOW FROM FINANCING ACTIVITIES	
Proceeds from issuance of share capital	4,00,000
Redemption of preference share capital (Rs. 1,20,000 + Rs. 6,000)	(1,26,000)
Redemption of debentures (Rs. 1,20,000 + Rs. 6,000)	(1,26,000)
Dividend paid	(1,20,000)
Interest on debentures	(36,000)
Net Cash from financing activities	(8,000)
Net increase/decrease in cash and cash equivalent during the year	Nil
Cash and cash equivalent at the beginning of the year	10,000
Cash and cash equivalent at the end of the year	10,000

Working Notes:

1. Revaluation of inventory will increase opening inventory by Rs. 24,000. $2,16,000/90 \times 100 = \text{Rs. } 24,000$

Therefore, opening balance of other current assets would be as follows:

Rs. 11,10,000 + Rs. 24,000 = Rs. 11,34,000

Due to under valuation of inventory, the opening balance of profit and loss account be increased by Rs. 24,000.

The opening balance of profit and loss account after revaluation of inventory will be Rs. 2,40,000 + Rs. 24,000 = Rs. 2,64,000

2. Investment Account

Particulars	Rs	Particulars	Rs
To Balance b/d	4,00,000	By Bank A/c	1,20,000
To Capital reserve A/c (Profit on sale of investment)	40,000	(balancing figure being investment sold)	
		By Balance c/d	3,20,000
	4,40,000		4,40,000

3. Fixed Assets Account

Particulars	Rs	Particulars	Rs
To Balance b/d	32,00,000	By Bank A/c (sale of assets)	1,00,000
To Bank A/c (Balancing figure being assets purchased)	8,56,000	By Accumulated depreciation A/c	80,000
		By Profit and loss A/c (loss on sale of assets)	20,000
		By Accumulated depreciation A/c	40,000
		By Profit and loss A/c (assets written off)	16,000
		By Balance c/d	38,00,000
	40,56,000		40,56,000

4. Accumulated Depreciation Account

Particulars	Rs	Particulars	Rs
To Fixed assets A/c	80,000	By Balance b/d	9,20,000
To Fixed assets A/c	40,000	By Profit and loss A/c (depreciation for the period)	3,60,000
To Balance c/d	11,60,000		
	12,80,000		12,80,000

ICAI's View on Preference Dividend: Preference Dividend is not declared on Balance Sheet date because it is not shown as payable on Closing Balance sheet. Hence, if not declared from P&L then must not be paid and to be ignored.

Alternate View: If it is cumulative Preference Share Capital, dividend must have been declared & already paid on 31/3

(a) Added to CFOA since declared out of P&L.

(b) Deduct from Financing Activity since Paid in cash.

QUESTION 13: – (Q.CFS.RMP.311(A) EXAM Jan21) (Similar to Q310)

The following information was extracted from the books of S Ltd. for the year ended 31.03.2020.

- (1) Net profit before taking into account income tax and after taking into account the following items was Rs. 30 Lakhs
 - (a) Depreciation on Property, Plant and Equipment Rs. 7,00,000
 - (b) Discount on issue of debentures written off Rs. 45,000
 - (c) Interest on debentures paid Rs. 4,35,000
 - (d) Investment of Book value Rs. 3,50,000 sold for 3,75,000
 - (e) Interest received on investments Rs.70,000
- (2) Income tax paid during the year Rs.12,80,000
- (3) The company issued 60,000 equity shares of Rs. 10 each at a premium of 20% on 10.04.2019
- (4) 20,000 9% Preference Shares of Rs. 100 were redeemed on 31st March 2020 at a premium of 5%
- (5) Dividend paid during the year amounted to Rs. 11,00,000 (Including dividend distribution tax)
- (6) A new plant costing 7 Lakhs was purchased in part exchange of an old plant on 1st January 2020. The book value of the old plant was Rs. 8 Lakhs but the vendor took over the old plant at a value of Rs. 6 Lakhs only. The balance amount was paid to vendor through cheque on 30th March 2020.
- (7) Company decided to value inventory at cost, whereas previously the practice was to value inventory at cost less 10%. The inventory according to books on 31.03.2020 was 14,76,000. The Inventory on 31.03.2019 was correctly valued at Rs. 13,50,000
- (8) Current assets and current liabilities in the beginning and at the end of the years 2019-2020 were as:

	As on 01.04.2019	As on 31.03.2020
	Rs.	Rs.
Inventory	13,50,000	14,76,000
Trade Receivables	3,27,000	3,13,200
Cash in Hand	2,40,700	3,70,500
Trade payables	2,84,700	2,87,300
Outstanding expenses	97,000	1,01,400

You are required to prepare a Cash Flow Statement for the year ended 31st March 2020 as per AS 3 (revised) using the indirect method.

SOLUTION**S Ltd.****Cash Flow Statement for the year ended 31st March, 2020**

Cash flows from operating activities		
Net profit before taxation*		30,00,000
Adjustments for:		
Depreciation on PPE	7,00,000	
Discount on debentures	45,000	
Profit on sale of investments	(25,000)	
Interest income on investments	(70,000)	
Interest on debentures	4,35,000	
Stock adjustment	1,64,000	
{14,76,000 less 16,40,000(14,76,000/90X100)}		
Operating profit before working capital change		12,49,000
Changes in working capital		42,49,000
(Excluding cash and bank balance):		
Less: Increase in inventory	(2,90,000)	

{16,40,000(14,76,000/90X100) less 13,50,000}		
Add: Decrease in Trade receivables	13,800	
Increase in trade payables	2,600	
Increase in o/s expenses	4,400	(2,69,200)
Cash generated from operations		39,79,800
Less: Income taxes paid		(12,80,000)
Net cash generated from operating activities		26,99,800
Cash flows from investing activities		
Sale of investments	3,75,000	
Interest received	70,000	
Payments for purchase of fixed assets (7,00,000 – 6,00,000)	(1,00,000)	
Net cash used in investing activities		3,45,000
Cash flows from financing activities		
Redemption of Preference shares	(21,00,000)	
Issue of shares	7,20,000	
Interest paid	(4,35,000)	
Dividend paid	(11,00,000)	
Net cash used in financing activities		(29,15,000)
Net increase in cash		1,29,800
Cash at beginning of the period		2,40,700
Cash at end of the period		3,70,500

*Net profit given in the question is after considering only the items listed as information point (1) of the question; hence amount of loss on plant not added back

QUESTION 14: (Q.CFS.SM.401(A))

Given below is the Statement of Profit and Loss of ABC Ltd. and relevant Balance Sheet information:

Extract of Balance sheet

		Particular	Notes	31.3.20X1 (Rs. In lakhs)	31.3.20X0 (Rs. In lakhs)
		Equity and Liabilities			
1		Current liabilities			
	A	Trade Payables		250	230
	B	Short term Provisions	1	200	180
	C	Other current liabilities	2	70	50
		Assets			
1		Current assets			
	A	Inventories		200	180
	B	Trade Receivable		400	250
	C	Other current assets	3	195	180

Statement of Profit and Loss of ABC Ltd. for the year ended 31st March, 20X1

	Particulars	Notes	Rs. In lakhs
I	Revenue from operations		4,150
II	Other income	4	100
III	Total income (I + II)		4250
	Expenses:		
	Purchase on Stock-in-Trade		2,400

	Change in inventories of finished goods		(20)
	Employee benefits expense		800
	Depreciation expense		100
	Finance cost	5	60
	Other expenses		200
IV	Total expenses		3,540
V	Profit before tax (III -IV)		710
VI	Tax expense:		
	Current tax		200
VII	Profit for the year from continuing operations		510

Appropriations

Balance of profit and loss account brought forward	50
Transfer to general reserve	200
Dividend paid	330

Notes to accounts:

		20X1 (Rs. In lakhs)	20X0 (Rs. In lakhs)
1	Short term provision		
	Provision for tax	200	180
2	Other current liabilities		
	Outstanding wages	50	40
	Outstanding expenses	20	10
	Total	70	50
3	Other current assets:		
	Advance tax	195	180
4	Other income:		
	Interest and dividend	100	
5	Finance cost:		
	Interest	60	

Compute cash flow from operating activities using both direct and indirect method.

SOLUTION**By direct method****Computation of Cash Flow from Operating Activities**

Particulars	Rs in lakhs	Rs in lakhs
Cash Receipts:		
Cash sales and collection from Trade receivables		
Sales + Opening Trade receivables – Closing Trade receivables (A)	4,150+250-400	4,000
Cash payments:		
Cash purchases & payment to Trade payables Purchases + Opening Trade payables – Closing Trade payables	2,400+230-250	2,380
Wages and salaries paid	800+40-50	790
Cash expenses	200+10-20	190
Taxes paid – Advance tax		195
(B)		3,555
Cash flow from operating activities (A – B)		445

By Indirect Method
Computation of Cash Flow from Operating Activities

	Rs in lakhs	Rs in lakhs
By Indirect method		
Profit before tax		710
Add: Non-cash items: Depreciation		100
Add: Interest: Financing cash outflow		60
Less: Interest and Dividend: Investment cash inflow		(100)
Less: Tax paid		(195)
Working capital adjustments		
Trade receivables	250-400 = (150)	
Inventories	180-200 = (20)	
Trade payables	250-230 = 20	
Outstanding wages	50-40 = 10	
Outstanding expenses	20-10 = 10	(130)
Cash flow from operating activities		445

QUESTION 15: (Q.CFS.SM.302(B))

From the following Balance Sheets of Mr. Zen, prepare a Cash flow statement as per AS-3 for the year ended 31.3.20X1:

Balance Sheets of Mr. Zen

Liabilities	As on 1.4.20X0	As on 1.4.20X1
	Rs	Rs
Zen's Capital A/c	10,00,000	12,24,000
Trade payables	3,20,000	3,52,000
Mrs. Zen's loan	2,00,000	--
Loan from Bank	<u>3,20,000</u>	<u>4,00,000</u>
	<u>18,40,000</u>	<u>19,76,000</u>
Assets		
Land	6,00,000	8,80,000
Plant and Machinery	6,40,000	4,40,000
Inventories	2,80,000	2,00,000
Trade receivables	2,40,000	4,00,000
Cash	<u>80,000</u>	<u>56,000</u>
	<u>18,40,000</u>	<u>19,76,000</u>

Additional information:

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.

SOLUTION

Cash Flow Statement of Mr. Zen as per AS 3
for the year ended 31.3.20X1

Particulars	Rs
(i) CASH FLOW FROM OPERATING ACTIVITIES	
Net Profit (given)	3,60,000
Adjustments for	
Depreciation on Plant & Machinery (W.N.2)	1,44,000
Loss on Sale of Machinery (W.N.1)	16,000
Operating Profit before working capital changes	5,20,000
Decrease in inventories	80,000

Increase in trade receivables	(1,60,000)	
Increase in trade payables	32,000	(48,000)
Net cash generated from operating activities		4,72,000
(ii) CASH FLOW FROM INVESTING ACTIVITIES		
Sale of Machinery (W.N.1)	40,000	
Purchase of Land (8,80,000 – 6,00,000)	(2,80,000)	
Net cash used in investing activities		(2,40,000)
(iii) CASH FLOW FROM FINANCING ACTIVITIES		
Repayment of Mrs. Zen's Loan	(2,00,000)	
Drawings (W.N.3)	(1,36,000)	
Loan from Bank	80,000	
Net cash used in financing activities		(2,56,000)
Net decrease in cash		(24,000)
Opening balance as on 1.4.20X0		80,000
Cash balance as on 31.3.20X1		56,000

Working Notes:**1. Plant & Machinery A/c**

Particulars	Rs	Particulars	Rs
To Balance b/d (6,40,000 + 2,00,000)	8,40,000	By Cash – Sales	40,000
		By Provision for Depreciation A/c	24,000
		By Profit & Loss A/c – Loss on Sale (80,000 – 64,000)	16,000
		By Balance c/d (4,40,000+3,20,000)	7,60,000
	8,40,000		8,40,000

2. Provision for depreciation on Plant and Machinery A/c

Particulars	Rs	Particulars	Rs
To Plant and Machinery A/c	24,000	By Balance b/d	2,00,000
To Balance c/d	3,20,000	By Profit & Loss A/c (Bal. fig.)	1,44,000
	3,44,000		3,44,000

3. To find out Mr. Zen's drawings:

Particulars	Rs
Opening Capital	10,00,000
Add: Net Profit	3,60,000
	13,60,000
Less: Closing Capital	(12,24,000)
Drawings	1,36,000

4. BUYBACK OF SECURITIES

QUESTION 16: (Q.BB.RMP.204(A) MTP Oct'20) (Buyback & Redemption)

The following was the summarized balance sheet of Bhoomi Ltd. as on 31st March, 2020:

Equity & liability	Rs. (In lakhs)	Assets	Rs. (In lakhs)
Authorised Capital:		Property, plant and equipment	1,12,000
Equity shares of Rs. 10 each	80,000	Investments	24,000
Issued Capital		Cash at Bank	13,200
Equity Shares of Rs.10 each Fully Paid up	64,000	Trade Receivables	66,000
10% Redeemable Preference Shares of 10 each, Fully Paid Up	20,000		
Reserves & Surplus:			
Capital Redemption Reserve	8,000		
Securities Premium	6,400		
General Reserve	48,000		
Profit & Loss Account	2,400		
9% Debentures	40,000		
Trade Payables	26,400		
	2,15,200		2,15,200

On 1st April, 2020 the Company **redeemed all its Preference Shares** at a Premium of 10% and bought back 25% of its Equity Shares at Rs.20 per Share. In order to make Cash available, the Company sold all the Investments for Rs. 25,000 Lakhs and raised a Bank Loan amounting to Rs.16,000 lakh on the Security of the Company's Plant.

Give the necessary Journal Entries considering that the buyback is authorized by the articles of company and necessary resolution is passed by the company for this. The amount of Securities premium may be utilized to the maximum extent allowed by law.

SOLUTION:

Journal entries In the books of Bhoomi Ltd.

			Dr.	Cr.
			Rs. in lakhs	
1	Bank A/c	Dr.	25,000	
	To Investments A/c			24,000
	To Profit and Loss A/c			1,000
	(Being Investments sold and, profit being credited to Profit and Loss Account)			
2	10% Redeemable Preference Share Capital A/c	Dr.	20,000	
	Premium payable on Redemption of Preference Shares A/c	Dr.	2,000	
	To Preference Shareholders A/c			22,000
	(Being amount payable on redemption of Preference shares, at a Premium of 10%)			

CA Intermediate		Advanced Accounts		
3	Securities Premium A/c	Dr.	2,000	
	To Premium payable on Redemption of Preference Shares A/c			2,000
	(Being Securities Premium utilised to provide Premium on Redemption of Preference Shares)			
4	Equity Share Capital A/c	Dr.	16,000	
	Premium payable on Buyback A/c	Dr.	16,000	
	To Equity Share buy back A/c			32,000
	(Being the amount due on buy-back)			
5	Securities Premium A/c (6,400 – 2,000)	Dr.	4,400	
	General Reserve A/c (balancing figure)	Dr.	11,600	
	To Premium payable on Buyback A/c			16,000
	(Being premium on buyback provided first out of Securities Premium and the balance out of General Reserves.)			
6	Bank A/c	Dr.	16,000	
	To Bank Loan A/c			16,000
	(Being Loan taken from Bank to finance Buyback)			
7	Preference Shareholders A/c	Dr.	22,000	
	Equity Shares buy back A/c	Dr.	32,000	
	To Bank A/c			54,000
	(Being payment made to Preference Shareholders and Equity Shareholders)			
	General Reserve Account	Dr.	36,000	
	To Capital Redemption Reserve Account			36,000
	(Being amount transferred to Capital Redemption Reserve Account to the extent of face value of preference shares redeemed and equity Shares bought back) (20,000 + 16,000)			

QUESTION 17: (Q.BB.RMP.206(A) EXAM Nov'19, RTP Nov'21) (Buyback & Bonus)

X Ltd. furnishes the following summarized Balance Sheet as at 31 -03-2018.

Liabilities	(in Rs)	(in Rs)
Share Capital		
Equity Share Capital of Rs 20 each fully paid up	50,00,000	
10,000, 10% Preference Shares of Rs 100 each fully paid up	<u>10,00,000</u>	60,00,000
Reserves & Surplus		
Capital Reserve	1,00,000	
Security Premium	12,00,000	
Revenue Reserve	5,00,000	
Profit and Loss	20,00,000	
Dividend Equalization Fund	<u>5,50,000</u>	43,50,000
Non-Current Liabilities		
12% Debenture		12,50,000
Current Liabilities and Provisions		<u>5,50,000</u>
Total		<u>1,21,50,000</u>
Assets		

Fixed Assets		
Tangible Assets		1,00,75,000
Current Assets		
Investment	3,00,000	
Inventory	2,00,000	
Cash and Bank	<u>15,75,000</u>	<u>20,75,000</u>
Total		<u>1,21,50,000</u>

The shareholders adopted the resolution on the date of the above-mentioned Balance Sheet to:

- (1) Buy back 25% of the paid-up capital and it was decided to offer a price of 20% over market price. The prevailing market value of the company's share is Rs 30 per share.
- (2) To finance the buy-back of shares, company:
 - (a) Issues 3000, 14% debentures of Rs 100 each at a premium of 20%.
 - (b) Issues 2500, 10% preference shares of Rs 100 each.
- (3) Sell investment worth Rs 1,00,000 for Rs 1,50,000.
- (4) Maintain a balance of Rs 2,00,000 in Revenue Reserve.
- (5) Later the company issue three fully paid-up equity share of Rs 20 each by way of **bonus share** for every 15-equity share held by the equity shareholders.

You are required to pass the necessary journal entries to record the above transactions and prepare Balance Sheet after buy back.

SOLUTION:

In the books of X Limited Journal Entries

	Particulars	Dr. Rs	Cr. Rs
1.	Bank A/c Dr.	3,60,000	
	To 14 % Debenture A/c		3,00,000
	To Securities Premium A/c		60,000
	(Being 14 % debentures issued to finance buy back)		
2.	Bank A/c Dr.	2,50,000	
	To 10% preference share capital A/c (Being 10% preference share issued to finance buy back)		2,50,000
3.	Bank A/c Dr.	1,50,000	
	To Investment A/c		1,00,000
	To Profit on sale of investment (Being investment sold on profit)		50,000
4.	Equity share capital A/c (62,500 x Rs 20) Dr.	12,50,000	
	Securities premium A/c (62,500 x Rs 16) Dr.	10,00,000	
	To Equity shares buy back A/c (62,500 x Rs36)		22,50,000
	(Being the amount due to equity shareholders on buy back)		
5.	Equity shares buy back A/c Dr.	22,50,000	
	To Bank A/c		22,50,000
	(Being the payment made on account of buyback of 62,500 Equity Shares as per the Companies Act)		
6.	Revenue reserve Dr.	3,00,000	

	Securities premium	Dr.	2,60,000	
	Profit and Loss A/c	Dr.	4,40,000	
	To Capital redemption reserve A/c*			10,00,000
	(Being amount equal to nominal value of buy back shares from free reserves transferred to capital redemption reserve account as per the law) [12,50,000 less 2,50,000]			
7.	Capital redemption reserve A/c	Dr.	7,50,000	
	To Bonus shares A/c (W.N.1) (Being the utilization of capital redemption reserve to issue 37,500 bonus shares)			7,50,000
8.	Bonus shares A/c	Dr.	7,50,000	
	To Equity share capital A/c			7,50,000
	(Being issue of 3 bonus equity share for every 15 equity shares held)			

*Alternatively, entry for combination of different amounts (from Revenue reserve, Securities premium and profit and Loss account.) may be passed for transferring the required amount to CRR.

Note: It may be noted that as per the provisions of the Companies Act, no buy-back of any kind of shares or other specified securities shall be made out of the proceeds of an earlier issue of the same kind of shares or same kind of other **specified securities**. Issue of debentures has been excluded for the purpose of “**specified securities**” and the entire amount of Rs 10,00,000 (after deducting only pref. share capital) has been credited to CRR while solving the question.

Balance Sheet (After buy back and issue of bonus shares)

Particulars	Note No	Amount Rs
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	57,50,000
(b) Reserves and Surplus	2	27,10,000
(2) Non-Current Liabilities		
(a) Long-term borrowings	3	15,50,000
(3) Current Liabilities		
(a) Trade payables		-
(b) current liabilities & Provisions		5,50,000
Total		1,05,60,000
II. Assets		
(1) Non-current assets		
(a) Property, Plant and Equipment		1,00,75,000
(2) Current assets		
(a) Investments		2,00,000
(b) Inventory		2,00,000
(c) Cash and cash equivalents (W.N. 2)		85,000
Total		1,05,60,000

Notes to Accounts

			Rs
1.	Share Capital		
	Equity share capital (Fully paid-up shares of Rs 20 each)		
	(2,50,000-62,500+37,500 shares)	45,00,000	
	10% preference shares @ Rs 100 each (10,00,000 + 2,50,000)	<u>12,50,000</u>	
2.	Reserves and Surplus		
	Capital Reserve	1,00,000	57,50,000
	Revenue reserve	2,00,000	
	Securities premium	12,00,000	
	Add: Premium on debenture	60,000	
	Less: Adjustment for premium paid on buy back (10,00,000)		
	Less: Transfer to CRR	<u>(2,60,000)</u>	Nil
	Capital Redemption Reserve		
	Transfer due to buy-back of shares from P&L 10,00,000		
	Less: Utilisation for issue of bonus shares <u>(7,50,000)</u>	2,50,000	
	Profit & Loss A/c	20,00,000	
	Add: Profit on sale of investment	50,000	
	Less: Transfer to CRR	<u>(4,40,000)</u>	16,10,000
	Dividend equalization reserve	<u>(5,50,000)</u>	<u>5,50,000</u>
	Long-term borrowings - 12% Debentures 12,50,000		
	- 14% Debentures	<u>3,00,000</u>	15,50,000

Working Notes:

- Amount of bonus shares = $[(2,50,000 - 25\%)3/15] \times 20 = 37,500 \times 20 = 7,50,000$
- Cash at bank after issue of bonus shares

	Rs
Cash balance as on 30.3.2018	15,75,000
Add: Issue of debenture	3,60,000
Add: issue of preference shares	2,50,000
Add: Sale of investments	<u>1,50,000</u>
	23,35,000
Less: Payment for buy back of shares	<u>(22,50,000)</u>
	<u>85,000</u>

QUESTION 18: (Q.BB.SM.207(A) Buyback, Redemption, ESOP, Investment in Own Debentures)

Extra Ltd. (a non-listed company) furnishes you with the following Balance Sheet as of 31st March, 20X1:

		(in lakhs ₹)		
		Particulars	Notes	₹
1		Equity and Liabilities		
		Shareholders' funds		
	A	Share capital	1	120
	B	Reserves and Surplus	2	118
2		Non-current liabilities		
		Long term borrowings	3	4
3		Current liabilities		
	A	Trade Payables		70
		Total		312
		Assets		
1		Non-current assets		
	A	Property, plant and Equipment		50
	B	Non-current Investments		120
2		Current assets		
	A	Cash and Cash equivalents		142
		Total		312

Notes to accounts

No.	Particulars	₹
1	Share Capital	
	Authorized, issued and subscribed capital:	
	Equity shares of ₹ 10 each fully paid	100
	9% Redeemable preference shares of ₹ 100 each fully paid	20
	Total	120
2	Reserves and Surplus	
	Capital reserves	8
	Revenue reserves	50
	Securities premium	60
	Total	118
3	Long term borrowings	
	10% Debentures	4

- The company **redeemed the preference shares** at a premium of 10% on 1st April, 20X1.
- It also bought back 3 lakhs equity shares of ₹ 10 each at ₹ 30 per share. The payment for the above was made out of huge bank balances.
- Included in its investment were "**investments in own debentures**" costing ₹ 2 lakhs (face value ₹ 2.20 lakhs). These debentures were cancelled on 1st April, 20X1.
- The company had 1,00,000 **equity stock options outstanding** on the above- mentioned date, to the employees at ₹ 20 when the market price was ₹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.

SOLUTION

Date	Particulars		Debit	Credit
20X1 1st April	9% Redeemable preference share capital A/c	Dr.	20.00	
	Premium on redemption of preference shares A/c	Dr.	2.00	
	To Preference shareholders A/c			22.00
	(Being preference share capital transferred to shareholders account)			
	Preference shareholders A/c	Dr.	22.00	
	To Bank A/c			22.00
	(Being payment made to shareholders)			
	Equity shares buy-back A/c	Dr.	90.00	
	To Bank A/c			90.00
	(Being 3 lakhs equity shares of ₹ 10 each bought back @ ₹ 30 per share)			
	Equity share capital A/c	Dr.	30.00	
	Securities premium A/c	Dr.	60.00	
	To Equity Shares buy-back A/c			90.00
	(Being cancellation of shares bought back)			
	Revenue reserve A/c	Dr.	50.00	
	To Capital redemption reserve A/c			50.00
	(Being creation of capital redemption reserve account to the extent of the face value of preference shares redeemed and equity shares bought back as per the law)			
	10% Debentures A/c	Dr.	2.20	
	To Investment (own debentures) A/c			2.00
	To Profit on cancellation of own debentures A/c			0.20
	(Being cancellation of own debentures costing ₹ 2 lakhs, face value being ₹ 2.20 lakhs and the balance being profit on cancellation of debentures)			
	Bank A/c	Dr.	10.00	
	Employees stock option outstanding (Current liabilities) A/c	Dr.	5.00	
	To Equity share capital A/c			5.00
	To Securities premium A/c			10.00
	(Being the allotment to employees, of 50,000 shares of ₹ 10 each at a premium of 20 per share in exercise of stock options by employees)			
	Securities premium A/c	Dr.	2.00	
	To Premium on redemption of preference shares A/c			2.00
	(Being premium on redemption of preference shares adjusted through securities premium)			

Balance Sheet of Extra Ltd. as at 01.04.20X1**(in lakhs ₹)**

Particulars		Notes	₹
1	Equity and Liabilities		
	Shareholders' funds		
	A Share capital	1	75.00
	B Reserves and Surplus	2	66.20
2	Non-current liabilities		
	Long term borrowings	3	1.80
3	Current liabilities		
	A Other Current Liabilities	4	65.00
	Total		208
	Assets		
1	Non-current assets		
	A Property, plant and Equipment		50.00
	B Non-current Investments	5	118.00
2	Current assets		
	A Cash and Cash equivalents	6	40.00
	Total		208

Notes to accounts

No.	Particulars		₹
1	Share Capital		
	Equity shares of ₹ 10 each fully paid		100
	Less: Cancellation of bought back shares		(30)
	Add: Shares issued against ESOP		5
	Total		75
2	Reserves and Surplus		
	Capital Reserve		
	Opening balance	8.00	
	Add: Profit on cancellation of debentures	0.20	8.20
	Revenue reserves		
	Opening balance	50.00	
	Less: Creation of Capital Redemption Reserve	(50.00)	-
	Securities Premium		
	Opening balance	60.00	
	Less: Adjustment for cancellation of equity shares	(60.00)	
	Less: Adjustment for premium on redemption of preference shares	(2.00)	
	Add: Shares issued against ESOP at premium	10.00	8.00
	Capital Redemption Reserve		50.00
	Total		66.20
3	Long term borrowings		
	10% Debentures		4.00
	Less: Cancellation of own debentures		(2.20)
	Total		1.80
4.	Other Current liabilities		
	Opening balance		70.00

	Less: Adjustment for ESOP outstanding		(5.00)
	Total		65.00
5.	Non-current investments		
	Opening balance		120.00
	Less: Investment in own debentures		(2.00)
	Total		118.00
6.	Cash and Cash Equivalents		
	Opening balance		142.00
	Less: Payment to preference shareholders		(22.00)
	Less: Payment to equity shareholders		(90.00)
	Add: Share price received against ESOP		10.00
	Total		40.00

QUESTION 19: (Q.BB.RMP.302(A) EXAM May'23)

VIJ Ltd. has the following Capital Structure as on 31st March, 2022:

Particulars	(₹ in Lakhs)
Equity Share Capital (Shares of ₹ 10 each, fully Paid)	990
Reserves & Surplus:	
General Reserve	720
Securities Premium Account	270
Profit & Loss Account	270
Infrastructure development Reserve	540
Loan Funds	5,400

On the recommendation of the Board of Directors, the shareholders of the company have approved on 2nd September, 2022 a proposal to buy-back the maximum permissible number of equity shares, considering the sufficient funds available at the disposal of the company.

The current market value of the company's shares is ₹ 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 rate.

You are also informed that the Infrastructure Development Reserve is created to satisfy income tax requirements.

You are required to compute the maximum permissible number of equity shares that can be brought back in the light of the above information and **also under a situation where the loan funds of the company were either ₹ 3,600 lakh or ₹ 4,500 lakh.**

The entire buy-back is completed by 09/12/2022, show the accounting entries with full narration in the company's books in each situation.

SOLUTION:**Statement determining the maximum number of shares to be bought back**

(Number of shares)

Particulars	When loan fund is		
	₹ 5,400 lakhs	₹ 3,600 lakhs	₹ 4,500 lakhs
Shares Outstanding Test (W.N.1)	24.75	24.75	24.75
Resources Test (W.N.2)	18.75	18.75	18.75
Debt Equity Ratio Test (W.N.3)	Nil	11.25	Nil
Maximum number of shares that can be bought back [least of the above]	Nil	11.25	Nil

Journal Entries for the Buy-Back
(applicable only when loan fund is ₹ 3,600 lakhs)

₹ in lakhs

	Particulars		Debit	Credit
(a)	Equity share capital account	Dr.	112.50	
	To Equity share buy- back account (Being cancellation of shares bought back)	Dr.	225.00	337.5
(b)	Equity share buy-back account	Dr.	337.50	
	To Bank account (Being buy-back of 11.25 lakhs equity shares of ₹10 each @ ₹30 per share)			337.5
(c)	General reserve account	Dr.	112.50	
	To Capital redemption reserve account (Being transfer of free reserves to capital redemption reserve to the extent of nominal value of share capital bought back out through free reserves)			112.50

Notes:

1. In place of entry (a), Alternative set of entries can be given as follows:

₹ in lakhs

Equity share capital A/c	Dr.	112.50	
Premium payable on buy-back	Dr.	225.00	
To Equity shares buy-back A/c (Being the amount due on buy-back of equity shares)			337.50
Securities Premium A/c	Dr.		
To Premium payable on buy-back (Being premium payable on buy-back charged from Securities premium)		225.00	225.00

2. In place of entry (c), Alternative set of entries can be given as follows:

₹ in lakhs

Securities Premium A/c	Dr.	45.00	
General Reserve A/c	Dr.	67.50	
To Capital redemption reserve A/c (Being transfer of free reserves to capital redemption reserve to the extent of nominal value of share capital bought back out through free reserves)			112.50

Working Notes:**1. Shares Outstanding Test**

Particulars	(Shares in lakhs)
Number of shares outstanding	99
25% of the shares outstanding	24.75

2. Resource Test

Particulars	
Paid up capital (₹ in lakhs)	990
Free reserves (₹ in lakhs) (720+270+270)	<u>1260</u>
Shareholders' funds (₹ in lakhs)	<u>2250</u>
25% of Shareholders fund (₹ in lakhs)	₹562.5 lakhs
Buy-back price per share	₹ 30
Number of shares that can be bought back (shares in lakhs)	18.75 lakhs shares

3. Debt Equity Ratio Test

	Particulars	When loan fund is		
		₹ 5,400 lakhs	₹ 3,600 lakhs	₹ 4,500 lakhs
(a)	Loan funds (₹ in lakhs)	5,400	3,600	4,500
(b)	Minimum equity to be maintained after buyback in the ratio of 2:1 (₹ in lakhs)	2,700	1,800	2,250
(c)	Present equity shareholders fund (₹ in lakhs)	2,250	2,250	2,250
(d)	Future equity shareholder fund (₹ in lakhs)	N.A	2137.5 (2,250-112.5)	N.A.
(e)	Maximum permitted buy-back of Equity (₹ in lakhs)	Nil	337.5 (by simultaneous equation)	Nil
(f)	[(d) – (b)] ¹ Maximum number of shares that can be bought back @ ₹30 per share (shares in lakhs) (See Working Note)	Nil	11.25 (by simultaneous equation)	Nil

Under Situations 1 & 3 the company does not qualify for buy-back of shares as per the provisions of the Companies Act, 2013.

Working Note:

Suppose No. of Shares to be bought back is 'x' and if face value of each share is 10/- then:

- Face Value of Buyback shares is 10x
- CRR to be Created due to buyback equal to face value is 10x
- Premium on Buyback is 20x (30/- buyback price less Face Value 10/-)
- Therefore, total impact of Buyback on Current Equity would be 40x

Situation 2:

Present Equity – Impact of Buyback on Equity = Minimum Equity to be maintained

$$2250 - 40x = 1800$$

X = 11.25 lakhs Numbers of Buyback Shares

5. ACCOUNTING FOR RECONSTRUCTION OF COMPANIES

QUESTION 20: (EXAM SEP'25) (JAMMU & PUNJAB)

Following is the Balance Sheet of Ellora Limited as at 31st March, 2025:

Particulars	Note	Amount (₹)
Equity and Liabilities		
Shareholders Funds		
Share Capital	1	46,00,000
Reserves and Surplus	2	(21,40,000)
Non-current Liabilities		
Long Term borrowings	3	15,00,000
Current Liabilities		
Trade Payables		12,00,000
Short Term Borrowings- Bank Overdraft		7,80,000
Other Current Liabilities	4	4,90,000
Short Term Provisions- Provision for Taxation		4,00,000
Total		68,30,000
Assets		
Non-current Assets		
Property, Plant and Equipment	5	23,00,000
Intangible Assets	6	6,70,000
Non-current Investments	7	2,20,000
Current Assets		
Inventories		17,00,000
Trade Receivables		19,40,000
Total		68,30,000

Notes to Accounts

	Particulars	Amount (₹)
1	Share Capital	
	Equity Share Capital	
	3,00,000 Equity Shares of ₹ 10/- each, fully paid up	30,00,000
	Preference Share Capital	
	16,000 6% Cumulative Preference Shares of ₹ 100/- each, fully paid up	16,00,000
	Total	46,00,000
2	Reserves and Surplus	
	Debit balance of Profit and Loss Account	(21,40,000)
3	Long Term Borrowings	
	Secured	
	6% Debentures(secured on the freehold property)	15,00,000
4	Other Current Liabilities	
	Loan from Directors	4,00,000
	Interest Payable on Debentures	90,000
	Total	4,90,000
5	Property, Plant and Equipment	

CA Intermediate		Advanced Accounts
	Freehold Property	17,00,000
	Plant and Machinery	6,00,000
	Total	23,00,000
6	Intangible Assets	
	Goodwill	5,20,000
	Patents and Trademarks	1,50,000
	Total	6,70,000
7	Non-current Investments	
	Investments in Marketable Securities - valued at Cost (Market Value 5,40,000/-)	2,20,000

Due to continued losses and liquidity constraints, it was decided to reconstruct the company. The following scheme of internal reconstruction was approved by the shareholders and sanctioned by the Tribunal:

1. The Equity Shares shall be written down to Rs. 2/- each and the Preference Shares shall be written down to ₹ 75/-each.
2. Of the Preference Shares' Dividends which are in arrears for four years, the Preference Shareholders have agreed to forego their claim for arrears of dividends for three years and accept allotment of Equity Shares of 2/-each towards dividend for the fourth year.
3. Interest payable on Debentures is paid in cash.
4. The Debenture holders have agreed to take over freehold property, book value 4,00,000/- at a valuation of 4,80,000/- in part repayment of their holdings. Besides they have agreed to provide additional funds of 5,20,000/- secured by a floating charge on the company's assets at an interest rate of 9%.
5. Inventory is to be written down by ₹ 2,60,000/-
6. Provision for bad and doubtful debts is to be created for 2,74,000/-
7. Intangible Assets and Debit balance of Profit and Loss Account are to be written off.
8. The remaining freehold property after giving to Debenture holders is to be revalued at 15,50,000/-
9. The Non-current Investments are sold off for ₹ 5,60,000/-
10. A contingent liability of ₹ 1,00,000/- is payable, which has arisen due to the wrong action of one of the Directors. He has agreed to compensate this loss out of the loan given by him to the company. For the remaining loan of 3,00,000/-, the Directors have agreed to accept a cash payment of 20,000/- and allotment of 1,30,000 Equity Shares of 2/- each in full settlement.
11. There is a capital commitment of 10,00,000/-, The contract is cancelled on payment of 5% of the contract price as a penalty.
12. The company issued 2,00,000 new Equity shares of ₹ 2/- each at par, payable in full on allotment. The issue was underwritten for a commission of 5%. Shares were fully taken up.
13. The taxation liability of the company is settled at 3,00,000/- and the same is paid immediately.
14. The expenses of reconstruction amounted to 15,000/-.

You are required to:

- (a) Pass the Journal Entries to record the above transactions (including cash transactions) in the books of the company.
- (b) Prepare Capital Reduction Account.

SOLUTION

QUESTION 21: (Q.IR.SM.209(A) Removed from ICAI New Syllabus Material)

Repair Ltd. is in the hands of a receiver for debenture holders who holds a charge on all assets except uncalled capital. The following statement shows the position as regards creditors as on 30th June, 20X1:

	₹
Property, plant and equipment (Cost ₹ 3,90,000) - estimated at	1,50,000
Cash in hand of the receiver	2,70,000
Charged under debentures	4,20,000
Uncalled capital	1,80,000
Deficiency	7,50,000
6,000 shares of ₹ 60 each, ₹ 30 paid up	1,80,000
First debentures	3,00,000
Second debentures	6,00,000
Unsecured trade payables	4,50,000

A holds the first debentures for Rs. 3,00,000 and second debentures for Rs. 3,00,000. He is also an unsecured creditor for Rs. 90,000. B holds second debentures for Rs. 3,00,000 and is an unsecured trade payables for Rs. 60,000. The following scheme of reconstruction is proposed:

1. A is to cancel Rs. 2,10,000 of the total debt owing to him, to bring Rs. 30,000 in cash and to take first debentures (in cancellation of those already issued to him) for Rs. 5,10,000 in satisfaction of all his claims.
2. B is to accept Rs. 90,000 in cash in satisfaction of all claims by him.
3. In full settlement of 75% of the claim, unsecured creditors (other than A and B) agreed to accept four shares of Rs. 7.50 each, fully paid against their claim for each share of Rs. 60. The balance of 25% is to be postponed and to be payable at the end of three years from the date of Court's approval of the scheme. The nominal share capital is to be increased accordingly.
4. Uncalled capital is to be called up in full and Rs. 52.50 per share cancelled, thus making the shares of Rs. 7.50 each.

Assuming that the scheme is duly approved by all parties interested and by the Court, give necessary journal entries.

SOLUTION:**Journal Entries**

Particulars		Debit	Credit
First debentures A/c	Dr.	3,00,000	
Second debentures A/c	Dr.	3,00,000	
Unsecured creditors A/c	Dr.	90,000	
To A's A/c			6,90,000
(Being A's total liability ascertained)			
A's A/c	Dr.	2,10,000	
To Capital reduction A/c			2,10,000
(Being cancellation of debt upto ₹ 2,10,000)			
Bank A/c	Dr.	30,000	
To A's A/c			30,000
(Being cash received in course of settlement)			
A's A/c	Dr.	5,10,000	
To First debentures A/c			5,10,000

(Being liability of A, discharged against first debentures)			
Second debentures A/c Dr.	3,00,000		
Unsecured creditors A/c Dr.	60,000		
To B's A/c			3,60,000
(Being B's liability ascertained)			
B's A/c Dr.	3,60,000		
To Bank A/c			90,000
To Capital reduction A/c			2,70,000
(Being B's liability discharged)			
Unsecured trade payables A/c Dr.	3,00,000		
To Equity share capital A/c			1,12,500
To Loan (Unsecured) A/c			75,000
To Capital reduction A/c			1,12,500
(Being settlement of unsecured creditors)			
Share call A/c Dr.	1,80,000		
To Share capital A/c			1,80,000
(Being final call money due)			
Bank A/c Dr.	1,80,000		
To Share call A/c			1,80,000
(Being final call money received)			
Share capital A/c (Face value ₹ 60) Dr.	3,60,000		
To Share capital (Face value ₹ 7.50)			45,000
To Capital reduction A/c			3,15,000
(Being share capital reduced to ₹ 7.50 each)			
Capital reduction A/c Dr.	9,07,500		
To Profit and loss A/c			8,70,000
To Capital Reserve			37,500
(Being reconstruction surplus used to write off losses and balance transfer to capital reserve)			

Working Notes:

1.	Settlement of claim of remaining unsecured creditors	₹
	75% of ₹ 3,00,000	2,25,000
	Considering their claim for share of ₹ 60 each	
	$2,25,000 / 60 = 3,750$ shares	
	Less: Number of shares to be issued	
	$3,750 \times 4 = 15,000$ shares of ₹ 7.5 each	
	Total value = $15,000 \times 7.50$	(1,12,500)
	Transferred to Capital reduction A/c	<u>1,12,500</u>

2. Ascertainment of profit and loss account's debit balance at the time of reconstruction.

	₹	₹
Asset		
Fixed assets	3,90,000	
Cash	<u>2,70,000</u>	6,60,000
<i>Less: Capital & Liabilities:</i>		
Share capital	1,80,000	
1 st Debenture	3,00,000	
2 nd Debenture	6,00,000	
Unsecured trade payables	<u>4,50,000</u>	<u>(15,30,000)</u>
Profit and loss A/c (Debit balance)		<u>(8,70,000)</u>

QUESTION 22: (Q.IR.RMP.2010(A) RTP Nov18, Nov20 & May22)

The summarized balance sheet of Z Limited as on 31st March, 2017 is as under:

Particulars	Amount in Rs.
Share Capital:	
5,00,000 Equity shares of Rs. 10 each fully paid up	50,00,000
9%, 20,000 Preference shares of Rs. 100 each fully paid up	20,00,000
Reserves and Surplus:	
Profit and Loss Account (Dr. balance)	14,60,000
Non-Current Liabilities:	
10% Secured Debentures	16,00,000
Current Liabilities:	
Interest due on Debentures	1,60,000
Trade Payables	5,00,000
Loan from Directors	1,00,000
Bank Overdraft	1,00,000
Provision for Tax	1,00,000
Non-Current Assets:	
Property, plant and Equipment:	
Land & Buildings	30,00,000
Plant & Machinery	12,50,000
Furniture & Fixtures	2,50,000
Intangible Assets:	
Goodwill	11,00,000
Patents	5,00,000
Current Assets:	
Trade Investments	5,00,000
Trade Receivables	5,00,000
Inventory	10,00,000

Note: Preference dividend is in arrears for last 2 years.

Mr. Y holds 60% of debentures and Mr. Z holds 40% of debentures. Moreover Rs. 1,00,000 and Rs. 60,000 were also payable to Mr. Y and Mr. Z respectively as trade payable.

The following scheme of reconstruction has been agreed upon and duly approved.

- (i) All the equity shares to be converted into fully paid equity shares of Rs. 5.00 each.
- (ii) The Preference shares be reduced to Rs. 50 each and the preference shareholders agreed to forego their arrears of preference dividends, in consideration of which 9% preference shares are to be converted into 10% preference shares.
- (iii) Mr. Y and Mr. Z agreed to cancel 50% each of their respective total debt including interest on debentures. Mr. Y and Mr. Z also agreed to pay Rs. 1,00,000 and Rs. 60,000 respectively in cash and to receive new 12% debentures for the balance amount.
- (iv) Persons relating to trade payables, other than Mr. Y and Mr. Z also agreed to forgo their 50% claims.
- (v) Directors also waived 60% of their loans and accepted equity shares for the balance.
- (vi) Capital commitments of Rs. 3.00 lacs were cancelled on payment of Rs. 15,000 as penalty.
- (vii) Directors refunded Rs. 1,00,000 of the fees previously received by them.
- (viii) Reconstruction expenses paid Rs. 15,000.
- (ix) The taxation liability of the company was settled for Rs. 75,000 and was paid immediately.
- (x) The Assets were revalued as under:

Land and Building	32,00,000
Plant and Machinery	6,00,000
Inventory	7,50,000
Trade Receivables	4,00,000
Furniture and Fixtures	1,50,000
Trade Investments	4,50,000

You are required to prepare necessary journal entries for all the above-mentioned transactions including amounts to be written off of Goodwill, Patents, Loss in Profit and Loss account and Discount on issue of debentures. And also, prepare Bank Account and Reconstruction Account.

SOLUTION

Journal Entries in the Books of Z Ltd.

			Rs.	Rs.
(i)	Equity Share Capital (Rs. 10 each) A/c Dr. To Equity Share Capital (Rs. 5 each) A/c To Reconstruction A/c (Being conversion of 5,00,000 equity shares of Rs. 10 each fully paid into same number of fully paid equity shares of Rs. 5 each as per scheme of reconstruction.)		50,00,000	25,00,000 25,00,000
(ii)	9% Preference Share Capital (Rs. 100 each) A/c Dr. To 10% Preference Share Capital (Rs. 50 each) A/c To Reconstruction A/c (Being conversion of 9% preference share of Rs. 100 each into same number of 10% preference share of Rs. 50 each and claims of preference dividends settled as per scheme of reconstruction.)		20,00,000	10,00,000 10,00,000
(iii)	10% Secured Debentures A/c Dr. Trade payables A/c Dr. Interest on Debentures payable A/c Dr. Bank A/c Dr.		9,60,000 1,00,000 96,000 1,00,000	

CA Intermediate		Advanced Accounts	
	To 12% Debentures A/c		6,78,000
	To Reconstruction A/c		5,78,000
	(Being Rs. 11,56,000 due to Y (including trade payables) cancelled and 12% debentures allotted for the amount after waving 50% as per scheme of reconstruction.)		
(iv)	10% Secured Debentures A/c	Dr. 6,40,000	
	Trade Payables	Dr. 60,000	
	Interest on debentures payable A/c	Dr. 64,000	
	Bank A/c	Dr. 60,000	
	To 12% debentures A/c		4,42,000
	To Reconstruction A/c		3,82,000
	(Being Rs. 7,64,000 due to Z (including trade payables) cancelled and 12% debentures allotted for the amount after waving 50% as per scheme of reconstruction.)		
(v)	Trade payables A/c	Dr. 1,70,000	
	To Reconstruction A/c		1,70,000
	(Being remaining trade payables sacrificed 50% of their claim.)		
(vi)	Directors' Loan A/c	Dr. 1,00,000	
	To Equity Share Capital (Rs. 5) A/c		40,000
	To Reconstruction A/c		60,000
	(Being Directors' loan claim settled by issuing 8,000 equity shares of Rs. 5 each as per scheme of reconstruction.)		
(vii)	Reconstruction A/c	Dr. 15,000	
	To Bank A/c		15,000
	(Being payment made towards penalty of 5% for cancellation of capital commitments of Rs. 3 Lakhs.)		
(viii)	Bank A/c	Dr. 1,00,000	
	To Reconstruction A/c		1,00,000
	(Being refund of fees by directors credited to reconstruction A/c.)		
(ix)	Reconstruction A/c	Dr. 15,000	
	To Bank A/c		15,000
	(Being payment of reconstruction expenses.)		
(x)	Provision for Tax A/c	Dr. 1,00,000	
	To Bank A/c		75,000
	To Reconstruction A/c		25,000
	(Being payment of tax liability in full settlement against provision for tax)		
(xi)	Land and Building A/c	Dr. 2,00,000	
	To Reconstruction A/c		2,00,000
	(Being appreciation in value of Land & Building recorded)		
(xii)	Reconstruction A/c	Dr. 49,85,000	

CA Intermediate		Advanced Accounts	
	To Goodwill A/c		11,00,000
	To Patent A/c		5,00,000
	To Profit and Loss A/c		14,60,000
	To Plant and Machinery A/c		6,50,000
	To Furniture & Fixture A/c		1,00,000
	To Trade Investment A/c		50,000
	To Inventory A/c		2,50,000
	To Trade Receivables A/c		1,00,000
	To Capital Reserve (bal. fig.)		7,75,000
	(Being writing off of losses and reduction in the value of assets as per scheme of reconstruction, balance of reconstruction A/c transfer to Capital Reserve.)		

Bank Account

		Rs.			Rs.
To	Reconstruction (Y)	1,00,000	By	Balance b/d (overdraft)	1,00,000
To	Reconstruction(Z)	60,000	By	Reconstruction A/c	15,000
To	Reconstruction A/c (Refund of earlier fees by directors)	1,00,000		(Capital commitment penalty paid)	
		2,60,000	By	Reconstruction A/c (reconstruction expenses paid)	15,000
			By	Provision for tax A/c (tax paid)	75,000
			By	Balance c/d	55,000
					2,60,000

Reconstruction Account

		Rs.			Rs.
To	Bank (penalty)	15,000	By	Equity Share Capital A/c	25,00,000
To	Bank (Reconstruction expenses)	15,000	By	9% Pref. Share Capital A/c	10,00,000
To	Goodwill	11,00,000	By	Mr. Y (Settlement)	5,78,000
To	Patent	5,00,000	By	Mr. Z (Settlement)	3,82,000
To	P & L A/c	14,60,000	By	Trade Payables A/c	1,70,000
To	P & M	6,50,000	By	Director's loan	60,000
To	Furniture and Fixtures	1,00,000	By	Bank	1,00,000
To	Trade investment	50,000	By	Provision for tax	25,000
To	Inventory	2,50,000	By	Land and Building	2,00,000
To	Trade Receivables	1,00,000			
To	Capital Reserve (bal. fig.)	7,75,000			
		50,15,000			50,15,000

QUESTION 23: (Q.IR.RMP.211(A) MTP Oct20, May22)

The summarised Balance Sheet of Preeti Limited as on 31st March 2019, was as follows:

	(Rs.)
Authorized and subscribed capital:	
20,000 Equity shares of Rs. 100 each fully paid	20,00,000
Unsecured loans:	
15% Debentures	6,00,000
Interest payable thereon	90,000
Current Liabilities:	
Trade payables	1,04,000
Provision for income tax	72,000
Property, plant and equipment:	
Machineries	7,00,000
Current Assets:	
Inventory	5,06,000
Trade receivables	4,60,000
Bank	40,000
Profit & loss A/c (Dr.)	11,60,000

It was decided to reconstruct the company for which necessary resolution was passed and sanctions were obtained from the appropriate authorities. Accordingly, it was decided that:

- i) Each share be sub-divided into 10 fully paid up equity shares of Rs. 10 each.
- ii) After sub-division, each shareholder shall surrender to the company 50% of his holding for the purpose of reissue to debenture holders and trade payables as necessary.
- iii) Out of shares surrendered 20,000 shares of Rs. 10 each shall be converted into 10% Preference shares of Rs. 10 each fully paid up.
- iv) The claims of the debenture holders shall be reduced by 50%. In consideration of the reduction, the debenture holder shall receive Preference Shares of Rs. 2,00,000 which are converted out of shares surrendered.
- v) Trade payables claim shall be reduced by 25%. Remaining trade payables are to be settled by the issue of equity shares of Rs. 10 each out of shares surrendered.
- vi) Balance of Profit and Loss account to be written off.
- vii) The shares surrendered and not re-issued shall be cancelled.

Pass Journal Entries giving effect to the above.

SOLUTION:

Sr. No.	Particulars	Dr.	Cr.
1	Equity Share Capital A/c (Rs.10) Dr. To Share Surrender A/c To Equity Share Capital (Rs. 10) A/c (Sub-division of 20,000 equity shares of Rs. 100 each into 2,00,000 equity shares of Rs. 10 each and surrender of 1,00,000 of such sub-divided shares as per capital reduction scheme)	20,00,000	10,00,000 10,00,000
2	15% Debentures Account Dr. Interest payable A/c (proportionate 50%) Dr. To Reconstruction A/c	3,00,000 45,000	3,45,000

3	(Transferred 50% of the claims of the debenture holders to Reconstruction A/c in consideration of which 10% Preference shares are being issued, out of share surrender A/c as per capital reduction scheme)		
	Trade payables A/c Dr. To Reconstruction A/c	1,04,000	1,04,000
4	(Transferred claims of the trade payables to Reconstruction A/c, 25% of which is reduction and equity shares are issued in consideration of the balance amount)		
	Share Surrender A/c Dr. To 10% Preference Share Capital A/c To Equity Share Capital A/c To Reconstruction A/c	10,00,000	2,00,000 78,000 7,22,000
5	(Issued preference and equity shares to discharge the claims of the debenture holders and the trade payables respectively as per scheme and the balance in share surrender account is transferred to reconstruction account)		
	Reconstruction A/c Dr. To Profit & Loss A/c To Capital Reserve A/c 11,000 (Adjusted debit balance of profit and loss account against reconstruction account and the balance is transferred to Capital Reserve account)	11,71,000	11,60,000 11,000

Note: Alternative set of correct journal entries may be given for transfer of surrendered shares to trade payables and debenture holders.

QUESTION 24: (Q.IR.RMP.213(A) RTP May20)

The following is the Balance Sheet of Star Ltd. as on 31st March, 2019:

				Rs
A.	EQUITY & LIABILITIES			
	1.	Shareholders' Fund:		
		(a)	Share Capital:	
			9,000 7% Preference Shares of Rs 100 each fully paid	9,00,000
			10,000 Equity Shares of Rs 100 each fully paid	10,00,000
		(b)	Reserve & Surplus:	
			Profit & Loss Account	(2,00,000)
	2.	Non-current liabilities:		
			"A" 6% Debentures (Secured on Bombay Works)	3,00,000
			"B" 6% Debentures (Secured on Chennai Works)	3,50,000
	3.	Current Liabilities and Provisions:		
		(a)	Workmen's Compensation Fund:	
			Bombay Works	10,000
			Chennai Works	5,000
		(b)	Trade Payables	<u>1,25,000</u>
			TOTAL	<u>24,90,000</u>
B.	ASSETS:			
	Non-current Assets:			

	1. PPE:		
		Bombay Works	9,50,000
		Chennai Works	7,75,000
	2. Investment:		
		Investments for Workman's Compensation Fund	15,000
	3. Current Assets:		
	(a)	Inventories	4,50,000
	(b)	Trade Receivables	2,50,000
	(c)	Cash at Bank	50,000
		TOTAL	24,90,000

A reconstruction scheme was prepared and duly approved. The salient features of the scheme were as follows:

1. Paid up value of 7% Preference Share to be reduced to Rs 80, but the rate of dividend being raised to 9%.
2. Paid up value of Equity Shares to be reduced to Rs 10.
3. The directors to refund Rs 50,000 of the fees previously received by them.
4. Debenture holders forego their interest of Rs 26,000 which is included among the trade payables.
5. The preference shareholders agreed to waive their claims for preference share dividend, which is in arrears for the last three years.
6. "B" 6% Debenture holders agreed to take over the Chennai Works of Rs 4,25,000 and to accept an allotment of 1,500 equity shares of Rs 10 each at par, and upon their forming a company called Zia Ltd. (to take over the Chennai Works) they allotted 9,000 equity shares of Rs 10 each fully paid at par to Star Ltd.
7. The Chennai Workmen's compensation fund disclosed that there were actual liabilities of Rs 1,000 only. As a consequence, the investments of the fund were realized to the extent of the balance. Entire investments were sold at a profit of 10% on book value and the proceeds were utilized for part payment of the creditors.
8. Inventory was to be written off by Rs 1,90,000 and a provision for doubtful debts is to be made to the extent of Rs 20,000.
9. Chennai works completely written off.
10. Any balance of the Capital Reduction Account is to be applied as two-third to write off the value of Bombay Works and one-third to Capital Reserve.

Pass necessary Journal Entries in the books of Star Ltd. after the scheme has been carried into effect.

SOLUTION

In the books of Star Ltd.

Journal Entries

	Particulars	Amount Rs.	Amount Rs.
(i)	7% Preference share capital (Rs. 100) Dr. To 9% Preference share capital (Rs. 80) To Capital reduction A/c (Being preference shares reduced to Rs. 80 and also rate of dividend raised from 7% to 9%)	9,00,000	7,20,000 1,80,000
(ii)	Equity share capital A/c (Rs. 100 each) Dr. To Equity share capital A/c (Rs. 10 each) To Capital reduction A/c (Being reduction of nominal value of one share of Rs. 100 each to Rs. 10 each)	10,00,000	1,00,000 9,00,000
(iii)	Bank A/c Dr.	50,000	

	To Capital reduction A/c (Being directors refunded the fee amount)		50,000
(iv)	Trade payables A/c (Interest on debentures) Dr. To Capital reduction A/c (Being interest forgone by the debenture holders)	26,000	26,000
(v)	No entry required		
(vi) a	'B' 6% Debentures A/c Dr. To Debentures holders A/c (Being amount due to Debentures holders)	3,50,000	3,50,000
b	Debentures holders A/c Dr. To Chennai Works A/c To Equity share capital A/c (Being Chennai works taken over and equity shares issued to 'B' 6% Debenture holders)	4,40,000	4,25,000 15,000
c	Equity share of Zia Ltd. A/c Dr. To Debentures holders A/c (Being 9,000 equity shares of Zia Ltd. Issued by Debentures holders)	90,000	90,000
(vii) a	Chennai Works – Workmen Compensation Fund Dr. To Capital reduction A/c (Being difference due to reduced amount of actual liability transferred to capital reduction account)	4,000	4,000
b	Bank A/c Dr. To Investment for Workmen Compensation Fund To Capital reduction A/c (Being investment for Workmen Compensation Fund sold @ 10% profit)	15,400	14,000 1,400
c	Trade Payables A/c Dr. To Bank A/c (Being part payment made to trade payables)	15,400	15,400
(viii)	Capital reduction A/c Dr. To Provision for Doubtful Debts A/c To Inventory A/c (Being assets revalued)	2,10,000	20,000 1,90,000
(ix)	Capital reduction A/c Dr. To Profit & Loss A/c To PPE– Chennai Works (Being assets revalued and losses written off)	5,50,000	2,00,000 3,50,000*
(x)	Capital reduction A/c Dr. To PPE– Bombay Works To Capital reserve A/c (Being assets revalued and remaining amount transferred to capital reserve account)	4,01,400	2,67,600 1,33,800

6. AMALGAMATION OF COMPANIES

(AS 14)

QUESTION 25: (EXAM MAY'25)

The following is summarized Balance Sheet of Pickles Ltd. as on 31/03/2025.

		Particulars	Notes	₹
		Equity and Liabilities		
1		Shareholders Funds		
	A	Share Capital	1	11,00,000
	B	Reserves and Surplus	2	2,10,000
2		Non-Current liabilities		
	A	Long term borrowings	3	1,00,000
	B	Long term Provisions	4	60,000
3		Current liabilities		
	A	Trade Payables		1,75,000
	B	Other Current Liabilities		65,000
		Total		17,10,000
		Assets		
1		Non-current Assets		
	A	Property, Plant and Equipment	5	7,50,000
	B	Intangible assets	6	75,000
2		Current Assets		
	A	Inventories		5,25,000
	B	Trade receivables		3,00,000
	C	Cash and Cash equivalents		60,000
		Total		17,10,000

Notes to Accounts

		₹
1	Share Capital	
	6,000 Equity Shares of ₹ 100 each	6,00,000
	5,000 6% Preference Shares of ₹ 100 each	5,00,000
		11,00,000
2	Reserves and Surplus	
	General reserve	1,00,000
	Profit and Loss account	1,10,000
		2,10,000
3	Long term borrowings	
	8% Debentures	1,00,000
4	Long term Provisions	
	Retirement Gratuity Fund	60,000
5	Property, Plant and Equipment	
	Land and Building	3,50,000
	Plant and Machinery	3,00,000
	Furniture and Fittings	1,00,000
		7,50,000

6	Intangible Assets		
	Patents		75,000

On 31/03/2025, Foods Ltd. acquires the business of Pickles Ltd. on the following terms:

- Foods Ltd. to take over all assets (except cash) and liabilities at their book values.
- Part of the Furniture and Fixtures is disposed off by Pickles Ltd. for ₹ 55,000 at cost
- The retirement of employees was due on 31/03/2025. A portion of ₹ 35,000 from Retirement Gratuity Fund was earmarked towards the payment due to them.
- Foods Ltd. decided to pay for each Preference share in Pickles Ltd., ₹ 27 in cash and one 8% Preference share of ₹ 100 in Foods Ltd.
- For each Equity share in Pickles Ltd., it was decided to pay ₹ 30 in cash and one Equity share of Foods Ltd. for ₹ 145. (Face value of each share of Foods Ltd. is ₹ 100)
- Liquidation expenses of ₹ 22,500 paid by Pickles Ltd. were subsequently reimbursed by Foods Ltd.
- The fixed assets of Pickles Ltd were not revalued for the purpose of amalgamation.

You are required to pass the necessary journal entries and also prepare Realisation Account and cash account in the books of Pickles Ltd.

ANSWER

Journal Entries in the books of Pickles Ltd.

		Debit (₹)	Credit (₹)
Realisation A/c	Dr.	16,50,000	
To Land & Building A/c			3,50,000
To Plant & Machinery A/c			3,00,000
To Furniture & Fixtures A/c			1,00,000
To Patent A/c			75,000
To Inventories A/c			5,25,000
To Trade Receivables A/c (Being assets transferred to Realisation A/c)			3,00,000
8% Debentures A/c	Dr.	1,00,000	
Trade Payables A/c	Dr.	1,75,000	
Other Current Liabilities A/c	Dr.	65,000	
Retirement Gratuity Fund A/c	Dr.	35,000	
To Realisation A/c (being liabilities transferred to Realisation A/c)			3,75,000
Cash A/c	Dr.	55,000	
To Realisation A/c (being part of furniture sold)			55,000
Foods Ltd. A/c	Dr.	16,85,000	
To Realisation A/c (being purchase consideration receivable)			16,85,000
Cash A/c	Dr.	3,15,000	
Equity Shares in Foods Ltd A/c	Dr.	8,70,000	
Preference Shares in Foods Ltd A/c	Dr.	5,00,00	
To Foods Ltd. A/c (Being consideration received)			16,85,000
6% Preference Share Capital A/c	Dr.	5,00,000	
Realization A/c	Dr.	1,35,000	

To Preference Shareholders A/c (Being amount due to preference shareholders for capital and extra amount payable under the scheme of acquisition)			6,35,000
Preference Shareholders A/c	Dr.	6,35,000	
To Cash A/c			1,35,000
To Pref. Shares in Foods Ltd A/c (Being payment made to preference shareholders)			5,00,000
Equity Share Capital A/c	Dr.	6,00,000	
General Reserve A/c	Dr.	1,00,000	
Profit & Loss A/c	Dr.	1,10,000	
Retirement Gratuity fund	Dr.	25,000	
To Equity Shareholders A/c (being various accounts representing capital, reserve, profit and loss account and others transferred to equity shareholder account)			8,35,000
Equity Shareholders A/c		11,65,000	
To Cash A/c			2,95,000
To Equity Shares in Foods Ltd. A/c (Being payment made to equity shareholders)			8,70,000
Foods Ltd A/c	Dr.	22,500	
To Cash A/c (being liquidation expenses paid)			22,500
Cash A/c	Dr.	22,500	
To Foods Ltd A/c (Being reimbursement by Foods Ltd.)			22,500
Realisation A/c	Dr.	3,30,000	
To Equity Shareholders A/c (Being Profit on realization is transferred to equity shareholders)			3,30,000

**Realisation Account
(Journal Entries)**

	Particulars	Amount (₹)		Particulars	Amount (₹)
To	Land & Building	3,50,000	By	Debentures	1,00,000
To	Plant & Machinery	3,00,000	By	Trade Payables	1,75,000
To	Furniture & Fixtures	1,00,000	By	Other Current Liabilities	65,000
To	Patent	75,000	By	Ret. Gratuity Fund	35,000
To	Inventories	5,25,000	By	Cash (Sale of Furniture)	55,000
To	Trade Receivables	3,00,000	By	Foods Ltd (PC)	16,85,000
To	Preference Shareholders	1,35,000			
To	Equity Shareholder A/c (Profit on realization)	3,30,000			
		21,15,00			21,15,000

Cash Account

	Particulars	Amount (₹)		Particulars	Amount (₹)
To	Balance b/d	60,000	By	Foods Ltd. A/c (Expenses)	22,500
To	Realisation A/c (Furniture Sale)	55,000	By	Pref. Shareholders A/c	1,35,000
To	Foods Ltd. A/c (Reimbursement)	22,500	By	Equity Shareholders A/c	2,95,000
To	Foods Ltd (Cash Part of PC) (1,35,000 + 1,80,000)	3,15,000			
		4,52,500			4,52,500

Working Notes:**1. Purchase Consideration**

		₹	₹	Form
(i)	Preference Shares: ₹ 27 per share	1,35,000		Cash
	Preference shares	5,00,000	6,35,000	Preference shares cash
(ii)	Equity Shares: ₹ 30 per share	1,80,000		
	6,000 equity shares in Food Ltd. @ ₹ 145	8,70,000	10,50,000	Equity shares
			16,85,000	

QUESTION 26: (Q.AMG.SM.104(A) Exam May'24)

Intelligent Limited and Diligent Limited are carrying their business independently for last two years. Following financial information in respect of both the companies as at 31st March, 2024 has been given to you:

Particulars	Intelligent Limited (Rs.)	Diligent Limited (Rs.)
Equity Share Capital of Rs. 100 each	12,00,000	10,00,000
8% Preference shares of Rs. 100 each	3,00,000	2,00,000
Trade Payable	12,00,000	4,00,000
Retirement Gratuity Fund (Long Term)	3,00,000	2,00,000
Profit and Loss Account		
Opening balance	4,50,000	2,50,000
Profit for the current year	2,50,000	1,50,000
Land and Buildings	10,00,000	8,00,000
Plant and Machinery	10,00,000	6,00,000
Inventories	7,00,000	4,00,000
Trade Receivables	6,00,000	3,00,000
Cash and Bank	4,00,000	1,00,000

On 1st April 2024, both the companies agreed to amalgamate and form a new company "Genius Limited" with an authorized capital of Rs. 40,00,000 divided into 30,000 equity shares of Rs. 100 each and 10,000 8% preference shares of Rs. 100 each.

The amalgamation has to be carried out on the basis of following agreement:

(1) Assets of both the companies were to be revalued as follows:

Particulars	Intelligent Limited (Rs.)	Diligent Limited (Rs.)
Land and Buildings	11,00,000	8,50,000

Plant and Machinery	9,00,000	4,00,000
Inventories	6,00,000	3,00,000

- (2) Trade payables of Intelligent Limited includes Rs. 1,00,000 due to Diligent Ltd. And the trade receivables of Diligent Limited shows Rs. 1,00,000 receivables from Intelligent Limited.
- (3) The purchase consideration is to be discharged in the following manner:
- Issue 22,000 Equity shares of Rs. 100 each fully paid up in the proportion of the sum of their profitability in the preceding two financial years.
 - Preference shareholders of both companies are issued equivalent number of 10% preference shares of Rs. 100 each of Genius Limited at a price of 125 per share.
 - 12% debentures of Rs. 100 each in Genius Limited at par to provide an income equivalent to 10% return on the basis of net assets in their respective business as on 1st April, 2024 after revaluation of assets.

You are required to

- Compute the amount of shares & Debentures to be issued to Intelligent Limited and Diligent Limited.
- Prepare a Balance Sheet of Genius Limited showing the position immediately after amalgamation.

SOLUTION:

Computation of shares and debentures to be issued

		Intelligent Ltd.	Diligent Ltd.
(i) Equity shares	22,000 x 7/11 = 14,000(W.N.1)	14,00,000	
	22,000 x 4/11 =8,000(W.N.1)		8,00,000
(ii) Preference shares	$\left(\frac{3,00,000}{100} \times 125\right)$ $\left(\frac{2,00,000}{100} \times 125\right)$	3,75,000	2,50,000
(iii) Debentures	Refer (W.N.3)	<u>17,50,000</u>	<u>11,25,000</u>
Total Purchase Consideration (i + ii + iii)		<u>35,25,000</u>	<u>21,75,000</u>

Balance Sheet of Genius Limited as at 1st April, 2024 (after amalgamation)

		Notes no.	₹
I.	Equity and Liabilities		
(1)	Shareholder's fund		
(a)	Share Capital	1	27,00,000
(b)	Reserves & Surplus	2	1,25,000
(2)	Non-current Liabilities		
(a)	Long term borrowings	3	28,75,000
(b)	Other non-current liabilities	4	5,00,000
(3)	Current Liabilities		
(a)	Trade Payables (12,00,000 + 4,00,000 – 1,00,000)		15,00,000

	Total		77,00,000
II.	Assets		
(1)	Non-current Assets		
(a)	Property, Plant & Equipment	5	32,50,000
(b)	Intangible Assets	6	22,50,000
(2)	Current Assets		
(a)	Inventories (6,00,000 + 3,00,000)		9,00,000
(b)	Trade Receivables (6,00,000 + 3,00,000 - 1,00,000)		8,00,000
(c)	Cash & Cash Equivalents		5,00,000
	Total		77,00,000

Notes to Accounts:

Sr. No.	Particular	₹
1.	<u>Share Capital</u>	
	<u>Authorized Share Capital</u>	
a)	Equity Share Capital 30,000 Equity Shares of ₹ 100 each	30,00,000
b)	Preference Share Capital 10% 10,000 Preference Shares ₹ 100 each	<u>10,00,000</u>
		<u>40,00,000</u>
	<u>Issued, Subscribed & Paid-up Capital</u>	
a)	Equity Share Capital 22,000 Equity Shares of ₹100 each (out of the above all shares are issued for consideration other than cash)	22,00,000
b)	Preference Share Capital 10% 5,000 Preference Shares of ₹100 each (out of the above all shares are issued for consideration other than cash)	<u>5,00,000</u>
		<u>27,00,000</u>
2.	<u>Reserves & Surplus</u>	
	Securities Premium	1,25,000
3.	<u>Long term borrowings</u>	
	12% Debentures of ₹ 100 each	28,75,000
4.	Other Non-current Liabilities Gratuity Fund	5,00,000
5.	Property, Plant & Equipment Land & Building (11,00,000 + 8,50,000) Plant & Machinery (9, 00,000 + 4,00,000)	19,50,000 <u>13,00,000</u>
		<u>32,50,000</u>
6.	Intangible Assets Goodwill	22,50,000

Working Notes:**1. Calculation of Ratio of Equity Shares**

	Intelligent Ltd.	Diligent Ltd
*Opening balance P&L	4,50,000	2,50,000
Profit for the current year	2,50,000	1,50,000
Total	7,00,000	4,00,000

The total profits- ₹ 7,00,000 + ₹ 4,00,000 = ₹ 11,00,000.

No. of shares to be issued = 22,000 equity shares in the proportion of the preceding 2 years' profits. i.e. in 7:4.

2. Calculation of Net assets as on 31.3.2024

Particulars	Intelligent Ltd.	Diligent Ltd
<u>Assets (after revaluation)</u>		
Land and Buildings	11,00,000	8,50,000
Plant & Machinery	9,00,000	4,00,000
Inventories	6,00,000	3,00,000
Trade Receivables	6,00,000	3,00,000
Cash & Cash Equivalents	<u>4,00,000</u>	<u>1,00,000</u>
Total (a)	<u>36,00,000</u>	<u>19,50,000</u>
<u>Liabilities</u>		
Trade Payables	12,00,000	4,00,000
Gratuity Fund	<u>3,00,000</u>	<u>2,00,000</u>
Total (b)	<u>15,00,000</u>	<u>6,00,000</u>
Net Assets (a – b)	21,00,000	13,50,000

3. Calculation of 12% Debentures to be issued to Intelligent Ltd. and Diligent Ltd.

	Intelligent Ltd.	Diligent Ltd
	₹	₹
Net assets (Refer working note)	21,00,000	13,50,000
10% return on Net assets	2,10,000	1,35,000
12% Debentures to be issued		
$[2,10,000 \times \frac{100}{12}] = 17,50,000$ of ₹ 100 each	17,500	
$[1,35,000 \times \frac{100}{12}] = 11,25,000$ of ₹ 100 each		11,250

4. Calculation of Goodwill / Capital Reserve

S.No.	Particulars	Intelligent Ltd.	Diligent Ltd.	
(i)	Purchase Consideration Paid	35,25,000	21,75,000	
(ii)	Less: Net Assets	21,00,000	13,50,000	
(iii)	Goodwill	14,25,000	8,25,000	22,50,000

Alternatively:**4. Calculation of Goodwill / Capital Reserve**

S.No.	Particulars	Intelligent Ltd.	Diligent Ltd.	
(i)	Purchase Consideration Paid	35,25,000	21,75,000	
(ii)	Less: Net Assets*	22,00,000	12,50,000	
(iii)	Goodwill	13,25,000	9,25,000	22,50,000

* Calculation of Net assets taken over

Particulars	Intelligent Ltd.	Diligent Ltd
Assets (after revaluation)		
Land and Buildings	11,00,000	8,50,000
Plant & Machinery	9,00,000	4,00,000
Inventories	6,00,000	3,00,000
Trade Receivables	6,00,000	2,00,000*
Cash & Cash Equivalents	<u>4,00,000</u>	<u>1,00,000</u>
Total (a)	<u>36,00,000</u>	<u>18,50,000</u>
Liabilities		
Trade Payables	11,00,000**	4,00,000
Gratuity Fund	<u>3,00,000</u>	<u>2,00,000</u>
Total (b)	<u>14,00,000</u>	<u>6,00,000</u>
Net Assets (a – b)	22,00,000	12,50,000

* ₹ 3,00,000 - ₹ 1,00,000 = ₹ 2,00,000

** ₹ 12,00,000 - ₹ 1,00,000 = ₹ 11,00,000

QUESTION 27: (Q.AMG.SM.105(A))

Following is the balance sheet of A Ltd. as on 31st March, 20X1

	Particulars	Notes	Rs. (000)
	Equity and Liabilities		
1	Shareholders' funds		
A	Share capital	1	22,50
B	Reserves and Surplus	2	9,00
2	Non-current liabilities		
A	Long-term borrowings	3	7,00
3	Current liabilities		
A	Trade Payables		<u>5,00</u>
	Total		<u>43,50</u>
	Assets		
1	Non-current assets		
A	Property, Plant and Equipment	4	32,50
	Non-current investments	5	6,00
2	Current assets		
A	Inventories		2,00
B	Trade receivables		2,00
C	Cash and Cash equivalents		<u>1,00</u>
	Total		<u>43,50</u>

Notes to accounts

1	Share Capital	Rs. in ('000)
	Equity share capital	
	1,50,000 Equity Shares of Rs. 10 each	15,00
	7,500 14% Preference Shares of Rs. 100 each	<u>7,50</u>
		<u>22,50</u>
2	Reserves and Surplus	
	General reserve	<u>9,00</u>
3	Long-term borrowings	
	Secured	
	15% Debentures	<u>7,00</u>
4	Property, plant and Equipment	
	Land and Building	<u>32,50</u>
5	Non-current investments	
	Investments at cost	<u>6,00</u>

B Ltd agreed to take over the assets and liabilities on the following terms and conditions:

- Discharge 15% debentures at a premium of 10% by issuing 15% debentures of B Ltd.
- PPE at 10% above the book value and investments at par value.
- Current assets at a discount of 10% and Current liabilities at book value.
- Preference shareholders are discharged at a premium of 10% by issuing 15% preference shares of Rs.100 each.
- Issue 3 equity shares of Rs. 10 each for every 2 equity shares in A Ltd. and pay the balance in cash.

Calculate Purchase consideration.

SOLUTION**Calculation of Purchase Consideration (Net Asset value Method)**

PARTICULARS	(Rs. in '000's)
Value of assets taken over:	
Property, Plant and Equipment Non-Current	35,75
Investments Current Assets	6,00
Total Assets (A)	<u>4,50</u>
	<u>46,25</u>
Less: Liabilities taken over:	
15% Debentures	7,70
Current Liabilities	<u>5,00</u>
Total Liabilities (B)	<u>12,70</u>
Purchase consideration (A -B)	<u>33,55</u>
Mode of Purchase Consideration	
In the form of 15% Preference shares	8,25
	22,50
In the form of Equity shares	<u>2,80</u>
In the form of Cash (Balance)	33,55
Total	

QUESTION 28: (Q.AMG.RMP.203(A) RTP Nov'22)

The balance sheets of Truth Limited and Myth Limited as at 31.03.2021 is given below. Myth Limited is to be amalgamated with Truth Limited from 1.04.2021. The amalgamation is to be carried out in the nature of purchase.

Particulars	Note No.	Truth Ltd. (Rs.)	Myth Ltd. (Rs.)
(1) Equity and Liabilities			
1. Shareholders' Funds			
(a) Share Capital	1	10,00,000	4,00,000
(b) Reserves and Surplus	2	11,35,000	4,13,000
2. Non -Current Liabilities	3	-	1,50,000
3. Current Liabilities	4	1,40,000	1,82,000
Total		22,75,000	11,45,000
(2) Assets			
1. Non -Current Assets			
(a) Property, Plant & Equipment		15,75,000	6,80,000
(b) Investments		1,87,500	1,00,000
2. Current Assets	5	5,12,500	3,65,000
Total		22,75,000	11,45,000

Notes to Accounts:

Note No.	Particulars	Truth Limited (Rs.)	Myth Limited (Rs.)
1	Share Capital		
	Equity shares of Rs. 10 each	10,00,000	4,00,000
2	Reserves & Surplus		
	General Reserve	5,05,000	2,30,000
	Profit & Loss A/c	4,45,000	1,58,000
	Export Profit Reserve	1,85,000	25,000
		11,35,000	4,13,000
3	Non- Current Liabilities		
	14% Debentures	---	1,50,000
4	Current Liabilities		
	Trade Payables	90,000	1,42,000
	Other Current Liabilities	50,000	40,000
		1,40,000	1,82,000
5	Current Assets		
	Inventory	2,15,000	85,000
	Trade Receivables	2,02,500	1,75,000
	Cash and Cash equivalents	95,000	1,05,000
		5,12,500	3,65,000

Truth Limited would issue 12% debentures to discharge the claim of the debenture holders of Myth Limited so as to maintain their present annual interest income. Non-trade investment, which constitute 80% of their respective total investments yielded income of 20% to Truth Limited and 15% to Myth Limited. This income is to be deducted from profits while computing average profit for the purpose of calculating goodwill. Profit before tax of both the companies during the last 3 years were as follows:

	Truth Limited (Rs.)	Myth Limited (Rs.)
2018-2019	8,20,000	2,55,000
2019-2020	7,45,000	2,15,000
2020-2021	6,04,000	2,14,000

Goodwill is to be calculated on the basis of simple average of three years profit by using Capitalization method taking 18% as normal rate of return. Ignore taxation. Purchase consideration is to be discharged by Truth Limited on the basis of intrinsic value per share. Prepare Balance Sheet of Truth Limited after the amalgamation.

SOLUTION

Balance Sheet of Truth Ltd. (after amalgamation with Myth Ltd.) as at 1.4.2021

Particulars	Note No.	(Rs.)
I. Equity and liabilities		
(1) Shareholder's funds		
(a) Share capital	1	13,13,750
(b) Reserves and surplus	2	20,76,250
(2) Non-current liabilities		
12% Debentures	3	1,75,000
(3) Current liabilities		
(a) Trade payables	4	2,32,000
(b) Other current liabilities	5	90,000
Total		38,87,000
II. Assets		
(1) Non-current assets		
(a) Property, plant and equipment	6	22,55,000
(b) Intangible assets (Goodwill) [WN 1]		4,67,000
(c) Non-current investments	7	2,87,500
(2) Current assets		
(a) Inventories (2,15,000 + 85,000)		3,00,000
(b) Trade receivables (2,02,500 + 1,75,000)		3,77,500
(c) Cash & cash equivalents (95,000 + 1,05,000)		2,00,000
Total		38,87,000

Notes to Accounts

		(Rs.)	(Rs.)
1. Share Capital			
	1,31,375 Equity Shares of Rs. 10 each [1,00,000 + 31,375]		13,13,750
	(of the above shares, 31,375 shares were issued to the vendors otherwise than for cash)		
2. Reserves and surplus			
	General Reserve	5,05,000	
	Profit and Loss A/c	4,45,000	
	Securities Premium [31,375 x 30]	9,41,250	

	Export profit reserve	1,85,000		
	Add: Balance of Myth Ltd.		2,10,000	
	25,000			
	Amalgamation Adjustment Reserve		(25,000)	20,76,250
3.	Long Term Borrowings			
	12% Debentures issued to Myth Ltd.			1,75,000
4.	Trade payables			
	Trade payables		90,000	
	Add: Taken over		1,42,000	2,32,000
5	Other Current Liabilities			
	Truth Ltd.		50,000	
	Myth Ltd.		40,000	90,000
6.	Property, Plant & Equipment			
	Truth Ltd.		15,75,000	
	Myth Ltd.		6,80,000	22,55,000
7.	Investment			
	Truth Ltd.		1,87,500	
	Myth Ltd.		1,00,000	2,87,500

Working Notes:**(1) Valuation of Goodwill****(i) Capital Employed**

	Truth Ltd.		Myth Ltd.	
	Rs.	Rs.	Rs.	Rs.
Assets as per Balance Sheet		22,75,000		11,45,000
Less: Non-trade Investment		(1,50,000)		(80,000)
Less: Liabilities:		21,25,000		10,65,000
14% Debentures	-		1,50,000	
Trade payables	90,000		1,42,000	
Other current liabilities	50,000	(1,40,000)	40,000	(3,32,000)
Capital Employed		19,85,000		7,33,000

(ii) Average Profit before Tax

	Truth Ltd.		Myth Ltd.	
2018-2019		8,20,000		2,55,000
2019-2020		7,45,000		2,15,000
2020- 2021		6,04,000		2,14,000
Total profit of 3 years (a)		21,69,000		6,84,000
Simple Average [(a)/3]		7,23,000		2,28,000
Less: Non-trading income*		(30,000)		(12,000)
		6,93,000		2,16,000
(iii) Goodwill	[(6,93,000 / 18) x 100]		[(2,16,000 / 18) x 100]	
Capitalised value of average profit		38,50,000		12,00,000
Less: Capital Employed [From (i) above]		(19,85,000)		(7,33,000)
Goodwill		18,65,000		4,67,000

* For Truth Ltd. = $1,87,500 \times 80\% \times 20\% = 30,000$; and
 Myth Ltd. = $1,00,000 \times 80\% \times 15\% = 12,000$

(2) Intrinsic Value per Share

	Truth Ltd.		Myth Ltd.	
		Rs.		Rs.
Goodwill [W.N. 1]	18,65,000		4,67,000	
Other Assets	22,75,000	41,40,000	11,45,000	16,12,000
Less: Liabilities				
12% Debentures	-		1,75,000**	
Trade payables	90,000		1,42,000	
Provision for Tax	50,000	(1,40,000)	40,000	(3,57,000)
Net Assets		40,00,000		12,55,000
Intrinsic value per share [Net Assets / No. of Shares]		40,00,000 / 1,00,000		12,55,000 / 40,000
		= Rs. 40		= Rs. 31.375

** $1,50,000 \times 14\% / 12\% = 1,75,000$

(3) Purchase Consideration & manner of its discharge

Intrinsic Value of Myth Ltd. [a]	Rs. 31.375 per share
No. of shares [b]	40,000 shares
Purchase Consideration c= [a x b]	Rs. 12,55,000
Intrinsic Value of Truth Ltd. [d]	Rs. 40 per share
No. of shares to be issued [c / d]	31,375 shares

QUESTION 29: (Q.AMG.RMP.205(A) RTP May'22)

The following are the Balance Sheets of Aakash Limited and Ganga Limited as at March 31, 2021:

Particulars	Note No.	Aakash Limited (Rs.)	Ganga Limited (Rs.)
I. Equity and Liabilities:			
(1) Shareholder's Funds:			
(a) Share Capital	1	80,00,000	20,00,000
(b) Reserves and Surplus	2	(3,24,00,000)	56,00,000
(2) Non-Current Liabilities:			
(a) Secured Loans	3	3,20,00,000	1,60,00,000
(b) Unsecured Loans	4	1,72,00,000	-
(3) Current Liabilities:			
(a) Trade Payables		56,00,000	36,00,000
(b) Other Current Liabilities	5	2,04,00,000	56,00,000
Total		5,08,00,000	3,28,00,000
II. Assets:			
(1) Non-Current Assets:			
Property, Plant & Equipment		68,00,000	1,36,00,000

(2) Current Assets:			
(a) Inventories		3,68,00,000	-
(b) Other Current Assets		72,00,000	1,92,00,000
Total		5,08,00,000	3,28,00,000

Notes to Accounts:

		Aakash Limited (Rs.)	Ganga Limited (Rs.)
1. Share Capital			
	Authorized, Issued, Subscribed & Paid up:		
	6,00,000 Equity Shares of Rs.10 each	60,00,000	-
	20,000 Preference Shares of Rs. 100 each	20,00,000	-
	2,00,000 Equity Shares of Rs. 10 each	-	20,00,000
		80,00,000	20,00,000
2. Reserves and Surplus			
	General Reserve	8,00,000	56,00,000
	Surplus	(3,32,00,000)	-
		(3,24,00,000)	56,00,000
3. Secured Loans (Secured Loans of Aakash Limited are secured against pledge of Inventories)		3,20,00,000	1,60,00,000
4. Unsecured Loans		1,72,00,000	-
5. Other Current Liabilities			
	Statutory Liabilities	1,44,00,000	20,00,000
	Liability to Employees	60,00,000	36,00,000
		2,04,00,000	56,00,000

Both the companies go into liquidation and a new company 'Aakash Ganga Limited' is formed to take over their business. The following information is given:

- (i) All Current Assets of two companies, except pledged inventory are taken over by Aakash Ganga Limited. The realizable value of all the Current Assets (including pledged inventory) is 80% of book value in case of Aakash Limited and 70% for Ganga Limited.
- (ii) Property, Plant and Equipment of both the companies are taken over at book value by AakashGanga Limited.
- (iii) Secured Loans include Rs. 32,00,000 accrued interest in case of Ganga Limited.
- (iv) 4,00,000 Equity Shares of Rs. 10 each are allotted by AakashGanga Limited at par against cash payment of entire face value to the shareholders of Aakash Limited and Ganga Limited in the ratio of shares held by them in Aakash Limited and Ganga Limited.
- (v) Preference Shareholders in Aakash Limited are issued Equity Shares in AakashGanga Ltd. worth Rs. 4,00,000 in lieu of their present holdings.
- (vi) Secured Loan agree to continue the balance amount of their loans to AakashGanga Limited after adjusting realizable value of pledged asset in case of Aakash Limited and after waiving 50% of interest due in the case of Ganga Limited.
- (vii) Unsecured Loans are taken over by AakashGanga Limited at 25% of loan amounts.
- (viii) Employees are issued fully paid Equity Shares in AakashGanga Limited in full settlement of their dues.
- (ix) Statutory Liabilities are taken over by AakashGanga Limited at full value and Trade Payables are taken over at 80% of the book value.

You are required to prepare the opening Balance Sheet of AakashGanga Limited as at 1.4.2021.

SOLUTION

Balance sheet of AakashGanga Ltd. as at 1st April, 2021

Particulars	Note No.	(Rs.)
I. Equity and Liabilities		
(1) Shareholders' Funds		
(a) Share Capital	1	1,40,00,000
(2) Non-Current Liabilities		
(a) Long term borrowings	2	2,12,60,000
(3) Current Liabilities		
(a) Trade Payables	3	73,60,000
(b) Other current liabilities	4	1,64,00,000
Total		5,90,20,000
II. Assets		
(1) Non-current assets		
(a) Property, Plant & Equipment	5	2,04,00,000
(b) Intangible assets	6	1,54,20,000
(2) Current assets		
(a) Cash and cash equivalents		40,00,000
(b) Other current assets	7	1,92,00,000
Total		5,90,20,000

Notes to Accounts

		(Rs.)
1. Share Capital		
Issued, subscribed & paid up:		
14,00,000 equity shares of Rs. 10 each, fully paid up (W.N.4)		1,40,00,000
(Of the above 10,00,000 shares have been issued for consideration other than cash)		
2. Long Term borrowings		
Secured Loans		
Aakash Limited 25,60,000		
Ganga Limited 1,44,00,000	1,69,60,000	
Unsecured Loans	43,00,000	2,12,60,000
3. Trade Payables (W.N.1)		
Aakash Limited	44,80,000	
Ganga Limited	28,80,000	73,60,000
4. Other current liabilities		
Statutory Liabilities		
Aakash Limited	1,44,00,000	
Ganga Limited	20,00,000	1,64,00,000
5. Property, Plant & Equipment		
Aakash Limited	68,00,000	
Ganga Limited	1,36,00,000	2,04,00,000
6. Intangible assets		
Goodwill (W.N.3)		1,54,20,000

7. Other Current Assets			
Aakash Limited		57,60,000	
Ganga Limited		1,34,40,000	1,92,00,000

Working Notes:**1. Value of total liabilities taken over by Aakash Ganga Ltd.****(Rs.)**

	Aakash Limited		Ganga Limited	
Current liabilities				
Statutory liabilities	1,44,00,000		20,00,000	
Liability to employees	60,00,000		36,00,000	
Trade payables @ 80%	44,80,000	2,48,80,000	28,80,000	84,80,000
Secured loans				
Given in Balance Sheet	3,20,00,000		1,60,00,000	
Interest waived	-		16,00,000	1,44,00,000
Value of Inventory (80% of Rs. 3,68,00,000)	2,94,40,000	25,60,000		
Unsecured Loans (25% of Rs. 1,72,00,000)		43,00,000		-
		3,17,40,000		2,28,80,000

2. Assets taken over by Aakash Ganga Ltd. (Rs.)

	Aakash Limited	Ganga Limited
	Rs.	Rs.
Property, Plant & Equipment	68,00,000	1,36,00,000
Current Assets (80% and 70% respectively of book value)	57,60,000	1,34,40,000
	1,25,60,000	2,70,40,000

3. Goodwill / Capital Reserve on amalgamation (Rs.)

Liabilities taken over (W.N. 1)		3,17,40,000	2,28,80,000
Equity shares to be issued to Preference Shareholders		4,00,000	-
	A	3,21,40,000	2,28,80,000
Less: Total assets taken over (W.N. 2)	B	(1,25,60,000)	(2,70,40,000)
	A-B	1,95,80,000	(41,60,000)
		Goodwill	Capital Reserve
Net Goodwill (1,95,80,000- 41,60,000)		1,54,20,000	

4. Equity shares issued by Aakash Ganga Ltd.

(i)	For Cash		40,00,000
	For consideration other than cash		
(ii)	In Discharge of Liabilities to Employees	96,00,000	
(iii)	To Preference shareholders	4,00,000	1,00,00,000

		1,40,00,000
	No. of shares @ Rs. 10	14,00,000

QUESTION 30: (Q.AMG.207(A) Jan'25 Exam)

Following are the summarized Balance Sheets of Light Limited and Bright Limited as at 31st March, 2024:

Particulars	Notes	Light Limited (Rs. In Lakhs)	Bright Limited (Rs. In Lakhs)
Equity and Liabilities			
Shareholders' Funds			
(a) Share Capital	1	50.00	40.00
(b) Reserves and Surplus	2	27.00	24.00
Non-Current Liabilities			
Long Term Provisions		1.50	-
Current Liabilities			
Trade Payables		3.40	2.00
Total		81.90	66.00
Assets			
Non-Current Assets			
Property, Plant and Equipment	3	68.70	50.25
Current Assets			
(a) Inventories		5.75	7.10
(b) Trade Receivables		4.30	5.80
(c) Cash and Cash equivalents		3.15	2.85
Total		81.90	66.00

Notes to Accounts:

Particulars	Light Limited (Rs. In Lakhs)	Bright Limited (Rs. In Lakhs)
1. Share Capital		
50,000 Equity Shares of Rs. 100 each	50.00	40.00
2. Reserves and Surplus		
Statutory Reserve	2.00	-
General Reserve	18.00	15.00
Securities Premium	-	5.00
Profit and loss	7.00	4.00
	27.00	24.00
3. Property, Plant and Equipment		
Land and Building	58.00	44.00
Plant and machinery	7.50	4.50
Other Assets	3.20	1.75
	68.70	50.25

Other Information

- (a) A company Rainbow Limited is formed to acquire the Assets and Liabilities of both the companies. Assets were acquired at book values except Land and Building of Light Limited, which is revalued at Rs. 62 lakhs.
- (b) Other Assets of Bright Limited are obsolete and are scrapped and sold for Rs. 50,000 by Bright Limited itself before acquisition of its assets and liabilities by Rainbow Limited.

- (c) Light Limited and Bright Limited will be issued 80,000 and 64,000 equity shares of Rs. 100 each respectively of new company Rainbow Limited in lieu of purchase consideration due to them.

You are required to Prepare:

- (a) Realization Account and Equity Shareholders Account in the books of Light Limited and Bright Limited;
 (b) Opening Balance Sheet of Rainbow Limited as at 31st March, 2024.

ANSWER

Adjustment in bank balance and profit & loss account before amalgamation

Other assets of Bright limited

	₹ In lakhs
Book value	1.75
Less: Sale proceeds	(0.50)
Loss on sale of other assets (debited to Profit & Loss A/c)	<u>1.25</u>

The new balance of Bank = 2.85 + 0.5 = 3.35 (₹ In lakhs)

The new balance of Profit & Loss A/c = 4 - 1.25 = 2.75 (₹ In lakhs)

(a) (i) Realisation Account

	Light Ltd. (₹ In lakhs)	Bright Ltd. (₹ In lakhs)		Light Ltd. (₹ In lakhs)	Bright Ltd. (₹ In lakhs)
To Sundry Assets, transfer :			By Long term provision	1.50	-
To Land & Building,	58.00	44.00	By Trade payables	3.40	2.00
To Plant & machinery	7.50	4.50	By Rainbow Ltd. - purchase	80.00	64.00
To Other assets	3.20	-			
To Inventories	5.75	7.10			
To Trade receivable	4.30	5.80			
To Cash & Bank Balance	3.15	3.35			
To Equity Shareholders - profit	3.00	1.25			
	<u>84.90</u>	<u>66.00</u>		<u>84.90</u>	<u>66.00</u>

(ii) Shareholders Account

	Light Ltd. (₹ In lakhs)	Bright Ltd. (₹ In lakhs)		Light Ltd. (₹ In lakhs)	Bright Ltd. (₹ In lakhs)
To Shares in Rainbow Ltd.	80.00	64.00	By Share Capital A/c - transfer	50.00	40.00
			By Statutory reserve	2.00	-
			By General	18.00	15.00

			Reserve		
			By Securities premium	-	5.00
			By Profit & Loss A/c	7.00	2.75
			By Realisation A/c	3.00	1.25
	80.00	64.00		80.00	64.00

(b)

Balance Sheet of Super Rainbow Ltd.

Particulars		Notes	(₹ In lakhs)
Equity and Liabilities			
1	Shareholders' funds		
A	Share capital	1	144.00
B	Reserves and Surplus	2	1.00
2	Non-current liabilities		
A	Long-term provisions		1.50
3	Current liabilities		
A	Trade Payables		5.40
	Total		151.90
Assets			
1	Non-current assets		
A	Property, Plant and Equipment	3	121.20
B	Intangible assets	4	1.25
2	Current assets		
	Inventories		12.85
	Trade receivables		10.10
	Cash and cash equivalents		6.50
	Total		151.90

(c) Notes to Accounts

		(₹ In lakhs)
1.	Share Capital	
	Equity share capital	
	Issued, subscribed and paid up	
	1,44,000 Equity shares of ₹ 100 each	144.00
	(all shares are issued for consideration other than cash)	
2.	Reserves and Surplus	
	Statutory Reserves	2.00
	Amalgamation Adjustment Reserves	(2.00)
	Capital Reserves	1.00

		1.00
3.	Property, Plant and Equipment	
	Land and Buildings	106.00
	Plant and Machinery	12.00
	Other Assets	3.20
		121.20
4	Intangible assets	
	Goodwill	1.25

Working notes:**1. Calculation of purchase consideration**

	Light Ltd. (₹ In lakhs)	Bright Ltd. (₹ In lakhs)
80,000 Equity Shares of ₹ 100	80	
64,000 Equity Shares of ₹ 100		64

2. Calculation of Net assets taken over

		(₹ In lakhs)	
Particulars		Light Ltd.	Bright Ltd.
<i>Assets taken over:</i>			
Land and Buildings		62.00	44.00
Plant and Machinery		7.50	4.50
Other Assets		3.20	-
Inventory		5.75	7.10
Trade Receivable		4.30	5.80
Cash at Bank (2.85 + 0.50)		<u>3.15</u>	<u>3.35</u>
	(i)	<u>85.90</u>	<u>64.75</u>
<i>Liabilities taken over:</i>			
Long term provisions		1.50	-
Trade payable		<u>3.40</u>	<u>2.00</u>
	(ii)	<u>4.90</u>	<u>2.00</u>
Net assets taken over	(i) – (ii)	81.00	62.75

3. Calculation of Goodwill/Capital Reserve

	(₹ In lakhs)	
Particulars	Light Ltd.	Bright Ltd.
Net Assets takeover	81.00	62.75
Less: Purchase Consideration	(80.00)	(64.00)
Goodwill/ (Capital Reserve)	(1.00)	1.25

QUESTION 31: (Q.AMG.SM.301(A))

The following are the Balance Sheets of A Ltd. and B Ltd. as at 31.3.20X1:

		Particulars	Notes	₹ A Ltd (in'000)	₹ B Ltd (in'000)
		Equity and Liabilities			
1		Shareholders' funds			
	A	Share capital	1	2,000	1,000
	B	Reserves and Surplus	2	1,000	(800)
2		Non-current liabilities			
	A	Long-term borrowings	3	750	450
3		Current liabilities			
	A	Trade Payables		300	300
	B	Short term Borrowings – Bank overdraft		--	50
		Total		4,050	1,000
		Assets			
1		Non-current assets			
	A	Property, Plant and Equipment		2,700	850
	B	Non-current investments		700	--
2		Current assets			
	A	Trade receivables		400	150
	B	Cash and Cash equivalents (cash at bank)		250	--
		Total		4050	1000

Notes to Accounts

1	Share capital	A Ltd. ('000)	B Ltd. ('000)
	Equity shares of ₹ 100 each	2000	1000
		2000	1000
2	Reserves and Surplus		
	General reserve	1000	--
	Profit and loss A/c (debit balance)	--	(800)
		1000	(800)
3	Long term borrowings		
	10% debentures	500	--
	Loan from banks	250	450
		750	450

B Ltd. has acquired the business of A Ltd. The following scheme of merger was approved:

- Banks agreed to waive off the loan of ₹ 60 thousands of B Ltd.
- B Ltd. will reduce its shares to ₹ 10 per share and then consolidate 10 such shares into one share of ₹ 100 each (new share).
- Shareholders of A Ltd. will be given one share (new) of B Ltd. in exchange of every share held in A Ltd.
- Trade payables of B Ltd. includes ₹ 100 thousands payable to A Ltd.

Pass necessary entries in the books of B Ltd. and prepare Balance Sheet after merger

SOLUTION:**Calculation of purchase consideration**

One share of B Ltd. will be issued in exchange of every share of A Ltd. (i.e. 20,000 equity shares of B Ltd. will be issued against 20,000 equity shares of A Ltd.)	20,000 shares
---	---------------

Journal Entries in the books of B Ltd.

Date		(₹ in thousands)	
		Dr. ₹	Cr. ₹
20X1			
March, 31	Loan from bank A/c Dr. To Capital reduction A/c (Being loan from bank waived off to the extent of ₹ 60 thousand)	60	60
	Equity share capital A/c (₹ 100) Dr. To Equity share capital A/c (₹ 10) To Capital reduction A/c (Being equity shares of ₹ 100 each reduced to ₹ 10 each)	1,000	100 900
	Equity share capital A/c (₹ 10) Dr. To Equity share capital A/c (₹ 100 each) (Being 10 equity shares of ₹ 10 each consolidated to one share of ₹ 100 each)	100	100
	Capital reduction A/c Dr. To Profit and loss A/c To Capital reserve A/c (Being accumulated losses set off against reconstruction A/c and balance transferred to capital reserve account)	960	800 160
	Property, Plant & Equipment A/c Dr. Investment A/c Dr. Trade receivables A/c Dr. Cash at bank A/c Dr. To Trade payables A/c To Loans from bank A/c To 10% Debentures A/c To Business purchase A/c To Reserves A/c (Being assets, liabilities and reserves taken over under pooling of interest method)	2,700 700 400 250	300 250 500 2,000 1,000
	Liquidator of A Ltd. A/c Dr. To Equity share capital A/c (Being payment made to liquidators of A Ltd. by allotment of 20,000 new equity shares)	2,000	2,000
	Trade payables A/c Dr. To Trade receivables A/c (Being mutual owing cancelled)	100	100

Balance Sheet of B Ltd. after merger as on 31.3.20X1

	Particulars	Notes	₹ in '000
	Equity and Liabilities		
1	Shareholders' funds		
A	Share capital	1	2,100
B	Reserves and Surplus	2	1,160
2	Non-current liabilities		
A	Long term borrowings	3	1,140
3	Current liabilities		
A	Trade payables		500
B	Short term borrowings	4	50
	Total		4,950
	Assets		
1	Non-current assets		

	A	Property, Plant and Equipment		3,550
	B	Non-current investments		700
2		Current assets		
	A	Trade receivables		450
	B	Cash and cash equivalents		250
		Total		4,950

Notes to accounts

			₹ in '000
1	Share Capital		
	21,000, Equity shares of ₹ 100 each fully paid		2,100
	(Out of the above, 20,000 shares have been issued for consideration other than cash)		
2	Reserves and Surplus		
	Capital reserve	160	
	General reserve	1,000	
	Total		1,160
3	Long Term Borrowings		
	10% Debentures	500	
	Loan from Bank (250+450-60)	640	1,140
4	Short term borrowings		
	Bank overdraft		50

QUESTION 32: (Q.AMG.SM.402(A))

K Ltd. and L Ltd. amalgamate to form a new company LK Ltd. The financial position of these two companies as at the date of amalgamation was as under:

		Particulars	Notes	₹ K Ltd.	₹ L Ltd.
		Equity and Liabilities			
1		Shareholders' funds			
	A	Share capital	1	12,00,000	6,00,000
	B	Reserves and Surplus	2	3,71,375	1,97,175
2		Non-current liabilities			
	A	Long-term borrowings	3	2,00,000	2,00,000
3		Current liabilities			
	A	Trade Payables		1,00,000	2,10,000
		Total		18,71,375	12,07,175
		Assets			
1		Non-current assets			
	A	Property, Plant and Equipment	4	11,30,000	8,20,000
	B	Intangible assets	5	80,000	-
2		Current assets			
	A	Inventories		2,25,000	1,40,000
	B	Trade receivables		2,75,000	1,75,000
	C	Cash and Cash equivalents	6	1,61,375	72,175
		Total		18,71,375	12,07,175

Notes to accounts

1	Share Capital		K Ltd.	L Ltd.
	Equity shares of ₹ 100 each		8,00,000	3,00,000
	7% Preference Shares of ₹ 100 each		4,00,000	3,00,000
			12,00,000	6,00,000
2	Reserves and Surplus			
	General reserve		-	1,00,000
	Profit and loss account		3,71,375	97,175
			3,71,375	1,97,175
3	Long-term borrowings			
	5% Debentures		2,00,000	-
	Secured loan		-	2,00,000
			2,00,000	2,00,000
4	Property, plant and Equipment			
	Land and Building		4,50,000	3,00,000
	Plant and machinery		6,20,000	5,00,000
	Furniture and fittings		60,000	20,000
			11,30,000	8,20,000
5	Intangible assets			
	Goodwill		80,000	-
			80,000	-
6	Cash and Cash Equivalents			
	Cash at Bank		1,20,000	55,000
	Cash in hand		41,375	17,175
			1,61,375	72,175

The terms of amalgamation are as under:

- (A)** (1) The assumption of liabilities of both the Companies.
 (2) Issue of 5 Preference shares of ₹ 20 each in LK Ltd. @ ₹ 18 paid up at premium of ₹ 4 per share for each preference share held in both the Companies.
 (3) Issue of 6 Equity shares of ₹ 20 each in LK Ltd. @ ₹ 18 paid up at a premium of ₹ 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 ₹ 20,000 due from L Ltd.
- (C)** The LK Ltd. is to issue 15,000 new equity shares of ₹ 20 each, ₹ 18 paid up at premium of ₹ 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.

SOLUTION:**Books of K Ltd. Realisation Account**

	₹		₹
To Goodwill	80,000	By 5% Debentures	2,00,000
To Land & Building	4,50,000	By Trade payables	1,00,000
To Plant & Machinery	6,20,000	By LK Ltd. (Purchase consideration)	15,60,000

To Furniture & Fitting	60,000	By Equity shareholders A/c (loss)	51,375
To Trade receivables	2,75,000		
To Stores & inventory	2,25,000		
To Cash at Bank	1,20,000		
To Cash in hand	41,375		
To Preference Shareholders (excess payment)	40,000		
	19,11,375		19,11,375

Equity Shareholders Account

	₹		₹
To Realisation A/c (loss)	51,375	By Share Capital A/c	8,00,000
To Equity Shares in LK Ltd.	10,56,000	By Profit & Loss A/c	3,71,375
To Cash	64,000		
	11,71,375		11,71,375

7% Preference Shareholders Account

	₹		₹
To Preference Shares in LK Ltd.	4,40,000	By Share capital	4,00,000
		By Realization A/c	40,000
	4,40,000		4,40,000

LK Ltd. Account

	₹		₹
To Realisation A/c	15,60,000	By Equity Shares in LK Ltd. For Equity 10,56,000 Pref 4,40,000	14,96,000
		By cash	64,000
	15,60,000		15,60,000

**Books of L Ltd.
Realisation Account**

	₹		₹
To Land & Building	3,00,000	By Trade payables	2,10,000
To Plant & Machinery	5,00,000	By Secured loan	2,00,000
To Furniture & Fittings	20,000	By LK Ltd. (Purchase consideration)	7,90,000
To Trade receivables	1,75,000	By Equity shareholders A/c Loss	31,175
To Inventory of stores	1,40,000		
To Cash at bank	55,000		
To Cash in hand	17,175		
To Pref. shareholders	30,000		
	12,37,175		12,37,175

Equity Shareholders Account

	₹		₹
To Equity shares in LK Ltd.	3,96,000	By Share Capital	3,00,000
To Realisation	37,175	By Profit & Loss A/c	97,175
To Cash	64,000	By Reserve	1,00,000

	4,97,175		4,97,175
--	-----------------	--	-----------------

7% Preference Shareholders Account

	₹		₹
To Preference Shares in LK Ltd.	3,30,000	By Share capital	3,00,000
		By Realization A/c	30,000
	3,30,000		3,30,000

LK Ltd. Account

	₹		₹
To Realisation A/c	7,90,000	By Equity Shares in LK Ltd. For Equity 3,96,000 Pref <u>3,30,000</u>	7,26,000
		By cash	64,000
	7,90,000		7,90,000

Working Notes:**(i) Purchase consideration**

	K Ltd. ₹	L Ltd. ₹
Payable to preference shareholders:		
Preference shares at ₹ 22 per share	4,40,000	3,30,000
Equity Shares at ₹ 22 per share	10,56,000	3,96,000
Cash [See W.N. (ii)]	64,000	64,000
	15,60,000	7,90,000

(ii) Value of Net Assets

		K Ltd. ₹		L Ltd. ₹
Goodwill		80,000		
Land & Building		4,50,000		3,00,000
Plant & Machinery		6,20,000		5,00,000
Furniture & Fittings		60,000		20,000
Trade receivables less 2.5%		2,68,125		1,70,625
Inventory less 2%		2,20,500		1,37,200
Cash at Bank		1,20,000		55,000
Cash in hand		41,375		17,175
		18,60,000	–	12,00,000
Less: Debentures	2,00,000			
Trade payables	1,00,000		2,10,000	
Secured Loans		(3,00,000)	2,00,000	(4,10,000)
		15,60,000		7,90,000
Payable in shares		14,96,000		7,26,000
Payable in cash		64,000		64,000

QUESTION 33: (Q.AMG.RMP.502(A) Exam July'21)

The summarized Balance Sheets of Black Limited and White Limited as on 31st March, 2020 is as follows:

Particulars	Notes	Black Limited (Rs. In 000)	White Limited (Rs. In 000)
Equity and Liabilities			
Shareholders' Funds			
(a) Share Capital	1	6,000	3,600
(b) Reserves and Surplus	2	1,080	660
Current Liabilities			
Trade payables		600	360
Total		7,680	4,620
Assets			
Non-current assets			
Property, Plant and Equipment		3,600	2,400
Current assets			
(a) Inventories		960	720
(b) Trade receivables		1,680	1,080
(c) Cash and Cash Equivalents		1,440	420
Total		7,680	4,620

Note No.	Particulars	Black Limited (Rs. in 000)	White Limited (Rs. in 000)
1.	Share Capital Equity Shares of Rs. 100 each	6,000	3,600
2.	Reserves and Surplus		
	General Reserve	360	180
	Profit and Loss Account	720	480
	Total	1,080	660

Black Limited takes over White Limited on 1st July, 2020.

No Balance Sheet of White Limited is available as on that date. It is, however estimated that White Limited earned profit of Rs. 2,40,000 after charging proportionate depreciation @ 10% p.a. on Property Plant and Equipment, during April-June, 2020.

Estimated profit of Black Limited during these 3 months was Rs. 4,80,000 after charging proportionate depreciation @ 10% p.a. on Property Plant and Equipment.

Both the companies have declared and paid 10% dividend within this 3 months' period.

Goodwill of White Limited is valued at Rs. 2,40,000 and Property Plant and Equipment are valued at Rs. 1,20,000 above the depreciated book value on the date of takeover.

Purchase consideration is to be satisfied by Black Limited by issuing shares at par. Ignore income tax. You are required to:

- Compute No. of shares to be issued by Black Limited to White Limited against purchase consideration.
- Calculate the balance of Net Current Assets of Black Limited and White Limited as on 1st July, 2020.
- Give balance of Profit or Loss of Black Limited as on 1st July, 2020

iv. Give balance of Property Plant and Equipment as on 1st July, 2020 after takeover.

SOLUTION

(i) **No. of shares issued by Black Ltd. to White Ltd. against purchase consideration**

White Ltd.	Rs.	Rs.
Goodwill		2,40,000
Property, plant and equipment	24,00,000	
Less: Depreciation $[24,00,000 \cdot 10\% \cdot 3/12]$	<u>(60,000)</u>	
	23,40,000	
Add: Appreciation	<u>1,20,000</u>	24,60,000
Inventory		7,20,000
Trade receivables		10,80,000
Cash and Bank balances	4,20,000	
Add: Profit after depreciation 2,40,000		
Add: Depreciation (non-cash) <u>60,000</u>	3,00,000	
Less: Dividend $[36,00,000 \cdot 10\%]$	<u>(3,60,000)</u>	<u>3,60,000</u>
		48,60,000
Less: Trade payables		<u>(3,60,000)</u>
Purchase Consideration		<u>45,00,000</u>
Number of shares to be issued by Black Ltd. @ Rs. 100 each		45,000 shares

ii. **Calculation of Net Current Assets as on 01.07.2020**

		Black Ltd.		White Ltd.
		Rs.		Rs.
Current assets:				
Inventory		9,60,000		7,20,000
Trade receivables		16,80,000		10,80,000
Cash and Bank	14,40,000		4,20,000	
Less: Dividend	(6,00,000)		(3,60,000)	
Add: Profit after depreciation	4,80,000		2,40,000	
Add: Depreciation being non cash	<u>90,000</u>	<u>14,10,000</u>	<u>60,000</u>	<u>3,60,000</u>
		40,50,000		21,60,000
Less: Trade payables		<u>(6,00,000)</u>		<u>(3,60,000)</u>
		34,50,000		18,00,000

iii. **Profit and Loss Account balance of Black Ltd. as on 1.07.2020**

	Rs.
P & L A/c balance as on 31.03.2020	7,20,000
Less: Dividend paid	<u>(6,00,000)</u>
	1,20,000
Add: Estimated profit for 3 months after charging depreciation	<u>4,80,000</u>
	6,00,000

iv. Property, plant and equipment as on 01.07.2020

Property, plant and equipment of Black Ltd. as on 31.03.2020		36,00,000
Less: Depreciation for 3 months $[36,00,000 \times 10\% \times 3/12]$		(90,000)
Property, plant and equipment of White Ltd. Taken over as on 31.03.2020	24,00,000	35,10,000
Less: Proportionate depreciation for 3 months on fixed assets	<u>(60,000)</u>	
	23,40,000	
Add: Appreciation above the estimated book value	<u>1,20,000</u>	<u>24,60,000</u>
Total Property, plant and equipment as on 1.7.2020		<u>59,70,000</u>

QUESTION 34: (Q.AMG.RMP.503(A) RTP – Nov19 & Nov23, MTP Nov21)

The following is the summarized Balance Sheet of A Ltd. as at 31st March, 2019:

Liabilities	Amount	Assets	Amount
8,000 Equity shares of 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
Total	17,60,000	Total	17,60,000

B Ltd. agreed to absorb A Ltd. on the following terms and conditions:

- 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.
- B Ltd. is to take over trade payables at book value.
- The purchase consideration is to be paid in cash to the extent of 6,00,000/- and the balance in fully paid equity shares of 100/- each at 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.**SOLUTION****Books of A Limited
Realization Account**

Particulars	Rs.	Particulars	Rs.
To Building	3,40,000	By Trade payables	3,20,000
To Machinery	6,40,000	By B Ltd.	12,10,000
To Inventory	2,20,000	By Equity Shareholders (Loss)	76,000
To Trade receivables	2,60,000		
To Patent	1,30,000		
To Bank (Exp.)	16,000		
	16,06,000		16,06,000

Bank Account

To Balance b/d	1,36,000	By Realization (Exp.)	16,000
To B Ltd.	6,00,000	By 10% Debentures	4,00,000
		By Loan	1,60,000
		By Equity shareholders	1,60,000
	7,36,000		7,36,000

Equity Share Holders Account

To Realization Account	76,000	Equity share capital	8,00,000
To Share issue Expenses	34,000	General reserve	80,000
To Equity shares in B Ltd.	6,10,000		
To Bank	1,60,000		
	8,80,000		8,80,000

B Ltd**Balance Sheet as on 1st April, 2019 (An extract)**

	Particulars	Notes	Rs.
	EQUITY AND LIABILITIES		
1	Shareholders' funds		
a	Share capital	1	4,88,000
b	Reserves and Surplus	2	1,07,000
2	Current liabilities		
a	Trade Payables	3	2,80,000
b	Bank overdraft		6,00,000
			14,75,000
	ASSETS		
1	Non-current assets		
	Property, Plant and Equipment		
A	Tangible assets	4	8,82,000
B	Intangible assets	5	2,16,000
2	Current assets		
a	Inventories	6	1,83,000
b	Trade receivables	7	1,94,000
			14,75,000

Notes to Accounts

Sr. No.	Particulars		Rs.
1	Share Capital		
	Equity share capital		
	4,880 Equity shares of 100 each (Shares have been issued for consideration other than cash)		4,88,000
	Total		4,88,000
2	Reserves and Surplus (an extract)		
	Securities Premium		1,22,000
	Profit and loss account		
	Less: Unrealized profit	(15,000)	(15,000)
	Total		1,07,000
3	Trade payables		
	Opening balance	3,20,000	
	Less: Inter-company transaction cancelled upon amalgamation	(40,000)	2,80,000

4	Tangible assets		
	Buildings		3,06,000
	Machinery		5,76,000
	Total		8,82,000
5	Intangible assets		
	Goodwill		2,16,000
6	Inventories		
	Opening balance	1,98,000	
	Less: Cancellation of profit upon amalgamation	(15,000)	1,83,000
7	Trade receivables		
	Opening balance	2,34,000	
	Less: Intercompany transaction cancelled upon amalgamation	(40,000)	1,94,000

Working Notes:

1. Valuation of Goodwill	Rs.
Average profit	1,24,400
Less: 8% of Rs. 8,80,000	(70,400)
Super profit	54,000
Value of Goodwill = 54,000 x 4	2,16,000
1. Net Assets for purchase consideration	
Goodwill as valued in W.N.1	2,16,000
Building	3,06,000
Machinery	5,76,000
Inventory	1,98,000
Trade receivables (2,60,000-26,000)	2,34,000
Total Assets	15,30,000
Less: Trade payables	(3,20,000)
Net Assets	12,10,000

Out of this Rs. 6,00,000 is to be paid in cash and remaining i.e., (12,10,000 – 6,00,000) Rs. 6,10,000 in shares of 125/-. Thus, the number of shares to be allotted $6,10,000/125 = 4,880$ shares.

3. Unrealized Profit on Inventory	Rs.
The Inventory of A Ltd. includes goods worth Rs. 1,00,000 which was sold by B Ltd. on profit. Unrealized profit on this Inventory will be 40,000. $40000 \times 100000 / 160000$	25,000
As B Ltd purchased assets of A Ltd. at a price 10% less than the book value, 10% need to be adjusted from the Inventory i.e., 10% of Rs. 1,00,000.	(10,000)
Amount of unrealized profit	15,000

QUESTION 35: (Q.AMG.RMP.504(A) RTP – May'21)

Mohan Ltd. gives you the following information as on 31st March, 2020:

	Rs.
Share capital:	
Equity shares of Rs. 10 each	3,00,000
6,000, 9% cumulative preference shares of Rs. 10 each	60,000
Profit and Loss Account (Dr. balance)	1,70,000
10% Debentures of Rs. 100 each	2,00,000

Interest payable on Debentures	20,000
Trade Payables	1,50,000
Property, Plant and Equipment	3,40,000
Goodwill	10,000
Inventory	80,000
Trade Receivables	1,10,000
Bank Balance	20,000

A new company Ravi Ltd. is formed with authorised share capital of Rs. 4,00,000 divided into 40,000 Equity Shares of Rs. 10 each. The new company will acquire the assets and liabilities of Mohan Ltd. on the following terms:

i)

- Mohan Ltd.'s debentures are paid by similar debentures in new company and for outstanding accrued interest on debentures, equity shares of equal amount are issued at par.
- The trade payables are paid by issue of 12,000 equity shares at par in full and final settlement of their claims.
- Preference shareholders are to get equal number of equity shares issued at par. Dividend on preference shares is in arrears for three years. Preference shareholders to forgo dividend for two years. For balance dividend, equity shares of equal amount are issued at par.
- Equity shareholders are issued one share at par for every three shares held in Mohan Ltd.

ii) Current Assets are to be taken at book value (except inventory, which is to be reduced by 10%). Goodwill is to be eliminated. The Property, plant and equipment is taken over at Rs. 3,08,400.

iii) Remaining equity shares of the new company are issued to public at par fully paid up.

iv) Expenses of Rs. 5,000 to be met from bank balance of Mohan Ltd. This is to be adjusted from the bank balance of Mohan Ltd. before acquisition by Ravi Ltd.

You are required to prepare:

(a) Realisation account and Equity Shareholders' account in the books of Mohan Ltd.

(b) Bank Account and Balance Sheet with notes to accounts in the books of Ravi Ltd.

SOLUTION

In the books of Mohan Ltd.

i)

Realisation Account

	Rs.		Rs.
To Goodwill	10,000	By 10% Debentures	2,00,000
To Property, plant and Equipment	3,40,000	By Interest accrued on	20,000
To Inventory	80,000	By Trade payables	1,50,000
To Trade receivables	1,10,000	By Ravi Ltd. (Purchase consideration) (W.N. 1)	1,65,400
To Bank (20,000 - 5,000)	15,000	By Equity shareholders A/c (loss on realization) (Bal. fig.)	25,000
To Preference shareholders A/c (W.N.2)	5,400		
	5,60,400		5,60,400

ii)

Equity shareholders' Account

	Rs.		Rs.
To Profit & loss A/c	1,70,000	By Equity Share capital	3,00,000
To Expenses*	5,000		
To Equity shares in Ravi Ltd.	1,00,000		
To Realization A/c	25,000		
	3,00,000		3,00,000

*Alternatively, expenses may be routed through Realization account.

In the books of Ravi Ltd.**i) Bank Account**

	Rs.		Rs.
To Business Purchase	15,000	By Balance c/d (Bal. fig.)	1,09,600
To Equity shares application & allotment A/c (W.N. 3)	94,600		
	1,09,600		1,09,600

ii) Balance Sheet as at 31st March, 2020

Particulars	Note No.	Rs.
I. Equity and Liabilities		
(1) Shareholder's Funds		
Share Capital	1	4,00,000
(2) Non-Current Liabilities		
Long-term borrowings	2	<u>2,00,000</u>
Total		<u>6,00,000</u>
II. Assets		
(1) Non-current assets		
(a) Property, plant and equipment		3,08,400
(2) Current assets		
(a) Inventories		72,000
(b) Trade receivables		1,10,000
(c) Cash and cash equivalents		<u>1,09,600</u>
Total		<u>6,00,000</u>

Notes to Accounts

		Rs.
1	Share Capital Authorised share capital 40,000 equity shares of Rs. 10 each Issued and Subscribed 40,000 shares of Rs. 10 each fully paid up (Out of the above, 30,540 (W.N.3) shares have been allotted as fully paid-up pursuant to contract without payment being received in cash)	<u>4,00,000</u> 4,00,000
2	Long Term Borrowings 10% Debentures	2,00,000

Working Notes:**1. Calculation of Purchase consideration**

	Rs.
Payment to preference shareholders	
6,000 equity shares @ Rs. 10	60,000
For arrears of dividend: (6,000 x Rs. 10) x 9%	5,400
Payment to equity shareholders	
(30,000 shares x 1/3) @ Rs. 10	<u>1,00,000</u>
Total purchase consideration	<u>1,65,400</u>

2. Preference shareholders' Account in books of Mohan Ltd.

	Rs.		Rs.
To Equity Shares in Ravi Ltd.	65,400	By Preference Share capital	60,000
		By Realization A/c (Bal. fig.)	5,400
	65,400		65,400

3. Calculation of number of Equity shares issued to public

	Number of shares	
Authorized equity shares		40,000
Less: Equity shares issued for		
Interest accrued on debentures	2,000	
Trade payables of Mohan Ltd.	12,000	
Preference shareholders of Mohan Ltd.	6,000	
Arrears of preference dividend	540	
Equity shareholders of Mohan Ltd.	<u>10,000</u>	<u>(30,540)</u>
Number of equity shares issued to public at par for cash		<u>9,460</u>

QUESTION 36: (Q.AMG.RMP.302(B) MTP – May19 & Nov18)

The following were the summarized Balance Sheets of P Ltd. and V Ltd. as at 31 -3-20X1:

Liabilities	P Ltd. (Rs. in lakhs)	V Ltd. (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	<u>1,830</u>	<u>702</u>
	33,400	12,500
Assets	P Ltd. (Rs. in lakhs)	V Ltd. (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. (Rs. in lakhs)	V Ltd. (Rs. in lakhs)
Trade payables		
Bills Payable	120	–
Creditors	<u>1,080</u>	<u>463</u>
	1,200	463

Trade receivables		
Debtors	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) Prepare 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.

SOLUTION

		(Rs. in lacs)	(Rs. In lacs)
		Debit	Credit
Business Purchase A/c Dr. To Liquidator of V Ltd. (Being business of V Ltd. taken over for consideration settled as per agreement)		9,000	9,000
Plant and Machinery Dr. Furniture & Fittings Dr. Inventory Dr. Debtors Dr. Cash at Bank Dr. Bills Receivable Dr. To Foreign Project Reserve To General Reserve (3,200 - 3,000) To Profit and Loss A/c (825 - 50*) To Liability for 12% Debentures To Creditors To Provisions To Business Purchase (Being assets & liabilities taken over from V Ltd.)		5,000 1,700 4,041 1,020 609 80	310 200 775 1,000 463 702 9,000
Liquidator of V Ltd. A/c Dr. To Equity Share Capital A/c (Purchase consideration discharged in the form of equity shares)		9,000	9,000
Profit & loss A/c Dr. To Bank A/c (Liquidation expenses paid by P Ltd.)		1	1
Liability for 12% Debentures A/c Dr. To 13% Debentures A/c (12% debentures discharged by issue of 13% debentures)		1,000	1,000
Bills Payable A/c Dr. To Bills Receivable A/c (Cancellation of mutual owing on account of bills)		80	80

Balance Sheet of P Ltd. as at 1st April, 20X1 (after merger)

	Particulars	Notes	Rs. (in lakhs)
	Equity and Liabilities		
1	Shareholders' funds		
	A Share capital	1	24,000
	B Reserves and Surplus	2	16,654
2	Non-current liabilities		
	A Long-term borrowings	3	1,000

3		Current liabilities		
	A	Trade Payables (1,543 + 40)		1,583
	B	Short-term provisions		2,532
		Total		45,769
		Assets		
1		Non-current assets		
	A	Fixed assets		
		Tangible assets	4	29,004
2		Current assets		
	A	Inventories		11,903
	B	Trade receivables		3,140
	C	Cash and cash equivalents		1,722
		Total		45,769

Notes to accounts

		Rs.
1.	Share Capital	
	Equity share capital	
	Authorised, issued, subscribed and paid up	
	24 crores equity shares of Rs. 10 each (Of the above shares, 9 crores shares have been issued for consideration other than cash)	<u>24,000</u>
	Total	<u>24,000</u>
2.	Reserves and Surplus	
	General Reserve	9,700
	Securities Premium	3,000
	Foreign Project Reserve	310
	Profit and Loss Account	<u>3,644</u>
	Total	<u>16,654</u>
3.	Long-term borrowings	
	Secured	
	13% Debentures	1,000
4.	Tangible assets	
	Land & Buildings	6,000
	Plant & Machinery	19,000
	Furniture & Fittings	<u>4,004</u>
	Total	<u>29,004</u>

Working Note:

Computation of purchase consideration

The purchase consideration was discharged in the form of three equity shares of P Ltd. for every two equity shares held in V Ltd.

Purchase consideration = Rs 6,000 lacs $\times \frac{3}{2}$ = Rs. 9,000 lacs.

* Cost of issue of debenture adjusted against P & L Account of V Ltd.

7. CONSOLIDATED FINANCIAL STATEMENT

(AS 21)

QUESTION 37 (EXAM MAY'25)

Rubber Ltd. Purchased 70% of shares of Tyre Ltd. on 31/03/2024 for ₹ 4,05,000. The following is the position of tyre Ltd. as on that date:

Particulars	Amount (₹)
Issued share capital of Tyre Ltd. on 31/03/2024	5,00,000
Balance in Profit and Loss A/c of Tyre Ltd. on 31/03/2024	70,000
Profit earned during the year 2024-25	45,000
5% Dividend declared and paid by Tyre Ltd. for 2023-24	25,000

You are required to calculate:

The capital reserve / goodwill at the date of acquisition

The calculations are to be made under the following assumptions:

Case (i) It is assumed that the dividend is paid out of post-acquisition profits.

Case (ii) It is assumed that the dividend is received for pre-acquisition period.

SOLUTION

Calculation of capital reserve / goodwill at the date of acquisition

Case (i) it is assumed Dividend is paid out of Post – acquisition Profits

Total dividend paid is ₹ 25,000 hence dividend received by Rubber will be credited to P & L.

Rubber Ltd.'s share of dividend = ₹ 25,000 x 70% = ₹ 17,500.

Goodwill on consolidation (at the date of acquisition):	₹	₹
Cost of shares		4,05,000
Less: Face value of capital i.e. 70% of capital 5,00,000	3,50,000	
Add: Share of Capital profits [70,000 x 70%]	49,000	(3,99,000)
Goodwill		6,000

Case (ii) it is assumed Dividend is received out of pre-acquisition profits.

Since dividend received is for pre-acquisition period, it has been reduced from the cost of investment in the subsidiary company.

Goodwill on consolidation (at the date of acquisition):	₹	₹
Cost of shares		4,05,000
Less: dividend received		(17,500)
		3,87,500
Less: Face value of capital i.e. 70% of capital 5,00,000	3,50,000	
Add: Share of Capital profits [70,000 x 70%]	49,000	(3,99,000)
Capital reserve		11,500

QUESTION 38: (Q.CFS.RMP.103(A) RTP Nov'21 & Similar in ICAI Module)

On 31st March, 2015, P Ltd. acquired 1,05,000 shares of Q Ltd. for Rs. 12,00,000. The position of Q Ltd. on that date was as under:

	Rs.
Property, plant and equipment	10,50,000
Current Assets	6,45,000

1,50,000 equity shares of Rs. 10 each fully paid	15,00,000
Pre-incorporation profits	30,000
Profit and Loss Account	60,000
Trade payables	1,05,000

P Ltd. and Q Ltd. give the following information on 31st March, 2021:

	P Ltd.	Q Ltd.
	Rs.	Rs.
Equity shares of Rs. 10 each fully paid (before bonus issue)	45,00,000	15,00,000
Securities Premium	9,00,000	–
Pre-incorporation profits	–	30,000
General Reserve	60,00,000	19,05,000
Profit and Loss Account	15,75,000	4,20,000
Trade payables	5,55,000	2,10,000
Property, plant and equipment	79,20,000	23,10,000
Investment: 1,05,000 Equity shares in Q Ltd. at cost	12,00,000	–
Current Assets	44,10,000	17,55,000

Directors of Q Ltd. made bonus issue on 31.3.2021 in the ratio of one equity share of Rs. 10 each fully paid for every two equity shares held on that date. Bonus shares were issued out of post-acquisition profits by using General Reserve.

Calculate as on 31st March, 2021

- (i) Cost of Control/Capital Reserve;
- (ii) Minority Interest;
- (iii) Consolidated Profit and Loss Account in each of the following cases:
 - Before issue of bonus shares.
 - Immediately after issue of bonus shares.

SOLUTION

Shareholding pattern

Particulars	Number of Shares	% of holding
P Ltd.		
(i) Purchased on 31.03.2015	1,05,000	
(ii) Bonus Issue (1,05,000/2)	52,500	
Total	1,57,500	70%
a. Minority Interest	67,500	30%

Calculations of (i) Cost of Control/Capital Reserve; (ii) Minority Interest; (iii) Consolidated Profit and Loss Account as on 31st March, 2021:

• Before issue of bonus shares

(i)	Cost of control/capital reserve	Rs.	Rs.
	Investment in Q Ltd.		12,00,000
	Less: Face value of investments	10,50,000	
	Capital profits (W.N.)	63,000	(11,13,000)
	Cost of control		87,000
(ii)	Minority Interest		Rs.
	Share Capital		4,50,000
	Capital profits (W.N.)		27,000
	Revenue profits (W.N.)		6,79,500
			11,56,500

(iii)	Consolidated profit and loss account – P Ltd.		Rs.
	Balance		15,75,000
	Add: Share in revenue profits of Q Ltd. (W.N.)		15,85,500
			31,60,500

b. Immediately after issue of bonus shares

(i)	Cost of control/capital reserve	Rs.	Rs.
	Face value of investments (Rs. 10,50,000 + Rs. 5,25,000)	15,75,000	
	Capital Profits (W.N.)	63,000	16,38,000
	Less: Investment in Q Ltd.		(12,00,000)
	Capital reserve		4,38,000
(ii)	Minority Interest		Rs.
	Share Capital (Rs. 4,50,000 + Rs. 2,25,000)		6,75,000
	Capital Profits (W.N.)		27,000
	Revenue Profits (W.N.)		4,54,500
			11,56,500
(iii)	Consolidated Profit and Loss Account – P Ltd.		Rs.
	Balance		15,75,000
	Add: Share in revenue profits of Q Ltd. (W.N.)		10,60,500
			26,35,500

Working Note:

Analysis of Profits of Q Ltd.

	Capital Profits	Revenue Profits	
	(Before and after issue of bonus shares) Rs.	Before Bonus Issue Rs.	After Bonus Issue Rs.
Pre-incorporation profits	30,000		
Profit and loss account on 31.3.2015	60,000		
General reserve*	90,000	19,05,000	19,05,000
Less: Bonus shares			(7,50,000)
			11,55,000

Profit for period of 1st April, 2015 to 31 st March, 2021 (Rs. 4,20,000 – Rs. 60,000)		3,60,000	3,60,000
		22,65,000	15,15,000
P Ltd.'s share (70%)	63,000	15,85,500	10,60,500
Minority's share (30%)	27,000	6,79,500	4,54,500

*Share of P Ltd. in General reserve has been adjusted in Consolidated Profit and Loss Account.

QUESTION 39: (Q.CFS.RMP.104(A) Exam Nov'23)

GB Limited acquired 80% of equity shares of TB Limited on 1st April, 2016 at a cost of Rs. 58,00,000 when TB Limited had an Equity share capital of Rs. 50,00,000 and Reserves and Surplus of Rs. 4,64,000.

The following information is provided:

Year	Profit / (Loss) of TB Limited (Rs.)
2016-17	(14,50,000)
2017-18	(23,20,000)
2018-19	(29,00,000)
2019-20	(6,96,000)
2020-21	1,90,000
2021-22	6,80,000
2022-23	12,70,000

You are required to calculate the minority interests and cost of control at the end of each year for the purpose of consolidation.

SOLUTION

Year	Profit / (Loss)	Minority Interest (20%)	Additional Consolidated P & L (Dr.) Cr.	Minority's Share of losses borne by GB Ltd.		Cost of Control
				Rs.	Balance	
At the time of acquisition in 2016		10,92,800	-			
2016-17	(14,50,000)	(2,90,000)	(11,60,000)			14,28,800 (W.N.)
Balance		8,02,800				
2017-18	(23,20,000)	(4,64,000)	(18,56,000)			14,28,800
Balance		3,38,800				
2018-19	(29,00,000)	(5,80,000)	(23,20,000)			14,28,800
		(2,41,200)				
	Loss of minority borne by Holding Co.	<u>2,41,200</u>	<u>(2,41,200)</u>	2,41,200	2,41,200	
Balance		Nil	<u>(25,61,200)</u>			
2019-20	(6,96,000)	(1,39,200)	(5,56,800)			14,28,800
	Loss of minority borne by Holding Co.	<u>1,39,200</u>	<u>(1,39,200)</u>	1,39,200	3,80,400	
Balance		Nil	(6,96,000)			
2020-21	1,90,000	38,000	1,52,000			14,28,800
	Profit share of minority adjusted against losses of minority absorbed by Holding Co.	(38,000)	<u>38,000</u>	(38,000)	3,42,400	
Balance		Nil	1,90,000			

CA Intermediate				Advanced Accounts		
2021-22	6,80,000	1,36,000	5,44,000			
	Profit	<u>(1,36,000)</u>	<u>1,36,000</u>	(1,36,000)	2,06,400	14,28,800
	share of minority adjusted against losses of minority absorbed by Holding Co.					
Balance		Nil	6,80,000			
2022-23	12,70,000	2,54,000	10,16,000	(2,06,400)	Nil	14,28,800
		<u>(2,06,400)</u>	<u>2,06,400</u>			
Balance		47,600	12,22,400			

Working Note:

Calculation of Minority interest and Cost of control on 1.4.2016

		Share of Holding Co.	Minority Interest
	100%	80%	20%
	(Rs.)	(Rs.)	(Rs.)
Share Capital	50,00,000	40,00,000	10,00,000
Reserve	4,64,000	<u>3,71,200</u>	<u>92,800</u>
		43,71,200	<u>10,92,800</u>
Less: Cost of investment		<u>(58,00,000)</u>	
Goodwill		14,28,800	

QUESTION 40: (Q.CFS.SM.202(A))

Exe Ltd. acquires 70% of equity shares of Zed Ltd. as on 31st March, 2017 at a cost of ₹ 70 lakhs. The following information is available from the balance sheet of Zed Ltd. as on 31st March, 2017:

	₹ in lakhs
Property, plant & Equipment	120
Investments	55
Current Assets	70
Loans & Advances	15
15% Debentures	90
Current Liabilities	50

The following revaluations have been agreed upon (not included in the above figures):

Property, plant & Equipment Up by 20%

Investments Down by 10%

Zed Ltd. **declared and paid dividend @ 20%** on its equity shares as on 31st March, 2017. Exe Ltd. purchased the shares of Zed Ltd. @ ₹20 per share.

Calculate the amount of goodwill/capital reserve on acquisition of shares of Zed Ltd.

SOLUTION**Revalued net assets of Zed Ltd. as on 31st March, 2017**

	₹ in lakhs	₹ in lakhs
Property, plant & Equipment [120 X 120%]		144.0
Investments [55 X 90%]		49.5
Current Assets		70.0
Loans and Advances		15.0
Total Assets after revaluation		278.5
Less: 15% Debentures	90.0	
Current Liabilities	50.0	(140.0)
Equity / Net Worth		138.5
Exe Ltd.'s share of net assets (70% of 138.5)		96.95
Exe Ltd.'s cost of acquisition of shares of Zed Ltd. (₹70 lakhs – ₹7 lakhs*)		63.00
Capital reserve		33.95

* Total Cost of 70 % Equity of Zed Ltd	₹ 70 lakhs
Purchase Price of each share	₹ 20
Number of shares purchased [70 lakhs / ₹ 20]	3.5 lakhs
Dividend @ 20 % i.e., ₹ 2 per share	₹ 7 lakhs

Since dividend received is for pre-acquisition period, it has been reduced from the cost of investment in the subsidiary company.

QUESTION 41: (Q.CFS.RMP.305(A) RTP Nov'22)

On 31st March, 2022, H Ltd. and S Ltd. give the following information:

	H Ltd. (Rs. in 000's)	S Ltd. (Rs. in 000's)
Equity Share Capital – Authorised	5,000	3,000
Issued and subscribed in Equity Shares of Rs. 10 each fully paid	4,000	2,400
General Reserve	928	690
Profit and Loss Account (Cr. Balance)	1,305	810
Trade payables	611	507
Provision for Taxation	220	180
Other Provisions	65	17
Plant and Machinery	2,541	2,450
Furniture and Fittings	615	298
Investment in the Equity Shares of S Ltd.	1,500	-
Inventory	983	786
Trade receivables	820	778
Cash and Bank Balances	410	102
Sundry Advances (Dr. balances)	260	190

Following Additional Information is available:

- (a) H Ltd. purchased 90 thousand Equity Shares in S Ltd. on 1st April, 2021. On that date the following balances stood in the books of S Ltd.:

General Reserve Rs. 1,500 thousand; Profit and Loss Account Rs. 633 thousand.

- (b) On 14th July, 2021 S Ltd. declared a dividend of 20% out of pre-acquisition profits. H

Ltd. credited the dividend received to its Profit and Loss Account.

- (c) **On 1st November, 2021, S Ltd. issued 3 fully paid Equity Shares of Rs. 10 each, for every 5 shares held as bonus shares out of pre-acquisition General Reserve.**
- (d) On 31st March, 2022, the Inventory of S Ltd. included goods purchased for Rs. 50 thousand from H Ltd., which had made a profit of 25% on cost.
- (e) Details of Trade payables and Trade receivables:

	H Ltd. (Rs. in 000's)	S Ltd. (Rs. in 000's)
Trade payables		
Bills Payable	124	80
Sundry creditors	487	427
	611	507
Trade receivables		
Debtors	700	683
Bills Receivables	120	95
	820	778

Prepare a consolidated Balance Sheet as at 31st March, 2022.

SOLUTION

Consolidated Balance Sheet of H Ltd. with its subsidiary S Ltd. as at 31st March, 2022

Particulars	Note No.	(Rs. in 000's)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	4,000
(b) Reserves and Surplus	2	3,063
(2) Minority Interest (W.N.6)		1,560
(3) Current Liabilities		
Trade payables	3	1,118
Short term provisions	4	482
Total		10,223
II. Assets		
(1) Non-current assets		
PPE	5	5,904
(2) Current assets		
(a) Inventories	6	1,759
(b) Trade receivables	7	1,598
(c) Cash and cash equivalents	8	512
(d) Short term loans and advances	9	450
Total		10,223

Notes to Accounts

		(Rs. in 000's)	(Rs. in 000's)
1. Share Capital			5,000
Authorised share capital			
5 lakhs equity shares of Rs. 10 each			
Issued, Subscribed and Paid up			

	4 lakhs equity shares of Rs. 10 each fully paid		4,000
2.	Reserves and surplus		
	Capital Reserve (Note 5)	679.8	
	General Reserve	928	
	Profit and Loss Account:		
	H Ltd. Rs. 1,305		
	Add: Share in S Ltd Rs. 340.20		
	Rs. 1,645.20		
	Less: Dividend wrongly credited Rs. (180)		
	Rs. 1,465.20		
	Less: Unrealised profit (50 X 1/5) Rs. (10)	1,455.20	3,063
3.	Trade payables		
	H Ltd.	611	
	S Ltd.	507	1,118
4.	Short –term provisions		
	Provision for Taxation H Ltd. Rs. 220		
	S Ltd. Rs. 180	400	
	Other Provisions H Ltd Rs. 65		
	S Ltd. Rs. 17	82	482
5.	PPE		
	Plant and Machinery		
	H Ltd. Rs. 2,541		
	S Ltd. Rs. 2,450	4,991	
	Furniture and fittings		
	H Ltd. Rs. 615		
	S Ltd. Rs. 298	913	5,904
6.	Inventories		
	Inventory H Ltd. Rs. 983		
	S Ltd. Rs. 786	1,769	
	Less: Unrealised profit (Rs. 50 x 1/5)	(10)	1,759
7.	Trade receivables		
	H Ltd.	820	
	S Ltd.	778	1,598
8.	Cash and cash equivalents		
	Cash and Bank Balances H Ltd	410	
	S Ltd.	102	512
9.	Short term loans and advances		
	Sundry Advances H Ltd.	260	
	S Ltd.	190	450

Working Notes:**Share holding pattern**

Particulars	Number of Shares	% of holding
a. S Ltd.		
(i) Purchased on 01.04.2021	90,000	
(ii) Bonus Issue (90,000/5 x 3)	54,000	
Total	1,44,000	60% (1,44,000 / 2,40,000 * 100)
b. Minority Interest	96,000	40%

*2,40,000 is after issue of bonus shares as per balance sheet as at 31.3.2022

1. S Ltd. General Reserve

	(Rs. in 000)			(Rs. in 000)	
To	Bonus to equity shareholders (2,400/8 x 3)	900	By	Balance b/d	1,500
To	Balance c/d	690	By	Profit and Loss A/c (Balancing figure)	90
		1,590			1,590

2. S Ltd.'s Profit and Loss Account

		(Rs. in 000)			(Rs. in 000)
To	General Reserve	90	By	Balance b/d	633
To	Dividend paid on 14.7.2021 (1,500/100 x 20)	300	By	Net Profit for the year (Bal. fig.)	567*
To	Balance c/d	810			
		1,200			1,200

* Out of Rs. 5,67,000 profit for the year, Rs. 90,000 has been transferred to reserves by S Ltd.

3. Distribution of Revenue Profits

	Rs. in '000
Revenue Profit as above	567.00
Share of H Ltd. (60%)	340.20
Share of Minority shareholders (567- 340.20)	226.80

4. Computation of Capital Profits

	Rs. in 000	Rs. in 000
General Reserve on the date of acquisition		1,500
Less: Bonus issue of shares		(900)
		600
Profit and Loss Account balance on the date of acquisition	633	
Less: Dividends paid	(300)	333
		933
Share of H Ltd. (60%)		559.80
Share of Minority shareholders		373.20

5. Computation of Capital Reserve

	Rs. in '000	
60% of share capital of S Ltd.		1,440
Add: Share of H Ltd. in the capital profits as in W.N. (4)		559.80
		1,999.80
Less: Investments in S Ltd.	1,500	
Less: Dividends received out of pre- acquisition profits Rs. 300/100 x 60	(180)	(1,320)
		679.80

6. Calculation of Minority Interest

	Rs. in '000
40% of share capital of S Ltd.	960.00
Add: Share of Revenue Profits (Note 3)	226.80
Share of Capital Profits (Note 4)	373.20
	1,560.00

QUESTION 42: (Q.CFS.RMP.306(A) RTP Nov'18) (Similar to Q305A)

The Summarised Balance Sheet of X Ltd. and its subsidiary Y Ltd. as on 31st March, 2017 are as follows:

Particulars	Amounts as at 31st March, 2017	
	X Ltd. (Rs in lakhs)	Y Ltd. (Rs in lakhs)
LIABILITIES		
Share Capital:		
Authorised	20,000	8,000
Issues and subscribed:		
Equity share of Rs. 10 each, fully paid up	15,000	6,000
15% preference shares of Rs. 10 each, fully paid up	4,000	1,000
General Reserves	2,500	1,450
Profit & Loss Account	2,750	1,250
Trade payables	1,646	1,027
	25,896	10,727
ASSETS		
Land & Building	3,550	1,510
Plant & Machinery	5,275	3,600
Furniture & Fittings	1,945	655
Investment in Y Ltd.: 450 Lakh Equity share in Y Ltd. purchased on 1st April, 2016	6,800	-
Inventory	4,142	2,520
Trade Receivables	3,010	1,882
Cash and Bank Balance	1,174	560
	25,896	10,727

The following information is also given to you:

- 10% dividend on Equity shares was declared by Y Ltd. on 31st March, 2016 for the year ended 31st March, 2016. X Ltd. credited the dividend received to its Profit & Loss Account.**
- Credit Balance of Profit & Loss account of Y Ltd. as on 1st April, 2016 was Rs 650 Lakhs.
- General Reserve of Y Ltd. stood at same Rs 1,450 Lakhs as on 1st April, 2016.
- Y Ltd.'s Plant & machinery showed a balance of Rs 4,000 Lakh on 1st April 2016. At the time of purchase of shares in Y Ltd., X Ltd. revalued Y's Ltd. Plant & Machinery upward by Rs 1,000 Lakh.**
- Included in Trade Payables of Y Ltd. are Rs 50 Lakh for goods supplied by X Ltd.
- On 31st March, 2017, Y's ltd. inventory included goods for Rs 150 lakhs which it had purchased from X Ltd. X Ltd. sold goods to Y Ltd. at cost plus 25%.**

You are required to prepare a Consolidated Balance Sheet of X Ltd. and its subsidiary Y Ltd. as on 31st March, 2017 giving working notes.

SOLUTION**Consolidated Balance Sheet of X Ltd. and its subsidiary Y Ltd.as on 31st March, 2017**

Particulars		Note No.	Rs in lakhs
I	Equity and Liabilities		
1.	Shareholders' Funds		
(a)	Share Capital	1	19,000
(b)	Reserves and Surplus	2	5,620
2.	Minority interest	3	3,400
3.	Current Liabilities		
(a)	Trade payables	4	2,623
Total			30,643
II	Assets		
1	Non-Current Assets		
	Fixed Assets		
(i)	Tangible Assets	5	17,435
2	Current Assets		
(a)	Inventories	6	6,632
(b)	Trade Receivables	7	4,842
(c)	Cash and Cash equivalents	8	1,734
Total			30,643

Notes to Accounts

		Rs in lakhs	
1.	Share Capital		
	Issued, Subscribed and Paid up (1,500 lakh Equity Shares of Rs 10 each fully paid up)		15,000
	400 lakh Preference Shares of Rs 10 each fully paid up		4,000
			19,000
2.	Reserves and Surplus		
	Credit Balance of Profit & Loss Account	2,750	
	Less: Capital Receipt wrongly credited (Dividend @ 10% on Rs 4500 Lakh Equity Shares)	450	
		2,300	
	Add: Share in Y Ltd. Revenue Profit (Working Note i)		825
		3,125	
	Less: Unrealised Profit (Working Note iv)	30	3,095
	Capital Reserve (Working Note iii)		25
	General Reserve	2,500	2,525
			5,620
3.	Minority interest		
	100 Lakh Preference Shares of Rs 10 fully paid up	1,000	
	150 Lakh Equity Shares of Rs10 each fully paid up	1,500	2,500
	Share in Revenue Profits (Working Note i)	275	
	Share in Capital Profit (working Note ii)	625	900
			3,400
4.	Trade payables		
	X Ltd.	1,646	
	Y Ltd.	1,027	
		2,673	
	Less: Mutual owing	50	2,623
5.	Tangible Assets		
	Land & Building		

X Ltd.	3,550	
Y Ltd	1,510	5,060
Plant & Machinery		
X Ltd.	5,275	
Y Ltd (Working note v)	4,500	9,775
Furniture & Fixtures		
X Ltd.	1,945	
Y Ltd	655	2,600
		17,435
6. Inventories		
X Ltd.	4,142	
Y Ltd	2,520	
	6,662	
Less: Unrealized Profit	(30)	6,632
7. Trade Receivables		
X Ltd.	3,010	
Y Ltd	1,882	
	4,892	
Less: Mutual Owing	50	4,842
8. Cash & cash Equivalents		
X Ltd.	1,174	
Y Ltd	560	1,734

Working Notes**(i) Calculation of Revenue Profits****Y's Ltd Profit & Loss Account**

	Rs in lakh		Rs in lakh
To Equity Dividend		By Balance b/d	650
10 % of 6,000 lakh	600	By Net profit for the year (Bal Fig.)	1,200
To balance c/d	1,250		
	1,850		1,850

Depreciation provided on Plant & Machinery

Balance as on 1st April, 2016	4,000
Less Balance as 31st March 2017	3,600
	400
Hence rate of Depreciation = $400/4000 \times 100$	10%
Net Profit for the year ended 31st March 2017	1,200
Less: Additional Depreciation	100
Revenue Profit	1,100
X Ltd.'s share- $1100 \times 450/600$	825
Y Ltd.'s share = $1100 \times 150/600$	275

(ii) Calculation of Capital Profits

Profit & Loss Balance as on 1st April, 2016	650
Less: Dividend Paid	600
	50
Add: General Reserve as on 1st April, 2016	1,450
Add: Profit on Revaluation of Plant & machinery	1,000
Capital Profit	2,500

X Ltd.'s Share in Capital Profit = $2,500 \times 450/600$	1,875
Y Ltd.'s Share in Capital Profit = $2,500 \times 150/600$	625

(iii) Calculation of Capital Reserve

Paid up value of 450 Lakh equity shares	4,500
Add: Share in Capital Profits	1,875
	6,375
Amount Paid to acquire the 450 Lakh Equity Shares	6,800
Less: Dividend received out of Pre acquisition profits	450
	6,350
Capital Reserve = $6,375 - 6,350$	25

(iv) Unrealised Profit

Rs 150 Lakh $\times 25/125^* = 30$ lakh

(v) Plant & Machinery of Y Ltd.

Balance as on 31st March, 2017		3,600
Add: Addition due to revaluation	1,000	
Less: Depreciation on additional Value of Plant & Machinery @ 10 %	100	900
		4,500

* Rs 150 lakh considered as cost to Y ltd.

QUESTION 43: (Q.CFS.RMP.402 (A) EXAM May'23)

G Ltd. and its subsidiary K Ltd. give the following information for the year ended 31st March, 2023:

	G Ltd.	K Ltd.
	(₹ in Crores)	(₹ in Crores)
Sales and other income	3,000	750
Increase in Inventory	750	100
Raw material consumed	600	100
Wages and Salaries	600	75
Production expenses	100	50
Administrative Expenses	75	50
Selling and Distribution Expenses	100	25
Interest	75	30
Depreciation	75	30

The following information is also given:

- G Ltd. sold goods of Rs. 200 crores to K Ltd. at cost plus 25% ($1/5^{\text{th}}$ of such goods were still in inventory of K Ltd. at the end of the year)
- G Ltd. holds 75% of the Equity share capital of K Ltd. and the Equity share capital of K Ltd. is ₹ 800 crores on 01.04.2022 (date of acquisition of shares)
- Administrative expenses of K Ltd. included ₹ 5 crore paid to G Ltd. as consultancy fees. Also, selling and distribution expenses of G Ltd. include ₹ 20 crores paid to K Ltd. as commission.

Prepare a consolidated statement of Profit and Loss of G Ltd. with its subsidiary K Ltd. for the year ended 31st March, 2023.

SOLUTION**Consolidated statement of profit and loss of G Ltd. and its subsidiary K Ltd.
for the year ended on 31st March, 2023**

Particulars	Note No.	₹ in Crores
Revenue from operations	1	3,525
Total Income		3,525
Expenses		650
Cost of material purchased/consumed	2	(842)
Changes of inventories of finished goods	3	675
Employee benefit expense	4	105
Finance cost	5	105
Depreciation and amortization expense	6	<u>225</u>
Other expenses	7	<u>918</u>
Total expenses		<u>2,607</u>
Profit before tax (II-III)		

Notes to Accounts

1	Revenue from operations Sales and other income G Ltd. K Ltd. Less: Inter-company sales Consultancy fees received by G Ltd. from K Ltd. Commission received by K Ltd. from G Ltd.	3,000 750 3,750 (200) (5) (20)	3,525
2	Cost of material purchased/consumed G Ltd. K Ltd. Less: Purchases by K Ltd. from G Ltd Direct expenses (Production) G Ltd. K Ltd	600 <u>100</u> 700 (200) 100 50	500 150 650
3	Changes of inventories of finished goods G Ltd. K Ltd.	750 <u>100</u> 850 <u>(8)</u>	842
4	Less: Unrealized profits Rs. 40 crores × 25/125		
5	Employee benefits and expenses Wages and salaries: G Ltd K Ltd.	600 <u>75</u> 75	675

6	Finance cost	30	105
	Interest:		
7	G Ltd.	75	
	K Ltd	30	105
7	Depreciation		
	G Ltd.		
7	K Ltd.	75	
	Other expenses	<u>50</u>	
7	Administrative expenses	125	
	G Ltd.	<u>(5)</u>	120
7	K Ltd.		
		100	
7	Less: Consultancy fees received by G Ltd. from	<u>25</u>	
	K Ltd	125	
7	Selling and distribution Expenses:	<u>(20)</u>	<u>105</u>
	G Ltd.		<u>225</u>
7	K Ltd.		
7	Less: Commission received by K Ltd. from G		
	Ltd.		

Note: The information (i) given in the question states that G Ltd. sold goods of ₹200 crores to K Ltd. at cost plus 25%. In the above solution it has been considered that the amount of ₹200 crores is sale value. Alternatively, ₹ 200 crores may be assumed as the cost of the goods sold. In that case, the solution will differ and will be as follows:

Alternative solution:

**Consolidated statement of profit and loss of G Ltd. and its subsidiary K Ltd.
for the year ended on 31st March, 2023**

Particulars	Note No.	₹ in Crores
Revenue from operations	1	<u>3,475</u>
Total income		<u>3,475</u>
<u>Expenses</u>		
Cost of material purchased /consumed	2	600
Changes of inventories of finished goods	3	(840)
Employee benefit expense	4	675
Finance cost	5	105
Depreciation and amortization expense	6	105
Other expenses	7	<u>225</u>
Total expenses		<u>870</u>
Profit before tax (II-III)		<u>2,605</u>

Notes to Accounts

		₹ in Crores	₹ in Crores
1	Revenue from operations		
	Sales and other income		
	G Ltd.	3,000	
	K Ltd	<u>750</u>	
		3,750	
	Less: Inter-company sales	(250)	

	Consultancy fees received by G Ltd. from K Ltd.	(5)	
	Commission received by K Ltd. from G Ltd.	<u>(20)</u>	3,475
2	Cost of material purchased/consumed		
	G Ltd.	600	
	K Ltd.	<u>100</u>	
		700	
	Less: Purchases by K Ltd. from G Ltd.	<u>(250)</u>	450
	Direct expenses (Production)		
	G Ltd.	100	
	K Ltd.	<u>50</u>	<u>150</u>
			<u>600</u>
3	Changes of inventories of finished goods		
	G Ltd.	750	
	K Ltd.	<u>100</u>	
		850	
	Less: Unrealized profits ₹ 40 crores × 25/100	<u>(10)</u>	<u>840</u>
4	Employee benefits and expenses		
	Wages and salaries:		
	G Ltd.	600	
	K Ltd.	<u>75</u>	<u>675</u>
5	Finance cost		
	Interest:		
	G Ltd.	75	
	K Ltd.	<u>30</u>	<u>105</u>
6	Depreciation		
	G Ltd.	75	
	K Ltd.	<u>30</u>	<u>105</u>
7	Other expenses		
	Administrative expenses		
	G Ltd.	75	
	K Ltd.	<u>50</u>	
		125	
	Less: Consultancy fees received by G Ltd. from K Ltd.	<u>(5)</u>	120
	Selling and distribution Expenses:	100	
	G Ltd.	<u>25</u>	
	K Ltd.	125	
		<u>(20)</u>	<u>105</u>
	Less: Commission received by K Ltd. from G Ltd.		<u>225</u>

QUESTION 44: (Q.CFS.SM.501(A))

Subsidiary B Ltd. provides the following balance sheet

Particulars	Note No.	20X0 (₹)	20X1 (₹)
Equity and Liabilities			
(I) Shareholder's Funds			
(a) Share Capital	1	5,00,000	5,00,000
(b) Reserves and Surplus	2	2,86,000	7,14,000
(2) Current Liabilities			
(a) Short term borrowings	3	--	1,70,000
(b) Trade Payables		4,90,000	4,94,000
(c) Short-term provisions	4	3,10,000	4,30,000
Total		15,86,000	23,08,000
II. Assets			
(1) Non-current assets			
(a) Property, Plant and Equipment	5	2,72,000	2,24,000
(b) Non-current Investment			4,00,000
(2) Current assets			
(a) Inventories		5,97,000	7,42,000
(b) Trade Receivables		5,94,000	8,91,000
(c) Cash & Cash Equivalents		51,000	3,000
(d) Other current assets	6	72,000	48,000
Total		15,86,000	23,08,000

Notes to Accounts

		20X0 (₹)	20X1 (₹)
1. Share capital			
	5,000 equity shares of ₹10 each, fully paid up	5,00,000	5,00,000
2. Reserves and Surplus			
	General Reserves	2,86,000	7,14,000
3. Short term borrowings			
	Bank overdraft	--	1,70,000
4. Short term provisions			
	Provision for taxation	3,10,000	4,30,000
5. Property, plant and equipment			
	Cost	3,20,000	3,20,000
	Less: Depreciation Total	(48,000)	(96,000)
6. Other current Assets		2,72,000	2,24,000
	Prepaid expenses	72,000	48,000

Also consider the following information:

- B Ltd. is a subsidiary of A Ltd. Both the companies follow calendar year as the accounting year.
- 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 ₹12,000 at the end of 20X0 and ₹ 34,000 at the end of 20X1.
- B Ltd. deducts 1% from Trade Receivables as a general provision against doubtful debts.
- Prepaid expenses in B Ltd. include advertising expenditure carried forward of ₹ 60,000 in 20X0 and ₹ 30,000 in 20X1, being part of initial advertising expenditure of ₹ 90,000 in 20X0 which is being written off over three years. Similar amount of advertising expenditure of A

Ltd. has been fully written off in 20X0.

Restate the balance sheet of B Ltd. as at 31st December, 20X1 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.

SOLUTION

As per para 20 and 21 of AS 21, Consolidated financial statements:

Consolidated financial statements should be prepared using uniform accounting policies for like transactions and other events in similar circumstances. If it is not practicable to use uniform accounting policies in preparing the consolidated financial statements, that fact should be disclosed together with the proportions of the items in the consolidated financial statements to which the different accounting policies have been applied.

If a member of the group uses accounting policies other than those adopted in the consolidated financial statements for like transactions and events in similar circumstances, appropriate adjustments are made to its financial statements when they are used in preparing the consolidated financial statements.

Accordingly in the given case, restatement would be required to make the accounting policies of A Ltd and B Ltd uniform.

Adjusted reserves of B Ltd.:

	₹	₹
Reserves as given		7,14,000
Add: Provision for doubtful debts $\{[8,91,000 / 99 \times 100] - 8,91,000\}$		9,000
		7,23,000
Less: Reduction in value of Inventory	34,000	
Advertising expenditure to be written off	30,000	64,000
		6,59,000

Note: No adjustment would be required in respect of opening inventory of B Ltd as that will not have any impact on P&L.

Restated Balance Sheet of B Ltd. as at 31st December, 2016

Particulars	Note No.	(₹)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	5,00,000
(b) Reserves and Surplus	2	6,59,000
(2) Current Liabilities		
(a) Short term borrowings	3	1,70,000
(b) Trade Payables		4,94,000
(c) Short-term provision	4	4,30,000
Total		22,53,000
II. Assets		
(1) Non-current assets		
(a) Property, Plant and Equipment		
Tangible assets	5	2,24,000
(b) Non-current Investment		4,00,000
(2) Current assets		
(a) Inventories	6	7,08,000
(b) Trade Receivables	7	9,00,000
(c) Cash & Cash Equivalents		3,000
(d) Other current assets	8	18,000
Total		22,53,000

Notes to Accounts

			₹
1. Share Capital			
	5,000 equity shares of ₹ 10 each, Fully Paid		5,00,000
2. Reserves and Surplus			
	Reserves (refer to W.N.)		6,59,000
3. Short term borrowings			
	Bank overdraft		1,70,000
4. Short-term provision			
	Provision for taxation		4,30,000
5. Tangible Assets			
	Cost	3,20,000	
	Less: Depreciation to date	(96,000)	2,24,000
6. Inventory			
	Cost	7,42,000	
	Less: Adjustment because of change in method of valuation	(34,000)	7,08,000
7. Trade receivables			
	Cost	8,91,000	
	Add: Provision adjustment	9,000	9,00,000
8. Other current assets			
	Prepaid expenses (48,000 – 30,000)		18,000

QUESTION 45: (Q.CFS.SM.503(A))

Variety Ltd. holds 46% of the paid-up share capital of VR Ltd. The shares were acquired at a market price of ₹ 17 per share. The balance of shares of VR Ltd. are held by a foreign collaborating company. A memorandum of understanding has been entered into with the foreign company providing for the following:

- The shares held by the foreign company will be sold to Variety Ltd. The price per share will be calculated by capitalising the yield at 15%. Yield, for this purpose, would mean 40% of the average of pre-tax profits for the last 3 years, which were ₹ 30 lakhs, ₹ 40 lakhs and ₹ 65 lakhs.
- The actual cost of the shares to the foreign company was ₹ 5,40,000 only. The profit that would accrue to them would be taxable at an average rate of 30%. The tax payable will be deducted from the proceeds and Variety Ltd. will pay it to the Government.
- Out of the net consideration, 50% would be remitted to the foreign company immediately and the balance will be an unsecured loan repayable after two years.

The above agreement was approved by all concerned for being given effect to on 1.4.20X1. The total assets of VR Ltd. as on 31st March, 20X1 was ₹ 1,00,00,000. It was decided to write down Property, Plant and Equipment by ₹ 1,75,000. Current liabilities of VR Ltd. as on the same date were ₹ 20,00,000. The paid-up share capital of VR Ltd. was ₹ 20,00,000 divided into 2,00,000 equity shares of ₹ 10 each.

Find out goodwill/capital reserve to Variety Ltd. on acquiring wholly the shares of VR Ltd.

SOLUTION**1. Computation of Purchase Consideration**

(a)	Yield of VR Ltd. $\{(40/100 \times [(30+40+65)/3])\}$	₹ 18 lakhs
(b)	Price per share of VR Ltd.	
	Capitalized Yield: (18 lakhs/0.15)	₹ 120 lakhs

	No. of Shares	2 lakhs
	Therefore, Price per share	₹ 60
(C)	Purchase Consideration for 54% shares in VR Ltd. 2 lakh shares x 54% x ₹ 60 per shares	₹ 64.80 lakhs
(d)	Discharge of Purchase Consideration:	
	Tax at source (₹ 64.80 lakhs - ₹ 5.40 lakhs) x 30/100	₹ 17.82 lakhs
	50% of Purchase Consideration (net of tax) in cash (₹ (64.80-17.82) x 50%)	₹ 23.49 lakhs
	Balance – Unsecured Loan	₹ 23.49 lakhs

2. Goodwill / Capital Reserve to Variety Ltd.

	₹ in lakhs	
Total Assets	100.00	
Less: Reduction in Value of Property, Plant and Equipment	(1.75)	
	98.25	
Less: Current Liabilities	(20.00)	
Net Assets of VR Ltd. on Date of Acquisition		78.25
Purchase Consideration: 54% purchased from Foreign Co.	64.80	
Investment: 46% existing stake	15.64	(80.44)
Goodwill on Date of Acquisition		2.19

8. ACCOUNTING FOR BRANCHES

INCLUDING FOREIGN BRANCHES

QUESTION 46: (Q.BRN.SM.101(A))

Beta, having head office at Mumbai has a branch at Nagpur. The head office does wholesale trade only at cost plus 80%. The goods are sent to branch at the wholesale price viz., cost plus 80%. The branch at Nagpur is wholly engaged in retail trade and the goods are sold at cost to H.O. plus 100%.

Following details are furnished for the year ended 31st March, 20X1:

	Head Office (Rs.)	Branch (Rs.)
Opening stock	2,25,000	
Purchases	25,50,000	
Goods sent to branch (Cost to H.O. plus 80%)	9,54,000	
Sales	27,81,000	9,50,000
Office expenses	90,000	8,500
Selling expenses	72,000	6,300
Staff salary	65,000	12,000

You are required to prepare Trading and Profit and Loss Account of the head office and branch for the year ended 31st March, 20X1.

SOLUTION

Working Note 1: -

Head Office

Opening Stock – 2,25,000 + Purchases – 25,50,000		
Total – 27,750,000		
Sale @180 COGS = $27,81,000 / 180 \times 100$ = 15,45,000	GSTB @180 COGS = $9,54,000 / 180 \times 100$ = 5,30,000	Closing Stock (b/f) 7,00,000

Working Note 2: -

Branch

Opening Stock – 0 + Purchases – 0 + Goods Received from HO – 5,30,000	
Total – 5,30,000	
COGS = $9,50,000 / 200 \times 100 = 4,75,000$	Closing Stock (b/f) 55,000

Branch Trading (Cost Basis)

Goods Received from HO	5,30,000	Sales	9,50,000
Gross Profit	4,75,000	Closing Stock	55,000
	10,05,000		10,05,000

QUESTION 47: (Q.BRN.RMP.202(A) Sep'24 Exam)

Following is the information of Kullu Branch of M/s Best Enterprises of Shimla for the year ending 31st March 2023:

- (1) Goods are invoiced to the branch at cost plus 20%
- (2) Branch sold goods at invoice price plus 25%.
- (3) Other Information is as follows:
 - (i) Stock (at cost price) as on 1st April, 2022 is Rs. 2,25,000
 - (ii) Goods sent by Head office to branch during the year (at cost price) are Rs. 14,85,000
 - (iii) Goods returned by Branch to Head office during the year (at Invoice price) are Rs. 75,000
 - (iv) Sales by the branch during the year Rs. 19,50,000
 - (v) Expenses incurred at Branch Rs. 56,000.

You are required to ascertain the following:

- (a) Profit earned by the Branch by Preparing Trading and profit and loss account for the year ended 31st March 2023
- (b) Also find the stock reserve on Closing stock

ANSWER**(i) In the books of Kullu Branch Trading and Profit and Loss Account**

Particulars	Amount Rs.	Particulars	Amount Rs.
To Opening stock	2,70,000	By Sales	19,50,000
To Goods received by Head office	17,82,000	By Goods returned by Branch	75,000
To Expenses	56,000	By Closing stock (Refer W.N.)	4,17,000
To Net profit (Bal fig)	<u>3,34,000</u>		
	24,42,000		24,42,000

(i) Calculation of Closing Stock**i)**

Cost price	100
Invoice price	120 (100+20)
Sales price	150 (120+25% of 120)
Opening Stock	2,70,000
Goods received	17,82,000
Less: Goods Returned	<u>75,000</u>
	<u>19,77,000</u>
Less: Cost of Goods Sold (Invoice price)	15,60,000
Closing Stock	4,17,000

Stock reserve in respect of unrealised profit = $4,17,000 \times (20/120) = \text{Rs. } 69,500$

QUESTION 48: (Q.BRN.RMP.304(A) MTP May'18)

Ayan Ltd. Invoices goods to its branch at cost plus $33\frac{1}{3}\%$ From the following Particulars prepare Branch Stock Account, Branch Stock Adjustment Account and Branch Profit and Loss Account as they would appear in the books of head office.

	Rs
Stock at commencement at Branch at invoice Price	3,60,000
Stock at close at Branch at Invoice Price	2,88,000
Goods sent to Branch during the year at invoice price (including goods invoiced at Rs. 48,000 to Branch on 31.03.2018 but not received by Branch before close of the year).	24,00,000
Return of goods to head office (invoice Price)	1,20,000
Credit Sales at Branch	1,20,000
Invoice value of goods pilfered	24,000
Normal loss at Branch due to wastage and deterioration of stock (at invoice price)	36,000
Cash Sales at Branch	21,60,000

Ayan closes its books on 31st March, 2018.

SOLUTION

In the books of Head Office Branch Stock Account

Particulars	Rs	Particulars	Rs
To Balance b/d	3,60,000	By Bank A/c (cash Sales)	21,60,000
To Goods sent to Branch A/c	24,00,000	By Branch Debtors A/c (Credit Sales)	1,20,000
To Branch Adjustment A/c – balancing fig. (Surplus)***	36,000	By Goods sent to Branch A/c (Returns to H.O.)	1,20,000
		By Branch Adjustment A/c* (Rs. 24,000 x 25/100)	6,000
		By Branch P&L A/c * (Cost of Abnormal Loss)	18,000
		By Branch Adjustment A/c** (Invoice price of normal loss)	36,000
		By Balance c/d: In hand in transit	2,88,000 48,000
	27,96,000		27,96,000

- Alternatively, combined posting for the amount of Rs. 24,000 may be passed through Goods pilfered account.
- Alternatively, it may first be transferred to normal Loss account which may ultimately be closed by transfer to Branch Adjustment account. The final amount of net profit will however remain same.
- It has been considered that the surplus may be due to sale of goods by branch at price higher than invoice price.

Branch Stock Adjustment Account

Particulars	(Rs)	Particulars	(Rs)
To Branch Stock A/c (Loading on Abnormal Loss)	6,000	By Stock Reserve A/c (Rs. 3,60,000 x 25/100)	90,000
To Branch Stock A/c (Normal Loss)	36,000	By Goods Sent to Branch A/c (Rs. 24,00,000 – Rs. 1,20,000) x 25/100	5,70,000
To Stock Reserve A/c (Rs. 3,36,000 x 25/100)	84,000	By Branch Stock A/c (Surplus)	36,000
To Gross Profit t/f to P & L A/c	5,70,000		
	6,96,000		6,96,000

Branch Profit and Loss Account

Particulars	Rs	Particulars	Rs
To Branch Stock A/c (Cost of Abnormal Loss)	18,000	By Branch Adjustment A/c (Gross Profit)	5,70,000
To Net Profit t/f to General P & LA/c	5,52,000		
	5,70,000		5,70,000

QUESTION 49: (Q.BRN.SM.403(A) Similar in RTP Nov'23)

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 with-holding 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 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.

SOLUTION

In the Head Office Books
Branch Account
for the year ended 31st March, 20X2

	Rs.'000		Rs.'000
To Balance b/d		By Balance b/d	
Cash in hand	10	Stock reserve Rs. $1,080 \times 1/6$	180
Trade debtors	384	By Goods sent to branch A/c (Returns to H.O.)	72
Stock	1,080	By Goods sent to branch A/c (Loading on net goods sent to branch - $13,128 \times 1/6$)	2,188
Furniture and fittings	500		
To Goods sent to branch A/c	13,200	Bank A/c (Remittance from branch to H.O.) (W.N.5)	11,700

To Bank A/c (Payment for furniture)	100	By Balance c/d	
To balance c/d stock reserve 1,470 x 1/6	245	Cash in hand	10
To Outstanding expenses	6	Trade debtors (W.N.3)	485
To Net profit transferred to General P/L account	1,096	Stock (W.N.1)	1,470
		Furniture & fittings (W.N.4)	516
	16,621		16,621

Working Notes:		
1. Invoice price and cost		
Let cost be		100
So, invoice price		120
Loading		20
Loading: Invoice price	$= 20 : 120 = 1 : 6$	

2. Invoice price of closing stock in branch

Branch Stock Account

	Rs. '000		Rs. '000
To Balance b/d	1,080	By Goods sent to branch	72
To Goods sent to branch	13,200	By Branch Cash	9,700
To Branch debtors	102	By Branch debtors	3,140
		By Balance c/d	1,470
	14,382		14,382

3. Closing balance of branch debtors

Branch Debtors Account

	Rs. '000		Rs. '000
To Balance b/d	384	By Branch cash	2,842
To Branch stock	3,140	By Branch expenses discount	58
		By branch stock (Returns)	102
		By Branch expenses (Bad debts)	37
		By Balance b/d	485
	3,524		3,524

4. Closing balance of furniture and fittings

Branch Furniture and Fittings Account

	Rs. '000		Rs. '000
To Balance b/d	500	By depreciation [(500x16%) (100x16%x3/12)]	84
To Bank	100	By Balance c/d	516
	600		600

Note: Since the new furniture was purchased on 1st Jan 20X2 depreciation will be for 3 months.

5. Remittance by branch to head office

Branch Cash Account

	Rs. '000		Rs. '000
To Balance b/d	10	By Branch expenses	842
To Branch stock	9,700	By Remittances to H.O. (b.f)	11,700
To Branch debtors	<u>2,842</u>	By Balance b/d	<u>10</u>
	12,552		12,552

QUESTION 50: (Q.BRN.RMP.406(A) RTP May'18, May'21)

Alpha Ltd. has a retail shop under the supervision of a manager. The ratio of gross profit at selling price is constant at 25 per cent throughout the year to 31st March, 2017.

Branch manager is entitled to a commission of 10 percent of the profit earned by his branch, calculated before charging his commission but subject to a deduction from such commission equal in 25 percent of any ascertained deficiency of branch stock. All goods were supplied to the branch in head office.

The following details for the year ended 31st March, 2017 are given as follows:

	Rs		Rs
Opening Stock (at cost)	74,736	Chargeable expenses	49,120
Goods sent to branch (at cost)	2,89,680	Closing Stock (Selling Price)	1,23,328
Sales	3,61,280		
Manager's commission paid on account	2,400		

From the above details, you are required to calculate the commission due to manager for the year ended 31st March, 2017.

SOLUTION**Step 1: Calculation of Deficiency****Branch stock account (at invoice price)**

Particulars	Rs	Particulars	Rs
To Opening Stock (Rs. 74,736 + 1/3 of Rs. 74,736)	99,648	By Sales	3,61,280
To Goods sent to Branch A/c (Rs. 2,89,680 + 1/3 of Rs. 2,89,680)	3,86,240	By Closing Stock	1,23,328
		By Deficiency at sale price [Balancing figure]	1,280
	4,85,888		4,85,888

Step 2: Calculation of Net Profit before Commission**Branch account**

Particulars	Rs	Particulars	Rs
To Opening [Rs. 74,736 + 1/3 of Rs. 74,736]	99,648	By Sales	3,61,280
To Gross sent to Branch A/c (Rs. 2,89,680 + 1/3 of Rs. 2,89,680)	3,86,240	By Closing Stock	1,23,328
To Expenses	49,120	By Stock Reserve A/c	24,912
To Stock Reserve A/c (Rs. 1,23,328 x 25/100]	30,832	By goods sent to Branch A/c	96,560

To Net Profit – subject to manager's commission	40,240		
	6,06,080		6,06,080

Step 3: Calculation of Commission still due to manager

		Rs
A	Calculation at 10% profit before charging his commission [Rs. 40,240 x 10/100]	4,024
B	Less: 25% of cost of deficiency in stock (25% of (75% of Rs. 1,280))	(240)
C	Commission for the year [A-B]	3,784
D	Less: Paid on account	(2,400)
E	Balance due (C-D)	1,384

QUESTION 51: (Q.BRN.RMP.502(A) RTP Nov'18)

Pass necessary Journal entries in the books of an independent Branch of M/s TPL Sons, wherever required, to rectify or adjust the following transactions:

- Branch paid Rs. 5,000 as salary to a Head Office Manager, but the amount paid has been debited by the Branch to Salaries Account.
- A remittance of Rs. 1,50,000 sent by the Branch has not received by Head Office on the date of reconciliation of Accounts.
- Branch assets accounts retained at head office; depreciation charged for the year Rs. 15,000 not recorded by Branch.
- Head Office expenses Rs. 75,000 allocated to the Branch, but not yet been recorded by the Branch.
- Head Office collected Rs. 60,000 directly from a Branch Customer. The intimation of the fact has not been received by the Branch.
- Goods dispatched by the Head office amounting to Rs. 50,000, but not received by the Branch till date of reconciliation.
- Branch incurred advertisement expenses of Rs. 10,000 on behalf of other Branches, but not recorded in the books of Branch.

Head office made payment of Rs. 16,000 for purchase of goods by branch, but not recorded in branch books.

SOLUTION

Books of Branch
Journal Entries

			Amounts Rs	
			Dr.	Cr.
(i)	Head Office Account To Salaries Account (Being rectification of salary paid on behalf of Head Office)	Dr.	5,000	5,000
(ii)	No entry in Branch Books is required.			
(iii)	Depreciation A/c To Head Office Account (Being depreciation of assets accounted for)	Dr.	15,000	15,000
(iv)	Expenses Account To Head Office Account (Being allocated expenses of Head Office recorded)	Dr.	75,000	75,000
(v)	Head Office Account	Dr.	60,000	

	To Debtors Account (Being adjustment entry for collection from Branch Debtors directly by Head Office)			60,000
(vi)	Goods in-transit Account To Head Office Account (Being goods sent by Head Office still in-transit)	Dr.	50,000	50,000
(vii)	Head Office Account To expenses Account / To Cash (Being expenditure incurred, wrongly recorded in books)	Dr.	10,000	10,000
(vii)	Purchases account A/c / Creditors To Head Office Account (Being purchases booked)	Dr.	16,000	16,000

QUESTION 52: (Q.BRN.SM.504(A))

Ring Bell Ltd. Delhi has a branch at Bombay where a separate set of books is used. The following is the Trail balance extracted on 31st Dec., 2010:

Particulars	HO		Branch	
	Dr.	Cr.	Dr.	Cr.
Equity Share capital	-	8,00,000	-	-
Profit & Loss a/c (01/01/2010)	-	25,310	-	-
Profit for 2010	-	82,200	-	31,700
Interim dividend paid	30,000	-	-	-
General Reserve	-	1,00,000	-	-
Fixed Assets	5,30,000	-	95,000	-
Stock	2,22,470	-	50,460	-
Debtors and Creditors	50,500	21,900	19,100	10,400
Cash Balance	62,730	-	6,550	-
HO a/c in branch books	-	-	-	1,29,010
Branch a/c in HO books	1,33,710	-	-	-

The difference between the balance of HO a/c and Branch a/c in both set of books is accounted for as follows:

- (1) Cash remitted by the branch on 31st Dec 2010 but received by the HO on 1st Jan. 2011- 3,000/-
- (2) Stock Stolen in transit from HO and charged to branch by the HO, but not credited to HO a/c in the branch books as the branch manager declined to admit any liability (not covered by insurance)- 1,700/-.

Give the Branch a/c in the HO books after incorporating the branch Trail balance through journal entries. Also prepare company's Balance Sheet as on 31st Dec., 2010.

(Answer: 10,39,810/-)

SOLUTION

The Branch Current Account in the Head Office Books and Head Office Current Account in the Branch Books do not show the same balances. Therefore, in order to reconcile them, the following journal entries will be passed in the Head Office books:

Journal Entries

		Dr.	Cr.
20X1		Rs.	Rs.
Dec., 31	Cash in Transit A/c To Branch Current A/c (Cash sent by the Branch on 31 st Dec., 20X1 but	Dr. 3,000	3,000

	received at H.O. on 1st Jan.,20X2)		
	Loss by theft A/c To Branch Current A/c (Stock lost in transit from H.O. to Branch)	Dr. 1,700	1,700

In order to incorporate, in the H.O. books, the given Branch trial balance which has been drawn up after preparing the Branch Profit & Loss Account, the following journal entries will be necessary:

Journal Entries

20X1			Rs.	Rs.
Dec. 31	Branch Current Account To Profit & Loss Account (Branch Profit for the year)	Dr.	31,700	31,700
	Branch Fixed Assets Branch Stock Branch Debtors Branch Cash To Branch Current Account (Branch assets brought into H.O. Books)	Dr. Dr. Dr. Dr.	95,000 50,460 19,100 6,550	1,71,110
	Branch Current A/c To Branch Creditors (Branch creditors brought into H.O. Books)	Dr.	10,400	10,400

Branch Current Account

	Rs.		Rs.
To Balance b/d	1,33,710	By Cash in transit	3,000
To Profit & Loss A/c	31,700	By Loss of theft	1,700
To Branch Creditors	10,400	By Sundry Branch Assets	1,71,110
	1,75,810		1,75,810

Profit and Loss Account for 20X1

	Rs.		Rs.
To Loss by Theft	1,700	By Balance b/d	25,310
To Balance c/d	1,07,510	By Year's Profit: H.O.	52,200
		Branch	31,700
	1,09,210		1,09,210

QUESTION 53: (Q.BRN.SM.505(A))

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 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.

	H.O.		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.

SOLUTION

In the books of KP

Trading and Profit & Loss Account for the year ended 31st Dec., 20X1

	H.O.	Branch	Total		H.O.	Branch	Total
	Rs.	Rs.	Rs.		Rs.	Rs.	Rs.
To Material consumed (W.N.1)	34,500	-	34,500	By Sales	2,00,000	65,200	2,65,200
To Wages	1,08,500	-	1,08,500	By Goods Sent to Branch	46,000	-	-
To Factory Overheads	39,000	-	39,000				
To Opening stock of finished goods	13,000	9,200	22,200	By Closing stock including transit (W.N.2)	15,000	9,560	24,560

CA Intermediate
Advanced Accounts

To Goods from H.O.		46,000					
To Gross Profit c/d (W.N.3)	66,000	19,560	85,560				
	2,61,000	74,760	2,89,760		2,61,000	74,760	2,89,760
To Admn. Salaries	13,900	4,000	17,900	By Gross Profit b/d	66,000	19,560	85,560
To Salesmen Salaries	22,500	6,200	28,700				
To Other Admn. & Selling Overheads	12,500	2,300	14,800				
To Stock Reserve (W.N.4)	47	-	47				
To Bonus to Staff	-	156	156				
To Net Profit	17,053	6,904	23,957				
	66,000	19,560	85,560		66,000	19,560	85,560

Balance Sheet as on 31st Dec., 20X1

	H.O.	Branch	Total		H.O.	Branch	Total
	Rs.	Rs.	Rs.		Rs.	Rs.	Rs.
Capital	50,000	-	50,000	Fixed Assets	-	-	-
Profit: H.O. 17,053 Branch 6,904	17053		23,957	Current Assets:			
				Raw material	2,300		2,300
Trade Creditors	13,000		13,000	Finished Goods (Less Stock Res.)	15,000	9,560	23,313*
Bonus Payable		156	156	Debtors	37,000	-	37,000
H.O. Account*		3500		Cash (including transit item)	23,500	1,000	24,500
Stock Reserve (W.N.4)	1,247			Branch A/c	3500		
	88,204	10,560	87,113		88,204	10,560	87,113

*9,560 × 100/115 i.e., (8,313 + 15,000) = Rs.23,313

** (5,000 + 6,904) – 1500 = Rs. 10,404.

Working Notes:
(1) Material Consumed

Opening raw material + Raw Material Purchased – Closing raw material
= 1,800 + 35,000 - 2,300 = 34,500

(2) Closing stock at head office

(a) Calculation of total factor cost = Material consumed + Wages + Factory overhead
= 34,500 + 1,08,500 + 39,000 = 1,95,000

(b) Cost (factory cost) of goods sold = Sales – Gross profit
= 2,00,000 – 2,00,000 × 70% = 1,40,000

(c) Stock transferred to branch = 46,000 × 100/115 = 40,000

(d) Closing stock = 1,95,000 – 1,40,000 – 40,000 = 15,000

(3) Gross profit of Branch = Sales × Gross profit ratio

$$= 65,200 \times 30\% = 19,560$$

$$(4) \text{ Closing stock reserve} = 9,560 \times 15/115 = 1,246$$

$$\text{Charge to profit and loss} = 1,247 - 1,200 = 47$$

QUESTION 54: (Q.BRN.SM.603(A))

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:

1 th January, 20X1	\$ 1.00	=	Rs. 46
31 st 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.

SOLUTION

(i)

In the Books of Head Office
Branch Trading and Profit & Loss A/c (in Dollars)
for the year ended 31st December, 20X1

Opening stock	11200	By sales	84000
Goods from H.O.	64000	By closing stock	8000
Gross profit c/d	16800		
	92000		92000
Expenses	5,000	By Gross Profit b/d	16,800

To deprecation (24000X 10%)	2400		
To manager commission	470		
To net profit C/d	8930		
	16800		16800

(i) (a)

Converted Branch Trial Balance (into Indian Currency)

Particulars	Rate per \$	Dr. (Rs.)	Cr. (Rs.)
Machinery	40	9,60,000	—
Stock January 1, 20X1	46	5,15,200	—
Goods from head office	Actual	29,26,000	—
Sales	47	—	39,48,000
Expenses	47	2,35,000	—
Debtors & creditors	48	2,30,400	1,63,200
Cash at bank	48	57,600	—
Head office A/c	Actual	—	8,60,000
Difference in exchange rate (b.f.)		47,000	—
		49,71,200	49,71,200
Closing stock \$ 8,000 (W.N. 2)	48		Rs. 3,84,000

(a) Branch Trading and Profit & Loss A/c for the year ended 31st December, 20X1

	Rs.		Rs.
To Opening stock	5,15,200	By Sales	39,48,000
To Goods from head office	29,26,000	By Closing stock (W.N.2)	3,84,000
To Gross profit c/d	8,90,800		
	43,32,000		43,32,000
To Expenses	2,35,000	By Gross profit b/d	8,90,800
To Depreciation @ 10% on Rs. 9,60,000	96,000		
To Exchange difference	47,000		
To Manager's commission (W.N.1)	22,560		
To Net Profit c/d	4,90,240		
	8,90,800		8,90,800

(b)

Branch Account

To Balance b/d	8,60,000	By Machinery	9,60,000	
To Net profit	4,90,240	Less:		
To Creditors	1,63,200	By Depreciation	(96,000)	8,64,000
To Outstanding		By Closing stock		3,84,000
To commission	22,560	By Debtors		2,30,400
		By Cash at bank		57,600
	15,36,000			15,36,000

Working Notes:**1. Calculation of manager's commission @ 5% on profit**

i.e.,	5% of \$[16,800 - (5,000 + 2,400)]
Or	5% × \$9,400 = \$ 470
Manager's commission in Rupees = \$ 470 x Rs. 48 = Rs. 22,560	

2. Calculation of closing stock

	\$
Opening stock	11,200
Add: Goods from head office	<u>64,000</u>
	75,200
Less: Cost of goods sold (at invoice price) 84000X100/125	<u>(67,200)</u>
Closing stock	<u>8,000</u>
Closing stock in Rupees = \$8,000 x Rs. 48 = Rs.3,84,000.	

Note: Manager is entitled to commission on profits earned at the end of the year.

QUESTION 55: (Q.BRN.RMP.605(A) Exam May'24)

Smart Limited is an Indian Company and has its Branch at New York. The following balances in respect of Smart Limited's USA Branch office are provided:

(i) Debit Balances (in USD)

Expenditure (excluding Depreciation)	1,03,095
Cash & bank balances	2,175
Debtors	7,365
Fixed Assets (Gross) (Rate of Depreciation on Fixed Assets : 20%)	34,200
Inventory – Stock 'P'	5,520
Inventory – Stock 'Q'	1,035

(ii) Credit Balances (in USD)

Incomes	1,32,000
Creditors	15,570
HO Control a/c	5,820

The following additional information is provided:

- The average exchange rate during the above financial year was 1 USD = Rs. 56.
- The fixed assets were purchased when the exchange rate was 1 USD = Rs. 55.
- The closing exchange rate on reporting date is 1 USD = Rs. 58.
- Stock item 'P' is valued at cost of USD 5,520 purchased when the exchange rate was Rs. 56.50. the present net realizable value of this item is Rs. 2,85,000.
- Stock item 'Q' is carried at net realizable value of USD 1,035. But its cost in USD is 1,065. It was purchased when exchange rate was 1 USD = Rs. 53.
- Branch Control Account as per HO books was Rs. 2,66,265.

You are required to show how it will be reflected in the books of Head office in the form of Trial Balance, if the USA Branch Office is classified as an integral Foreign Operation.

SOLUTION

Converted branch trail balance (in the books of head office)

Particular	Dr. \$	Cr. \$	Rate per \$	₹ Dr.	₹ Cr.
Expenditure	1,03,095		56	57,73,320	
Cash & bank balance	2,175		58	1,26,150	
Debtors	7,365		58	4,27,170	
Fixed assets	27,360		55	15,04,800	

Depreciation 20%	6,840		55	3,76,200	
Inventory P	5,520		Direct	2,85,000	
Inventory Q	1,065		53	56,445	
Income		1,32,000	56		73,92,000
Creditors		15,570	58		9,03,060
HO control A/c		5,820			2,66,265
Exchange difference				12,240	
				85,61,325	85,61,325

Working Note:

Inventory P	\$ 5,520	Inventory Q	\$ 1,065
Purchased Cost rate	56.50	NRV	\$ 1,035
NRV	₹ 2,85,000	Closing rate	58
Cost	₹ 3,11,880	Purchased Cost rate	53
Value at cost or NRV whichever is less	₹ 2,85,000	Value at cost or NRV whichever is less	\$ 1,035 @ ₹ 58 or \$1,065 @ ₹ 53 = 56,445 or 60,030

QUESTION 56: (Q.BRN.SM.301(B))

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:

- Outlet Stock Account.
- Outlet Profit & Loss Account.
- Stock Reserve Account.

SOLUTION**Outlet Stock Account**

	Rs.		Rs.
To Balance b/d	30,000	By Sales (Working Note 1)	3,60,000
To Goods sent to outlet	3,24,000	By Goods lost by fire (b.f.)	18,000
To Gross Profit c/d	60,000	By Balance c/d	36,000
	4,14,000		4,14,000

Outlet Profit & Loss Account

	Rs.		Rs.
--	------------	--	------------

To Expenses	20,000	By Gross Profit b/d	60,000
To Goods lost by fire (W.N. 2)	18,000		
To Profit transferred	22,000		
	60,000		60,000

Stock Reserve Account

	Rs.		Rs.
To HO P & L A/c –Transfer	6,000	By Balance b/d	6,000
To Balance c/d (Stock Res. required)	7,200	By HO P&L A/c (W.N. 3)	7,200
	13,200		13,200

Working Notes:**WN 1**

Whole sale Price	100+25	= 125
Retail Price	125 + 20%	= 150
Gross Profit at the outlet		
Wholesale Price – Retail Price	(150 – 125)	25

Retail sales value = $60,000 \times 150/125 = 3,60,000$

WN 2: Goods lost by fire

Opening Stock + Goods Sent + Gross Profit – Sales – Closing Stock

$30,000 + 3,24,000 + 60,000 - 3,60,000 - 36,000 = \text{Rs. } 18,000$

WN 3: Stock Reserve

Opening Stock = $30000 \times 25/125 = 6000$

Closing stock = $36000 \times 25/125 = 7200$

9. INTRODUCTION AND APPLICABILITY OF AS

QUESTION 57: (RTP MAY'26)

Virat Traders, an unlisted partnership firm, had a turnover of ₹ 249.99 crore and borrowings of ₹ 25.01 crore during the financial year 2023-24. It is not a bank, financial institution, or insurance company, and also not a subsidiary of any other entity. The firm wishes to avail MSME exemptions for FY 2024—25. Is it eligible?

SOLUTION

Company qualifies as an MSME if following conditions are satisfied:

- (a) whose equity or debt securities are not listed or are not in the process of listing on any stock exchange, whether in India or outside India;
- (b) which is not a bank, financial institution or an insurance company;
- (c) whose turnover (excluding other income) does not exceed 250 crore rupees in the immediately preceding accounting year;
- (d) which does not have borrowings in excess of 50 crore rupees at any time during the immediately preceding accounting year; and
- (e) which is not a holding or subsidiary of an entity which is not a MSME entity.

Yes, Virat Traders qualifies as an MSME since it meets all five criteria.

Further, it has been assumed that Virat Traders is not newly qualifying as an MSME in FY 2024-25 because a non-company entity that newly qualifies as an MSME can avail exemptions only after it remains as MSME for two consecutive years.

Until then, full AS compliance is required.

10. AS 1 – DISCLOSURE OF ACCOUNTING POLICIES

QUESTION 58: (Q.AS1.SM.01: MTP Nov18)

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.

SOLUTION

As per AS 1 “Disclosure of Accounting Policies”, any change in an accounting policy which has a material effect should be disclosed in the financial statements. The amount by which any item in the financial statements is affected by such change should also be disclosed to the extent ascertainable. Where such amount is not ascertainable, wholly or in part, the fact should be indicated. Thus Prashant Ltd. should disclose the change in valuation method of inventory and its effect on financial statements. The company may disclose the change in accounting policy in the following manner:

The company values its inventory at lower of cost and net realisable value. Since net realisable value of all items of inventory in the current year was greater than respective costs, the company valued its inventory at cost. In the present year i.e., 2014-15, the company has changed to weighted average method, which better reflects the consumption pattern of inventory, for ascertaining inventory costs from the earlier practice of using FIFO for the purpose. The change in policy has reduced current profit and value of inventory by Rs 16,000.

QUESTION 59: (Q.AS1.SM.02)

Jagannath Ltd. had made a rights issue of shares in 2012. In the offer document to its members, it had projected a surplus of ₹40 crores during the accounting year to end on 31st March, 2014. 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 ₹10 crores. The board in consultation with the managing director, decided on the following:

- (i) Value year-end inventory at works cost (₹ 50 crores) instead of the hitherto method of valuation of inventory at prime cost (₹ 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 ₹ 27 crores is lower than the amount of ₹ 45 crores which would have been provided had the old method been followed, by ₹ 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

₹ 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 ₹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 2013-2014.

SOLUTION

As per AS 1, any change in the accounting policies which has a material effect in the current period or which is reasonably expected to have a material effect in later periods should be disclosed. In the case of a change in accounting policies which has a material effect in the current period, the amount by which any item in the financial statements is affected by such change should also be disclosed to the extent ascertainable. Where such amount is not ascertainable, wholly or in part, the fact should be indicated. Accordingly, the notes on accounts should properly disclose the change and its effect.

Notes on Accounts:

- (i) During the year inventory has been valued at factory cost, against the practice of valuing it at prime cost as was the practice till last year. This has been done to take cognizance of the more capital-intensive method of production on account of heavy capital expenditure during the year. As a result of this change, the year-end inventory has been valued at ₹50 crores and the profit for the year is increased by ₹20 crores.
- (ii) In view of the heavy capital-intensive method of production introduced during the year, the company has decided to change the method of providing depreciation from reducing balance method to straight line method. As a result of this change, depreciation has been provided at ₹27 crores which is lower than the charge which would have been made had the old method and the old rates been applied, by ₹18 crores. To that extent, the profit for the year is increased.
- (iii) So far, the company has been providing 2% of sales for meeting “after sales expenses during the warranty period. With the improved method of production, the probability of defects occurring in the products has reduced considerably. Hence, the company has decided not to make provision for such expenses but to account for the same as and when expenses are incurred. Due to this change, the profit for the year is increased by ₹12 crores than would have been the case if the old policy were to continue.

The company has decided to provide ₹10 crores for the permanent fall in the value of investments which has taken place over the period of past five years. The provision so made has reduced the profit disclosed in the accounts by ₹10 crores.

QUESTION 60: (Q.AS1.RMP.05 EXAM Nov18) (MTP May21 & May22)

HIL Ltd. was making provision for non-moving stocks based on no issues having occurred for the last 12 months upto 31.03.2019. The company now wants to change it and make provision based on technical evaluation during the year ending 31.03.2020. Total value of stock on 31.3.20 is Rs. 120 lakhs. Provision required based on technical evaluation amounts Rs. 3.00 lakhs. However, provision required based on 12 months (no issues) is Rs. 4.00 lakhs. You are required to discuss the following points in the light of Accounting Standard (AS)-1:

- i. Does this amount to change in accounting policy?

- ii. Can the company change the method of accounting?
- iii. Explain how it will be disclosed in the annual accounts of HIL Ltd. for the year 2019 -20.

SOLUTION

The decision of making provision for non-moving inventories on the basis of technical evaluation does not amount to change in accounting policy. Accounting policy of a company may require that provision for non-moving inventories should be made but the basis for making provision will not constitute accounting policy. The method of estimating the amount of provision may be changed in case a more prudent estimate can be made.

In the given case, considering the total value of inventory, the change in the amount of required provision of non-moving inventory from Rs. 4 lakhs to Rs. 3 lakhs is also not material. The disclosure can be made for such change in the following lines by way of notes to the accounts in the annual accounts of HIL Ltd. for the year 2019-20 in the following manner:

“The company has provided for non-moving inventories on the basis of technical evaluation unlike preceding years. Had the same method been followed as in the previous year, the profit for the year and the value of net assets at the end of the year would have been lower by Rs. 1 lakh.”

11. AS 2 – VALUATION OF INVENTORIES

QUESTION 61: (Q.AS2.SM.04 MTP Nov19)

Mr. Mehul gives the following information relating to items forming part of inventory as on 31-3-2015. 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 31-3-2015 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 31-3-2015. Also calculate the value of total inventory as on 31-3-2015.

SOLUTION

As per AS 2 “Valuation of Inventories”, 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 sold at cost or above cost. However, when there has been a decline in the price of materials and it is estimated that the cost of the finished products will exceed net realizable value, the materials are written down to net realizable value. In such circumstances, the replacement cost of the materials may be the best available measure of their net realizable value. In the given case, selling price of product X is Rs. 300 and total cost per unit for production is Rs. 320.

Hence the valuation will be done as under:

- (i) 600 units of raw material will be written down to replacement cost as market value of finished product is less than its cost, hence valued at Rs. 90 per unit.
- (ii) 500 units of partly finished goods will be valued at 240 per unit i.e., lower of cost Rs. 320 (Rs. 260 + additional cost Rs. 60) or Net estimated selling price Rs. 240 (Estimated selling price Rs. 300 per unit less additional cost of Rs. 60).
- (iii) 1,500 units of finished product X will be valued at NRV of Rs. 300 per unit since it is lower than cost Rs. 320 of product X.

Valuation of Total Inventory as on 31.03.2015:

	Units	Cost (Rs.)	NRV/Replacement cost	Value = units x cost or NRV whichever is less (Rs.)
Raw material A	600	120	90	54,000
Partly finished goods	500	260	240	1,20,000
Finished goods X	1,500	320	300	4,50,000
Value of Inventory				6,24,000

QUESTION 62: (Q.AS2.SM.05 also RTP Nov.22)

The closing inventory at cost of a company amounted to Rs. 2,84,700. The following items were included at cost in the total:

- (a) 400 coats, which had cost Rs. 80 each and normally sold for Rs. 150 each. Owing to a defect in manufacture, they were all sold after the balance sheet date at 50% of their normal price. Selling expenses amounted to 5% of the proceeds.

- (b) 800 skirts, which had cost Rs. 20 each. These too were found to be defective. Remedial work in April cost Rs. 5 per skirt, and selling expenses for the batch totaled Rs. 800. They were sold for Rs. 28 each.

What should the inventory value be according to AS 2 after considering the above items?

SOLUTION

Valuation of Closing Stock

Particulars	Rs.	Rs.
Closing Stock at cost		2,84,700
Less: adjustment required for 400 defected coats		3,500
Cost of 400 coats (400 x 80)	32,000	
Net Realisable Value [400 x (75 – 5% of Rs. 75)]	28,500	
(400 coats should be measured at NRV which is lower i.e. 28,500 therefore adjustment of 3500 is required)		
Value of Closing Stock		2,81,200

Note: There is no adjustment for skirts because for skirts were sold at above cost.

QUESTION 63: (Q.AS2.OM.06)

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 31-3-20X1
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 31-03-20X1.

SOLUTION

As per Ind 2 'Inventories', most by-products as well as scrap or waste materials, by their nature, are immaterial. They are often measured at net realizable value and this value is deducted from the cost of the main product.

1) Calculation of NRV of By-product BP

Selling price of by-product	2,000 units x 20 per unit	40,000
Less: Separate processing charges of by-product BP		(8,000)
Packing charges		(2,000)
Net realizable value of by-product BP		30,000

2) Calculation of cost of conversion for allocation between joint products MP1 and MP2

Raw material		1,50,000
Wages		90,000
Fixed overhead		65,000
Variable overhead		50,000
Less: NRV of by-product BP (See Calculation 1)	30,000 5,000	(35,000)
Sale value of scrap		
Joint cost to be allocated between MP1 and MP2		3,20,000

3) Determination of “basis for allocation” and allocation of joint cost to MP1 and MP2

	MP I	MP 2
Output in units (a)	5,000	4,000
Sales price per unit (b)	60	50
Sales value (a x b)	3,00,000	2,00,000
Ratio of allocation	3	2
Joint cost of Rs. 3,20,000 allocated in the ratio of 3:2 (c)	1,92,000	1,28,000
Cost per unit [C/A]	38.4	32

4) Determination of Value of Closing stock of MP 1 & MP 2

Particulars	MP 1	MP 2
Closing stock in units	250 units	100 units
Cost per unit	38.4	32
Value of closing stock	9,600	3,200

QUESTION 64: (Q.AS2.RMP.10 RTP May20)

Particulars		Kg.	Rs
Opening Inventory:	Finished Goods	1,000	25,000
	Raw Materials	1,100	11,000
Purchases of Raw Material		10,000	1,00,000
Labour			76,500
Overheads (Fixed)			75,000
Sales		10,000	2,80,000
Closing Inventory:	Raw Materials	900	
	Finished Goods	1200	

The expected production for the year was 15,000 kg of the finished product. Due to fall in market demand the sales price for the finished goods was Rs. 20 per kg and the replacement cost for the raw material was Rs. 9.50 per kg on the closing day. You are required to calculate the closing inventory as on that date.

SOLUTION**Calculation of cost for closing inventory**

Particulars	Rs
Cost of Purchase (10,200 x 10)	1,02,000
Direct Labour	76,500
Fixed Overhead 75,000X10,200/15,000	51,000
Cost of Production	2,29,500

Cost of closing inventory per unit (2,29,500/10,200)	Rs 22.50
Net Realisable Value per unit	Rs 20.00

Since net realisable value is less than cost, closing inventory will be valued at Rs. 20.

As NRV of the finished goods is less than its cost, relevant raw materials will be valued at replacement cost i.e. Rs. 9.50.

Therefore, value of closing inventory: Finished Goods (1,200 x 20) Rs. 24,000

Raw Materials (900 x 9.50) =Rs. 8,550

Total =Rs. 32,550

QUESTION 65: (Q.AS2.RMP.12 MTP Nov21)

From the following information provided by XYZ Limited you are required to compute the closing inventory:

Raw Material P

Closing balance	600 units
	Rs. per unit
Cost price including GST	250
Input tax credit available	20
Freight inward	30
Handling charges	15
Replacement cost	180

Finished goods Q

Closing balance	1,500 units
	Rs. per unit
Material consumed	250
Direct labour	70
Direct overhead	30

Total fixed overhead for the year was Rs. 3,00,000 on a normal capacity of 30,000 units while actual production has been of 25,000 units.

Calculate the value of closing stock, when

- (i) Net realizable value of the finished good Q is Rs. 450 per unit.
(ii) Net Realizable value of the Finished Good Q is Rs. 340 per unit.

SOLUTION

- (i) When Net Realizable Value of the Finished Good Q is Rs. 450 per unit Value of Closing Stock:

	Valuation Base	Qty.	Rate (Rs.)	Amount (Rs.)
Raw Material P	Cost	600	275	1,65,000
Finished Good Q	Cost	1,500	360	5,40,000
Total value of closing stock				7,05,000

- (ii) When Net Realizable Value of the Finished Good Q is Rs. 340 per unit

Since NRV of finished goods Q is less than its cost i.e. Rs. 360 (Refer W.N.), raw material P is to be valued at replacement cost and finished goods is to be valued at NRV.

Value of Closing Stock:

	Valuation Base	Qty.	Rate (Rs.)	Amount (Rs.)
Raw material P	Replacement cost	600	180	1,08,000
Finished good Q	Net Realisable Value	1,500	340	5,10,000
Total value of closing stock				6,18,000

Working Note:

Statement showing calculation of cost of raw material P and finished good Q

Raw Material P	Rs.
Cost Price (250-20)	230
Add: Freight Inward	30
Handling charges	15
Cost	275
Finished Goods Q	Rs.
Materials consumed	250
Direct Labour	70
Variable overheads	30
Fixed overheads (Rs. 3,00,000 / 30,000 units)	10
	360

12. AS 10 – PROPERTY, PLANT & EQUIPMENT

QUESTIN 66: (Q.AS10.RMP.03 RTP Nov19 & May'25)

Shrishti Ltd. contracted with a supplier to purchase machinery which is to be installed in its Department A in three months' time. Special foundations were required for the machinery which were to be prepared within this supply lead time. The cost of the site preparation and laying foundations were Rs. 1,41,870. These activities were supervised by a technician during the entire period, who is employed for this purpose of Rs. 45,000 per month. The technician's services were given by Department B to Department A, which billed the services at Rs. 49,500 per month after adding 10% profit margin.

The machine was purchased at Rs. 1,58,34,000 inclusive of IGST @ 12% for which input credit is available to Shrishti Ltd. Rs. 55,770 transportation charges were incurred to bring the machine to the factory site. An Architect was appointed at a fee of Rs. 30,000 to supervise machinery installation at the factory site.

Ascertain the amount at which the Machinery should be capitalized under AS 10 considering that IGST credit is availed by the Shristhi Limited. Internally booked profits should be eliminated in arriving at the cost of machine.

SOLUTION

Calculation of Cost of Fixed Asset (i.e., Machinery)

Particulars		Rs.
Purchase Price		Given (Rs. 158,34,000 x 100/112)
Add:	Site Preparation Cost	Given
	Technician's Salary	Specific/Attributable overheads for 3 months (45,000 x3)
	Initial Delivery Cost	Transportation
	Professional Fees for Installation	Architect's Fees
Total Cost of Asset		1,45,00,140

QUESTION 67: (Q.AS.10.SM.04)

On 1st April 20X1, an item of property is offered for sale at Rs. 10 million, with payment terms being three equal installments of Rs.33,33,333 over a two years period (payments are made on 1st April 20X1, 31st March 20X2 and 31st March 20X3).

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 AS 10.

SOLUTION:

AS 10 requires that the cost of an item of PPE is the cash price equivalent at the recognition date. Hence, the purchaser that takes up the deferred payment terms will recognise the acquisition of the asset as follows

On 1st April, 20X1		(Rs)	(Rs)
Property, Plant and Equipment	Dr.	95,00,000	
To Cash			33,33,333

To Accounts Payable (Initial recognition of property)		61,66,667
<u>On 31st March 20X2</u>		
Interest Expense Dr.	3,30,533	
Accounts payable Dr.	30,02,800	
To Cash (Recognition of interest expense and payment of second installment)		33,33,333
<u>On 31st March 20X3</u>		
Interest Expense Dr.	1,69,467	
Accounts payable Dr.	31,63,867	
To Cash (Recognition of interest expense and payment of final installment)		33,33,334

QUESTION 68 (Q.AS.10.SM.05) (Exchange lacks commercial substance)

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?

SOLUTION

The entity recognises the assets received at the book value of car X. Therefore, it recognises cash of Rs 15,000 and car Y as PPE with a carrying value of Rs 12,85,000.

QUESTION 69 (Q.AS.10.SM.10)

Akshar Ltd. installed a new Plant (not a qualifying asset), at its production facility, and incurred the following costs:

- Cost of the Plant (as per supplier's invoice): ₹ 30,00,000
- Initial delivery and handling costs: ₹ 1,00,000
- Cost of site preparation: ₹ 2,00,000
- Consultant fee for advice on acquisition of Plant: ₹ 50,000
- Interest charges paid to supplier against deferred credit: ₹ 1,00,000
- Estimate of Dismantling and Site Restoration costs: ₹ 50,000 after 10 years (Present Value is ₹ 30,000)
- Operating losses before commercial production: ₹ 40,000

The company identified motors installed in the Plant as a separate component and a cost of ₹ 5,00,000 (Purchase Price) and other costs were allocated to them proportionately. The company estimates the useful life of the Plant and those of the Motors as 10 years and 6 years respectively and SLM method of Depreciation is used.

At the end of Year 4, the company replaces the Motors installed in the Plant at a cost of ₹ 6,00,000 and estimated the useful life of new motors to be 5 years. Also, the company revalued its entire class of Fixed Assets at the end of Year 4. The revalued amount of Plant as a whole is ₹ 25,00,000. At the end of Year 8, the company decides to retire the Plant from active use and also disposed the Plant as a whole for ₹ 6,00,000.

There is no change in the Dismantling and Site Restoration liability during the period of use. You are required to explain how the above transaction would be accounted in accordance with AS 10.

SOLUTION**1. Cost at Initial Recognition:**

Particulars	₹
Cost of the Plant (as per Invoice)	30,00,000
Initial Delivery and Handling Costs	1,00,000
Cost of Site Preparation	2,00,000
Consultants' Fees	50,000
Estimated Dismantling and Site Restoration Costs	30,000
Total Cost of Plant including Motors	33,80,000
Less: Cost of Motors identified as a separate component (1/6)*	5,63,333
Cost of the Plant (excluding Motors – balance 5/6)	28,16,667

* Purchase price of Motors = ₹ 5,00,000 out of ₹ 30,00,000 i.e., 1/6 of value of Plant

Note: Since the asset is not a qualifying asset, payment of interest to the supplier is not capitalized. Further, operating losses of ₹ 40,000 incurred before commercial production is not a directly attributable cost, and hence excluded from cost of asset. These costs are expensed to the P/L as and when they are incurred.

2. Recognition of Motors Replacement

Particulars	₹
Cost of Motors determined above	5,63,333
Less: Depreciation for 4 years (as per SLM)	3,75,555
5,63,333 ÷ 6 years x 4 years	
Carrying Amount of Motors at the end of Year 4	1,87,778

Accounting: The company should derecognize the existing Carrying Amount of Motors replaced of ₹ 1,87,778. Further, the acquisition cost of new motors of ₹ 6,00,000 would be capitalized as a separate component. This amount will be depreciated over the next 5 years at ₹ 6,00,000 ÷ 5 years = ₹ 1,20,000 p.a.

3. Revaluation

Particulars	₹
Cost of the Plant at initial recognition [from (1) above]	28,16,667
Less: SLM Depreciation for 4 years: ₹ 28,16,667 ÷ 10 years x 4 years	11,26,667
Carrying Amount of Plant at the end of Year 4	16,90,000
Revalued Amount of Plant (Excluding Motors, since the same is treated as a separate component: ₹ 25,00,000 – ₹ 6,00,000)	19,00,000
Therefore, Gain on Revaluation credited to Revaluation Reserve	2,10,000
Revised Depreciation Charge p.a.: 19,00,000 ÷ 6 years	3,16,667

4. Derecognition

Particulars	Motors	Plant (excluding Motors)
Cost / Revalued Amount at end of Year 4	6,00,000	19,00,000

Less: Depreciation for Years 5-8	$1,20,000 \times \frac{4}{4}$ = 4,80,000	$3,16,667 \times 4$ = 12,66,668
Carrying Amount before Disposal / De- recognition	1,20,000	6,33,332
Less: Disposal Proceeds ₹ 6,00,000 allocated in ratio of carrying amount	95,575	5,04,425
Loss to be written off to P/L	24,425	1,28,907

Notes:

- (a) The Revaluation Surplus of ₹ 2,10,000 would be transferred directly to Retained Earnings.
- (b) The allocation of disposal proceeds of ₹ 6,00,000 for the plant as whole is apportioned based on carrying amount of motors and plant (excluding motors)

Alternatively, it may be apportioned as 1/6 towards motors and 5/6 plant (excluding motors) based on the reasoning that the initially, motors amounted to 1/6 of the entire plant. This approach may not be preferable because there has been a revaluation of the plant (excluding motors) and a disposal and subsequent acquisition of the Motor, which is not in the initial proportion of 5/6 and 1/6 respectively.

QUESTION 70 (Q.AS.10.SM.11)

Bharat Infrastructure Ltd. acquired a heavy machinery at a cost of ₹ 1,000 lakhs, the breakdown of its components is not provided. The estimated useful life of the machinery is 10 years. At the end of Year 6, the turbine, which is a major component of the machinery, needed replacement, as further usage and maintenance was uneconomical. The remainder of the machine is in good condition and is expected to last for the remaining 4 years. The cost of the new turbine is ₹ 450 lakhs. Give the accounting treatment for the new turbine, assuming SLM Depreciation and a discount rate of 8%.

SOLUTION

As per AS 10, Property, Plant and Equipment, the derecognition of the carrying amount of components of an item of Property, Plant and Equipment occurs regardless of whether the cost of the previous part / inspection was identified in the transaction in which the item was acquired or constructed. If it is not practicable for an enterprise to determine the carrying amount of the replaced part/ inspection, it may use the cost of the replacement or the estimated cost of a future similar inspection as an indication of what the cost of the replaced part/ existing inspection component was when the item was acquired or constructed.

In the given case, the new turbine will produce economic benefits to Bharat Infrastructure Ltd. and the cost is measurable. Since the recognition criteria is fulfilled, the same should be recognised as a separate item of Property, Plant and Equipment. However, since the initial breakup of the components is not available, the cost of the replacement of ₹ 450 lakhs can be used as an indication based on the guidance given above, discounted at 8% for the 6-year period lapsed.

Thus, estimate of cost 6 years back = ₹ 450 lakhs $\div 1.08^6$ = ₹ 283.58 lakhs
Current carrying amount of turbine (to be de-recognised) = Estimated cost ₹ 283.58 lakhs (–) SLM depreciation at 10% (useful life 10 years) for 6 years ₹ 170.15 lakhs = ₹ 113.43 lakhs.

Hence revised carrying amount of the machinery will be as under:

Particulars	₹ in lakhs
Historical Cost [₹ 1,000 lakhs (-) SLM Depreciation at 10% (10 year life) for 6 years]	400.00
Add: Cost of new turbine	450.00
Less: Derecognition of current carrying amount of old turbine	(113.43)
New Carrying Amount of Machinery	736.57

QUESTION 71: (Q.AS.10.SM.13 EXAM May23)

In the books of Topmaker Limited, carrying amount of Plant and Machinery as on 1st April, 2022 is ₹ 56,30,000. On scrutiny, it was found that a purchase of Machinery worth ₹ 21,12,000 was included in the purchase of goods on 1st June, 2022. On 30th June, 2022 the company disposed a Machine having book value of ₹ 9,60,000 (as on 1st April, 2022) for ₹ 8,25,000 in part exchange of a new machine costing ₹ 15,65,000.

The company charges depreciation @ 10% p.a. on written down value method on Plant and Machinery.

You are required to compute:

- Depreciation to be charged to Profit & Loss Account;
- Book value of Plant & Machinery as on 31st March, 2023; and
- Profit/Loss on exchange of Plant & Machinery.

SOLUTION:**(i) Depreciation to be charged in the profit & Loss Account**

Particulars	Amount in ₹
Depreciation on old machinery [10% on ₹ 56,30,000 for 3 months (01.04.2022 to 30.06.2022)]	1,40,750
Add: Depreciation on Machinery acquired on 01.06.2022 (₹21,12,000 × 10% × 10/12)	1,76,000
Add: Depreciation on machinery after adjustment of exchange [10% of ₹ 56,30,000 – 9,60,000 + 15,65,000) for 9 months]	4,67,625
Total Depreciation to be charged in Profit & Loss A/c	7,84,375

(ii) Book Value of Plant & Machinery as on 31.3.2023

Particulars		Amount in ₹
Balance as books on 01.04.2022		56,30,000
Add: Included in purchases on 01.06.2022	21,12,000	
Add: Purchase on 30.06.2022	<u>15,65,000</u>	<u>36,77,000</u>
		93,07,000
Less: Book Value of Machine Sold on 30.06.2022		<u>(9,60,000)</u>
		83,47,000
Less: Depreciation on Machinery in use ₹ (7,84,375-24,000)		<u>(7,60,375)</u>
Book Value as on 31.03.2023		75,86,625

Note: The computation of depreciation and book value of plant and machinery can be presented in the following alternative manner

Particulars	Book value or Cost or Acquisition	Period	Deprecation	Book value as on 31.03.2023
Opening Value	46,70,000 (56,30,000-9,60,000)	01.04.2022 To 31.03.2023	4,67,000 (46,70,000×10%)	42,03,00
Sold	9,60,000	01.04.2022 to 30.06.2022	24,000 (9,60,000 x 10% x 3/12)	19,36,000
Purchases	21,12,000	01.06.2022 To 31.03.2023	1.17.375 (15,65,000 × 10%9/912	14,47,625
Total			7,84,375	75,86,625

(iii) Profit/Loss on Exchange of Machinery

Particulars	Amount in ₹
Balance as per books on 01.04.2022	9,60,000
Less: Depreciation for 3 months (₹ 9,60,000 × 10/100 × 3/12)	(24,000)
W.D.V. as on 30.06.2022	9,36,000
Less: Exchange Value	(8,25,000)
Loss on exchange on Machinery	1,11,000

QUESTION 72: (Q.AS.10.RMP.20)

Star Limited purchased machinery for ₹ 6,80,000 (inclusive of GST of ₹ 40,000). Input credit is available for entire amount of GST paid. The company incurred the following other expense for installation.

	₹
Cost of preparation of site for installation	21,200
Total Labour charges (200 out of the total of 500 men hours worked, were spent on installation of the machinery)	56,000
Spare parts and tools consumed in installation	5,000
Total salary of supervisor (Time spent for installation was 25% of the total time worked)	26,000
Total technical expense (1/10 relates to the plant installation)	34,000
Test run and experimental production expenses	18,000
Consultancy charges to architect for plant set up	11,000
Depreciation on assets used for installation	12,000

The machine was ready for use on 15.01.20X1 but was used from 01.02.20X1. Due to this delay further expenses of ₹ 8,900 were incurred. Calculate the value at which the plant should be capitalized in the books of Star Limited.

SOLUTION:**Calculation of cost of Plant**

Particulars		₹
Purchase Price	Given	6,80,000
Add: Site Preparation Cost	Given	21,200
Labour Charges	(56,000 x 200/500) Given	22,400
Spare Parts		5,000
Supervisor's Salary	25% of ₹ 26,000	6,500
Technical costs	1/10 of ₹ 34,000	3,400
Test run and experimental production charges	Given	18,000
Architect Fees for set up	Given	11,000
Depreciation on assets used for installation	Given	12,000
Total Cost of Asset		7,79,500
Less: GST Credit receivable		(40,000)
Value to be capitalized		7,39,500

Note: Further Expenses of ₹ 8,900 from 15.1.20X1 to 1.2.20X1 to be charged to profit and loss A/c plant was ready for production on 15.1.20X1

QUESTION 73: (RTP Sep'25)

Precision Tools Ltd. provides the following details related to its fixed assets for the year ended 31st March 2025:

The company purchased a machine for ₹ 12,00,000 on 1st October 2024. The following expenses were also incurred:

Freight and insurance: ₹ 60,000 Erection charges: ₹ 40,000

Testing Cost: Raw materials used ₹ 25,000, Wages ₹10,000, Sale of finished goods from testing production ₹ 8,000.

On 1st December 2024, it replaced the motor of an old machine with a new one costing ₹1,20,000, improving the output capacity by 15%. The old motor had a Cost of ₹50,000 and Accumulated Depreciation of ₹ 35,000.

On 15th March 2025, the company shifted a machine from one factory to another. It incurred the following:

Dismantling cost: ₹12,000

Transport and installation: ₹18,000

Loss due to damage in transit: ₹6,000

You are required to calculate the amount to be capitalized for each of the above cases as per AS 10.

SOLUTION

As per AS 10, Property, Plant and Equipment, the cost of an item of PPE includes:

- Purchase price including import duties and non-refundable taxes,
- Directly attributable costs to bring the asset to working condition (e.g., transport, installation, trial run),
- Any trial run net costs (i.e., cost – recoverable proceeds).

Particulars	Amount (₹)
Purchase Price	12,00,000
Freight & Insurance	60,000
Erection Charges	40,000
Net Cost of Testing (25,000 + 10,000 – 8,000)	27,000
Cost of Machinery	13,27,000

Recognition of Motors Replacement

Particulars	₹
Cost of Motors	50,000
Less: Depreciation	35,000
Carrying Amount of Motors	15,000

Accounting: The company should derecognize the existing Carrying Amount of Motors replaced of ₹ 15,000. Further, the acquisition cost of new motors of ₹ 1,20,000 would be capitalized as a separate component.

Costs of relocating or reorganising part or all of the operations of an enterprise are not included in the carrying amount of an item of PPE. Hence Costs of relocation of ₹ 36,000 (12,000 + 18,000 + 6,000) of PPE are not capitalized. Thus, entire expense to be charged off to Profit and Loss A/c.

Thus, total capitalization (net off derecognition) = 14,32,000 (13,27,2000 + 1,20,000 - 15,000).

QUESTION 74 (Exam Sep'25) (Jammu & Punjab) & (RTP May'26)

On 1st April, 2024, Y Limited purchased an industrial plot of land for ₹ 50,00,000 for the purpose of constructing a new factory. This cost of ₹ 50,00,000 included legal cost of ₹ 2,50,000 incurred for the purpose of acquisition of this plot. The construction of the factory commenced on 1st May, 2024. Y Limited provides you with the following details of the costs incurred in relation to the above construction:

Particulars	Amount (₹)
Preparation and levelling of the land	1,60,000
Employment costs of construction workers (per month)	58,000
Purchase of Raw materials for the construction	42,48,000
Cost of relocating the workers to new factory for work	75,000
Costs of inaugural function of the new factory on 1 st January, 2025	95,000
Overhead costs incurred directly on the construction of the factory (per month)	50,000

The construction of the factory was completed on 31st December, 2024 and production could commence on 1st February, 2025. The overall useful life of the factory building was estimated at 40 years from the date of completion. However, it was estimated that the roof would need to be replaced 20 years after the date of completion. The cost of replacing the roof at current prices would be 25% of the total cost of the building.

The construction of the factory was partly financed by a loan of ₹ 56,00,000 raised from State Bank of India on 1st April, 2024 at an interest rate of 9% per annum. During the period when the loan proceeds had been fully utilized to finance the construction, Y Limited earned an income of ₹ 50,000 from the temporary investment of the proceeds.

Assume that all of the net finance cost needs to be allocated to the cost of factory (excluding land) and interest cost to be capitalized based on nine months' period.

You are required to compute the carrying amount (i.e. value after charging depreciation) of the Factory in the books of Y Limited as at 31st March, 2025 as per the provisions of the relevant Accounting Standard.

SOLUTION –

Cost of construction of the factory

Particulars	Amount (₹)
Cost of Industrial Plot	50,00,000
Preparation and levelling of the land	1,60,000
Employment costs of construction workers (₹ 58,000 per month) for 8 months	4,64,000
Purchase of Raw materials for the construction	42,48,000
Overhead costs incurred directly on the construction of the factory (50,000per month) for 8 months	4,00,000
Interest on ₹ 56,00,000 for 9 months @ 9% = ₹ 3,78,000	
less ₹ 50,000	3,28,000
Total Cost (A)	1,06,00,000
Depreciation (B) (W.N.)	43,750
Carrying amount of the factory (A-B)	1,05,56,250

Working Note:

(1) Calculation of Depreciation

(a) On land of ₹ 50,00,000	Nil
(b) On remaining cost of Building i.e. ₹ 1,06,00,000 – 50,00,000	= ₹ 56,00,000
(a) Building ₹ 56,00,000 x 75% / 40 yrs x 3/12	= ₹ 26,250
(b) On roof ₹ 56,00,000 x 25% / 20 yrs x 3/12	= ₹ 17,500
Total Depreciation charged	₹ 43,750

(2) Cost of relocating the workers to new factory for work and cost of inaugural function of the new factory is not directly attributable to construction cost, hence not considered.

13. AS 13 – ACCOUNTING FOR INVESTMENT

QUESTION 75 (Q.AS13.SM.103)

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.

SOLUTION

As per AS 13 (Revised) 'Accounting for 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. And where investments are reclassified from current to long term, transfers are made at lower of cost and fair value on the date of transfer.

Accordingly, the re-classification will be done on the following basis:

- (i) In this case, carrying amount of investment on the date of transfer is less than the cost; hence this re-classified current investment should be carried at Rs 6.5 lakhs in the books.
- (ii) The carrying / book value of the long-term investment is same as cost i.e., Rs 7 lakhs. Hence this long-term investment will be reclassified as current investment at book value of Rs 7 lakhs only.
- (iii) In this case, reclassification of current investment into long-term investments will be made at Rs 10 lakhs as cost is less than its market value of Rs 12 lakhs.

QUESTION 76: (Q.INT.RMP.205 EXAM May'22 & Sep'24)

On 1st April 2021 Ms. Jayshree has 5,000 equity shares of Rama Limited (a listed company) of face value of Rs. 10 each. Ms. Jayshree has purchased the above shares at Rs. 15 per share and paid a brokerage of 2% and stamp duty of 1%.

On 15th May, 2021 Ms. Jayshree purchased another 5,000 shares of Rama Limited at Rs. 18 including brokerage and stamp duty.

On 26th August, 2021 Rama Limited issued bonus equity shares in the ratio of 1:2 held by the shareholders.

On 23rd October, 2021 Rama Limited announced a Right Issue which entitles the holders to subscribe 1 equity share for every 2-equity share held at Rs. 20 per share. Shareholders can exercise their rights in full or part. Ms. Jayshree sold 1/4th of entitlement to Mr. Mike for a consideration of Rs. 10 per share and subscribed the rest on November 2021.

Ms. Jayshree also sold 10,000 shares at Rs. 25 per share on 1st November, 2021.

The shares of Rama Limited were quoted at Rs. 11 per share on 31st March, 2022.

You are required to prepare Investment account for Ms. Jayshree for the year ended 31st march, 2022.

SOLUTION**In the books of Ms. Jayshree****Investment Account (Equity shares in Rama Ltd.)**

Date	Particulars	No. of shares	Amount (Rs.)	Date	Particulars	No. of shares	Amount (Rs.)
1.4.21	To Balance b/d	5,000	77,250	1.11.21	By Bank A/c	10,000	2,50,000
15.5.21	To Bank A/c	5,000	90,000				
26.8.21	To Bonus issue (W.N.1)	5,000	---	31.3.22	By Balance c/d	10,625	1,16,875
1.11.21	To Bank A/c (right shares) (W.N.4)	5,625	1,12,500	31.3.22	By Profit & Loss A/c (loss on valuation)		27,239
1.11.21	To Profit & Loss A/c		1,14,364				
		27,500	4,51,886			27,500	4,51,886

Working Notes:

- (1) Profit on sale of shares (average cost basis) on 1.11.21 10,000 shares @ Rs. 25 per share = 2,50,000
- (2) Cost of shares sold = $[(77,250 + 90,000 + 1,12,500) / 20,625 \times 10,000]$ = Rs. 1,35,634
Profit on sale of shares = Rs. 1,14,364
- (3) Value of shares on 31.3.22 $[(77,250 + 90,000 + 1,12,500) / 20,625 \times 10,625]$ = Rs. 1,44,114 or Rs. 1,16,875 (10,625 shares at Rs. 11)
- (4) Shares will be valued at Rs., 1,16,875 as market value is less than cost.

Note: Average cost basis has been considered for valuation of shares at the year end and for calculation of cost of shares sold in the given answer.

QUESTION 77: (Q.AS13.RMP.304 RTP May'24)

ABC Ltd. holds 2,000, 15% Debentures of ₹ 100 each in XYZ Ltd. as on April 1, 2022 at a cost of ₹ 2,50,000. Interest is payable on June, 30 and December, 31 each year.

Following are the details of 15% Debentures purchased and sold during the year 2022-23.

Particulars

On May 1, 2022, 1,000 debentures are purchased cum-interest at ₹ 1,05,000.

On November 1, 2022, 1200 debentures are sold ex-interest at ₹ 1,28,200.

On November 30, 2022, 500 debentures are purchased ex-interest at ₹ 54,500.

On December 31, 2022, 900 debentures are sold cum-interest for ₹ 1,18,000

You are required to prepare the investment Account showing value of holdings on March 31, 2023 at cost, using FIFO Method.

SOLUTION**In the Books of ABC Ltd****15% Debentures (Investment) Account**

Particulars	Face Value	Interest	Principal	Particulars	Face Value	interest	Principal
	₹	₹	₹		₹	₹	₹
1.4.22	To Balance b/d	2,00,000	7,500	30.6.22	By Bank A/c		
	To Bank			1.11.22	By Bank A/c	1,20,000	
						22,500	
						6,000	1,28,200

CA Intermediate					Advanced Accounts				
1.5.22	A/c				1.11.22	By P&L A/c			21,800
		1,00,000	5,000	1,00,000	31.12.22	By Bank A/c	90,000	6,750	1,11,250
30.11.22	To Bank A/c					By Bank A/c		10,500	
2	To P&L A/c	50,000	3,125	54,500	31.12.22	By Balance c/d			
31.12.22	To P&L A/c			1,250					
2	(Transfer)		35,375		31.3.23		1,40,000	5,250	1,44,500
31.3.23									
		3,50,000	51,000	4,05,750			3,50,000	51,000	4,05,750

1. Loss on sale of debentures on 1.11.22

Cost = $2,50,000 / 2,000 \times 1,200 = ₹ 1,50,000$

Sale proceeds = ₹ 1,28,200

Loss = ₹ 1,50,000 less ₹ 1,28,200 = ₹ 21,800

2. Profit on sale of debentures on 31.12.22

Cost = $2,50,000 / 2,000 \times 800 + 1,00,000 / 1,000 \times 100 = ₹ 1,10,000$
(1,00,000+10,000)

Sale proceeds = ₹ 1,11,250

Loss = ₹ 1,11,250 less ₹ 1,10,000 = ₹ 1,250

3.

Calculation of closing balance:	Units		₹
Debentures in hand remained in hand at 1.4.23	900	1,00,000 x	90,000
	<u>500</u>	9/10	<u>54,500</u>
Purchased on 1st May, 22	<u>1,400</u>	54,500	<u>1,44,500</u>
Purchased on 30th Nov. 22			

QUESTION 78: (Q.INT.RMP.306 EXAM Nov19)

Mr. Harsh provides the following details relating to his holding in 10% debentures (face value of Rs. 100 each) of Exe Ltd. held as current assets:

1.4.2018	opening balance - 12,500 debentures, cost Rs. 12,25,000
1.6.2018	purchased 9,000 debentures @ Rs. 98 each ex-interest
1.11.2018	purchased 12,000 debentures @ Rs. 115 each cum interest
31.1.2019	sold 13,500 debentures @ Rs. 110 each cum-interest
31.3.2019	Market value of debentures @ Rs. 115 each

Due dates of interest are 30th June and 31st December.

Brokerage at 1% is to be paid for each transaction. Mr. Harsh closes his books on 31.3.2019. Show investment account as it would appear in his books assuming FIFO method is followed.

SOLUTION**Investment Account of Mr. Harsh for the year ending on 31-3-2019****(Scrip: 10% Debentures of Exe Limited)****(Interest Payable on 30th June and 31st December)**

Date	Particulars	Nominal Value	Interest	Cost	Date	Particulars	Nominal Value	Interest	Cost
		Rs	Rs	Rs			Rs	Rs	Rs
1.4.18	To Balance b/d	12,50,000	31,250	12,25,000	30.6.18	By Bank 21,500 x 100 x 10% x 1/2	-	1,07,500	-
1.6.18	To Bank (ex-Interest) (W.N.1)	9,00,000	37,500	8,90,820	31.12.19	By Bank 33,500 x 100 x 10% x 1/2		1,67,500	
1.11.18	To Bank (cum-Interest) (W.N.2)	12,00,000	40,000	13,53,800	31.1.19	By Bank (W.N.3)	13,50,000	11,250	14,58,900
31.1.19	To P & L A/c (W.N.3)			1,34,920	31.3.19	By Balance c/d (W.N.4)	20,00,000	50,000	21,45,640
31.3.19	To P & L A/c (Bal. fig.)		2,27,500						
		33,50,000	3,36,250	36,04,540			33,50,000	3,36,250	36,04,540

Working Notes:**1. Purchase of debentures on 1.6.18**Interest element = $9,000 \times 100 \times 10\% \times 5/12 = \text{Rs. } 37,500$ Investment element = $(9,000 \times 98) + [1\% (9,000 \times 98)] = \text{Rs. } 8,90,820$ **2. Purchase of debentures on 1.11.2018**Interest element = $12,000 \times 100 \times 10\% \times 4/12 = \text{Rs. } 40,000$ Investment element = $12,000 \times 115 \times 101\% \text{ less } 40,000 = \text{Rs. } 13,53,800$ **3. Profit on sale of debentures as on 31.1.19**

	Rs
Sales price of debentures ($13,500 \times \text{Rs. } 110$)	14,85,000
Less: Brokerage @ 1%	(14,850)
	14,70,150
Less: Interest ($1,35,000 / 12$)	(11,250)
	14,58,900
Less: Cost of Debentures [$(12,25,000 + (890,820 \times 1,00,000 / 9,00,000))$]	(13,23,980)
Profit on sale	1,34,920

4. Valuation of closing balance as on 31.3.2019:

Market value of 20,000 Debentures at Rs. 115 = Rs. 23,00,000

Cost of

8,000 Debentures = $8,90,820 / 9,000 \times 8,000 = 7,91,840$ 12,000 Debentures = 13,53,800**Total** = **21,45,640**

Value at the end is Rs. 21,45,640, i.e., which is less than market value of Rs. 23,00,000.

QUESTION 79: (Q.AS13.RMP.402 EXAM July21)

Mr. Z has made following transactions during the financial year 2020-21:

Investment in 8% Corporate Bonds having face value Rs. 100/-

Date	Particulars
01-06-2020	Purchased 36,000 Bonds at Rs. 86 cum-interest. Interest is payable on 30th September and 31st March every year
15-02-2021	Sold 24,000 Bonds at Rs. 92 ex-interest

Interest on the bonds is received on 30th September and 31st March. Investment 2: Equity Shares of G Ltd having face value Rs. 10

Date	Particulars
01-04-2020	Opening balance 8,000 equity shares at a book value of Rs. 190 per share
01-05-2020	Purchased 7,000 equity shares @ Rs. 230 on cum right basis; Brokerage of 1% was paid in addition.
15-06-2020	The company announced a bonus issue of 2 shares for every 5 shares held
01-08-2020	The company made a rights issue of 1 share for every 7 shares held at Rs. 230 per share. The entire money was payable by 31.08.2020
25-08-2020	Rights to the extent of 30% of his entitlements was sold @ Rs. 75 per share. The remaining rights were subscribed.
16-09-2020	Dividend @ Rs. 6 per share for the year ended 31.03.2020 was received on 16.09.2020. No dividend payable on Right issue and Bonus issue.
01-12-2020	Sold 7,000 shares @ 260 per share. Brokerage of 1% was incurred extra.
25-01-2021	Received interim dividend @ Rs. 3 per share for the year 2020-21.
31-03-2021	The shares were quoted in the stock exchange @ Rs. 260.

Both investments have been classified as Current investment in the books of Mr. Z. On 15th May 2021, Mr. Z decides to reclassify investment in equity shares of Z Ltd. as Long term Investment. On 15th May 2021, the shares were quoted in the stock exchange @ Rs. 180.

You are required to:

- Prepare Investment Accounts in the books of Mr. Z for the year 2020-21, assuming that the average cost method is followed.
- Profit and loss Account for the year 2020-21, based on the above information.

Suggest values at which investment in equity shares should be reclassified in accordance with AS 13

SOLUTION

(i)

In the books of Mr. Z**Investment in 8% Corporate Bonds Account**

For the period 01 April 2020 to 31 March 2021

Date	Particulars	No's	Interest (Rs.)	Amount (Rs.)	Date	Particulars	No's	Interest (Rs.)	Amount (Rs.)
1/6/20	To Bank A/c (WN1)	36,000		30,48,000	30/9/20	By Bank A/c (Interest 36,000 x 100 x 8% x 6/12)		1,44,000	

CA Intermediate					Advanced Accounts				
15/2/21	To P & L A/c (WN 3)		48,000	1,76,000	15/2/21	By Bank A/c (WN2)	24,000	72,000	22,08,000
31/3/21	To P & L A/c		2,16,000		31/3/21	By Bank A/c (Interest 12,000 x 100 x 8% x 6/12)		48,000	
						By Balance c/d (WN 4)	12,000		10,16,000
	Total	36,000	2,64,000	32,24,000		Total	36,000	2,64,000	32,24,000

Note: For computing the interest on the bonds sold on 15 Feb 2021, if number of days (138 days) is taken instead of months, the interest received on 15.02.2021 should be Rs. 72,592 and the total interest transferred to Profit & Loss Account should be Rs. 2,16,592.

Investment in Equity Shares of Z Ltd
For the period 1st April 2020 to 31 March 2021

Date	Particulars	No's	Dividend (Rs.)	Amount (Rs.)	Date	Particulars	No's	Dividend (Rs.)	Amount (Rs.)
01/4/20	To balance b/d	8,000		15,20,000	16/9/20	By Bank A/c (WN 7)		48,000	42,000
01/5/20	To Bank A/c (WN 5)	7,000		16,26,100	1/12/20	By Bank A/c (WN 8)	7000		18,01,800
15/6/20	To Bonus Shares	6,000			25/1/21	By Bank A/c (WN 10)		48,300	
25/8/20	To Bank A/c (Right Shares) (WN 6)	2,100		4,83,000	31/3/21	By Balance c/d (WN 11)	16,100		25,00,100
01/12/20	To P & L A/c (Sale of shares) (WN 9)			7,14,800					
31/3/21	To P & L A/c		96,300						
	Total	23,100	96,300	43,43,900		Total	23,100	96,300	43,43,900

Working Notes

1. Computation of the Interest element in the bonds purchased on 01 June 2020

No of Bonds purchased	36,000
Face value per bond	Rs. 100
Face value of the bonds purchased	Rs. 36,00,000
Interest Rate	8%
Interest Amount	36,00,000 x 8% x 2/12
	Rs. 48,000
Cum-interest per bond	Rs. 86

Value of bond excluding interest	36,000 x Rs. 86 – Rs. 48,000
	Rs. 30,48,000

2. Computation of the Interest element in the bonds sold on 15 Feb 2021

No of Bonds sold	24,000
Face value per bond	Rs. 100
Face value of the bonds sold	Rs. 24,00,000
Interest Rate	8%
Interest Amount	Rs. 24,00,000 x 8% x 4.5/12
	= Rs. 72,000

3. Computation of Profit on Sale of Bonds on 15 Feb 2021

No of Bonds sold	24,000
Face value per bond	Rs. 100
Ex- interest Rate per bond	Rs. 92
Sales proceeds	Rs. 22,08,000
Average Cost of Bonds	(30,48,000/36,000) x 24,000
	Rs. 20,32,000
Profit on sale of bonds	Sale Proceeds – Average Cost
	Rs. 22,08,000 – Rs. 20,32,000
	Rs. 1,76,000

4. Valuation of Bonds as on 31 March 2021

No of Bonds held as on 31 Mar 2021	12,000
Average Cost of Bonds	(Rs. 30,48,000/36,000) x 12,000
	Rs. 10,16,000

5. Computation of the cost of the equity shares purchased on 01 May 2020

No of shares purchased	7,000
Cum right price per share	Rs. 230
Cost of purchase	Rs. 16,10,000
Brokerage @1%	Rs. 16,100
Cost including brokerage	Rs. 16,26,100

6. Right Shares

No of Right Shares Issued	(8,000+7,000+6,000)/7 = 3,000 shares
No of right shares sold	3,000 shares x 30% = 900 shares
Proceeds from sale of right shares to be credited to statement of profit & loss	900 shares x Rs. 75 = Rs. 67,500
No of right shares subscribed	3,000-900 = 2,100 shares
Amount of right shares subscribed	2,100 x 230 = Rs. 4,83,000

7. Computation of Dividend Received on 16 Sept 2020

No of shares held during the period of dividend	8,000 shares
Dividend per share	Rs. 6

Dividend Amount	8,000 x 6 = Rs. 48,000
No of shares received after the period of dividend (excluding bonus & right shares)	7,000 shares
Dividend per share	Rs. 6
Dividend Amount	7,000 x Rs. 6 = Rs. 42,000

The amount of dividend for the period for which the shares were not held by the investor has been treated as capital receipt. Thus Rs. 42,000 shall be treated as capital receipt

8. Sale Proceeds for the shares sold on 1st Dec. 2020

No of shares sold	7,000 Shares
Sale price per share	Rs. 260
Proceeds from sale of share	7,000 x 260 = Rs. 18,20,000
Less: Brokerage @ 1%	Rs. 18,200
Net Sale Proceeds	Rs. 18,01,800

9. Profit on sale of shares on 1st Dec. 2020

Sales Proceeds	Rs. 18,01,800
Average Cost	(15,20,000+16,26,100+4,83,000-42,000)/23,100x7,000
	= Rs. 10,87,000
Profit on sale of shares	= Sales Proceeds – Average Cost
	= Rs. 18,01,800 - Rs. 10,87,000
	= Rs. 7,14,800

10. Computation of Amount of Interim Dividend

No of shares held	8,000+7,000+6,000+2,100-7,000
	= 16,100
Dividend per share	Rs. 3 per share
Dividend Received	16,100 shares x Rs. 3 per share
	= Rs. 48,300

11. Valuation of Shares as on 31 March 2021

Cost of Shares	(15,20,000 + 16,26,100 + 4,83,000 – 42,000) / 23,100 x 16,100
	= 25,00,100
Market Value of Shares	= Rs. 260 x 16,100 = Rs. 41,86,000
Closing stock of equity shares has been value at Rs. 25,00,100 i.e., cost being lower than its market value.	

(ii)

Profit & Loss Account (Extract)

For the period 01 April 2020 to 31 March 2021

Particulars	Amount (Rs.)	Particulars	Amount (Rs.)
To Balance c/d	12,70,600	By Investment in 8% Corporate Bonds Account (Profit on sale of bonds)	1,76,000
		By Investment in 8% Corporate Bonds Account (Interest on bonds)	2,16,000

		By Sale of Right Shares	67,500
		By Investment in Equity Shares of G Ltd (Profit on sale of shares)	7,14,800
		By Investment in Equity Shares of G Ltd (Dividend Income)	96,300

(iii) As per AS 13, when investments are classified from Current Investments to Long term Investments, transfer is made at Cost and Fair value, whichever is less (as on the date of transfer). So, in the given case valuation shall be done as follows:

Date of reclassification/transfer – 15 May 2021

Per Unit Cost of 16,100 shares held – Rs. 25,00,100/16,100 shares – Rs. 155.29 Market Price/Fair Value per share – Rs. 180

As the cost per unit is lower than its fair value, the shares are to be transferred at its cost i.e., at Rs. 155.29 per share on 15 May 2021

Note:

1. In the eight last line of the question, investment in equity shares of G Ltd. was wrongly printed as Z Ltd. in the question paper. In the above solution, it has been considered as investment in G Ltd. If considered as Investment in equity shares in Z Ltd. (some other investment and not investment in G Ltd.), then the cost of the investment for shares in Z Ltd. will not be available.
2. The entire amount of sale proceeds from rights has been credited to Profit and Loss account in the above solution. However, the sale proceeds of rights in respect of 7,000 shares (purchased cum right on 1.5.20) can be applied to reduce the carrying amount of such investments (without crediting it to profit and loss account) considering that the value of these shares has reduced after becoming their ex-right. In that case, Rs. 22,500 (67,500X 7/21) will be applied to reduce the carrying amount of investment and Rs. 45,000 will be credited to profit and loss account.

QUESTION 80: (Q.AS13.RMP.404 RTP May19) (MTP May22)

A Ltd. purchased on 1st April, 2018 8% convertible debenture in C Ltd. of face value of Rs. 2,00,000 @ Rs. 108. On 1st July, 2018 A Ltd. purchased another Rs. 1,00,000 debentures @ Rs. 112 cum interest.

On 1st October, 2018 Rs. 80,000 debenture was sold @ Rs. 108. On 1st December, 2018, C Ltd. give option for conversion of 8% convertible debentures into equity share of Rs. 10 each. A Ltd. receive 5,000 equity share in C Ltd. in conversion of 25% debenture held on that date. The market price of debenture and equity share in C Ltd. at the end of year 2018 is Rs. 110 and Rs. 15 respectively. Interest on debenture is payable each year on 31st March, and 30th September. The accounting year of A Ltd. is calendar year.

Prepare investment account in the books of A Ltd. on average cost basis.

SOLUTION

Investment Account for the year ending on 31st December, 2018

Scrip: 8% Convertible Debentures in C Ltd.

[Interest Payable on 31st March and 30th September]

Date	Particulars	Nominal value (Rs)	Interest (Rs)	Cost (Rs)	Date	Particulars	Nominal Value (Rs)	interest (Rs)	Cost (Rs)
------	-------------	--------------------	---------------	-----------	------	-------------	--------------------	---------------	-----------

CA Intermediate					Advanced Accounts				
1.4.18	To bank A/c	2,00,000	-	2,16,000	30.09.18	By Bank A/c [Rs. 3,00,000 x 8% x (6/12)]		12,000	
1.7.18	To bank A/c (W.N.1)	1,00,000	2,000	1,10,000	1.10.18	By Bank A/c	80,000		86,400
31.12.18	To P & L A/c [Interest]	3,00,000	14,033	3,26,000	1.10.18	By P&L A/c (loss) (W.N.1)			533
					1.12.18	By Bank A/c (Accrued interest) (Rs. 55,000 x 0.08 x 2/12)		733	
					1.12.18	By Equity shares in C Ltd. (W.N. 3 and 4)	55,000		59,767
					1.12.18	By Balance c/d (W.N.5)	1,65,000	3,300	1,79,300
		3,00,000	16,033	3,26,000			3,00,000	16,033	3,26,000

SCRIP: Equity Shares in C LTD.

Date	Particulars	Cost (Rs)	Date	Particulars	Cost (Rs)
1.12.18	To 8 % debentures	59,767	31.12.18	By balance c/d	59,767

Working Notes:

- (i) Cost of Debenture purchased on 1st July = Rs. 1,12,000 – Rs. 2,000 (Interest) = Rs. 1,10,000
- (ii) Cost of Debentures sold on 1st Oct. = (Rs. 2,16,000 + Rs. 1,10,000) x 80,000/3,00,000 = Rs. 86,933
- (iii) Loss on sale of Debentures = Rs. 86,933 – Rs. 86,400 = Rs. 533
- Nominal value of debentures converted into equity shares = Rs. 55,000
 [(Rs. 3,00,000 – 80,000) x .25]

Interest received before the conversion of debentures:

Interest on 25% of total debentures = 55,000 x 8% x 2/12 = 733

- (iv) Cost of Debentures converted = (Rs. 2,16,000 + Rs. 1,10,000) x 55,000/3,00,000 = Rs. 59,767
- (v) Cost of closing balance of Debentures = (Rs. 2,16,000 + Rs. 1,10,000) x 1,65,000 / 3,00,000 = Rs. 1,79,300
- (vii) Closing balance of Debentures has been valued at cost being lower than the market value i.e., Rs. 1,81,500 (Rs. 1,65,000 @ Rs. 110)
- (viii) 5,000 equity Shares in C Ltd. will be valued at cost of Rs. 59,767 being lower than the market value Rs. 75,000 (Rs. 15 x 5,000)

Note: It is assumed that interest on debentures, which are converted into cash, has been received at the time of conversion.

14. AS 16 – BORROWING COSTS

QUESTION 81: (RTP Jan'25)

How will interest be capitalized when qualifying assets are funded by borrowings in the nature of bonds that are issued at a discount?

X Ltd. issued in year 1, a 3 year 10% p.a. (interest paid annually) bond with a face value of Rs. 1,00,000 at a price of Rs. 90,000 to finance a qualifying asset which is ready for intended use at the end of year 2. Compute the amount of borrowings costs to be capitalized if the company uses for amortization of discount straight line basis.

SOLUTION

As per AS 16, "Borrowing costs are interest and other costs incurred by an enterprise in connection with the borrowing of funds". Further, as per para 4 (b) of the standard, "amortization of discounts or premiums relating to borrowings" as a component of borrowing costs. Thus, the borrowing costs comprise the periodic interest payable on the bonds in question and the amount of discount amortised during the period.

Paragraph 6 of the Statement, inter-alia, states that "Borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset should be capitalized as part of the cost of that asset".

Further, paragraph 19 states that "Capitalisation of borrowing costs should cease when substantially all the activities necessary to prepare the qualifying asset for its intended use or sale are complete". Thus, only that portion of the amortised discount should be capitalised as part of the cost of a qualifying asset which relates to the period during which acquisition, construction or production of the asset takes place.

Straight line basis

(Amount in Rs.)

Years	Interest	Amortisation of discount	Total borrowing costs
Year 1	10,000	3,333	13,333
Year 2	10,000	3,333	13,333
Year 3	10,000	3,334	13,334

In the above case, the amount of borrowing costs capitalized would be Rs. 13,333 in Year 1 and Year 2. The borrowing costs of Rs. 13,334 incurred in Year 3 would be expensed since the asset is ready for its intended use at the end of Year 2.

QUESTION 82: (Q.AS16.RMP.202 RTP May'21) (Similar to Q201)

Shan Builders Limited has borrowed a sum of US \$ 10,00,000 at the beginning of Financial Year 2019-20 for its residential project at 4 %. The interest is payable at the end of the Financial Year. At the time of availment, exchange rate was Rs. 56 per US \$ and the rate as on 31st March, 2020 Rs. 62 per US \$. If Shan Builders Limited had borrowed the loan in India in Indian Rupee equivalent, the pricing of loan would have been 10.50%. You are required to compute Borrowing Cost and exchange difference for the year ending 31st March 2020 as per applicable Accounting Standards.

SOLUTION:

- Interest for the period 2019-20
= US \$ 10 lakhs × 4% × Rs. 62 per US \$ = Rs. 24.80 lakhs
- Increase in the liability towards the principal amount
= US \$ 10 lakhs × Rs. (62 - 56) = Rs. 60 lakhs
- Interest that would have resulted if the loan was taken in Indian currency
= US \$ 10 lakhs × Rs. 56 × 10.5% = Rs. 58.80 lakhs
- Difference between interest on local currency borrowing and foreign currency borrowing = Rs. 58.80 lakhs - Rs. 24.80 lakhs = Rs. 34 lakhs.

Therefore, out of Rs. 60 lakhs increase in the liability towards principal amount, only Rs. 34 lakhs will be considered as the borrowing cost. Thus, total borrowing cost would be Rs. 58.80 lakhs being the aggregate of interest of Rs. 24.80 lakhs on foreign currency borrowings plus the exchange difference to the extent of difference between interest on local currency borrowing and interest on foreign currency borrowing of Rs. 34 lakhs. Hence, Rs. 58.80 lakhs would be considered as the borrowing cost to be accounted for as per AS 16 "Borrowing Costs" and the remaining Rs. 26 lakhs (60 - 34) would be considered as the exchange difference to be accounted for as per AS 11 "The Effects of Changes in Foreign Exchange Rates".

QUESTION 83: (Q.AS16.RMP.204 EXAM May22)

Zebra limited began construction of a new plant on 1st April, 2021 and obtained a special loan of Rs. 20,00,000 to finance the construction of the plant. The rate of interest on loan was 10%. The expenditure that was incurred on the construction of plant was as follows:

	Rs.
1 st April, 2021	10,00,000
1 st August, 2021	24,00,000
1 st January, 2022	4,00,000

The company's other outstanding non-specific loan was Rs. 46,00,000 at an interest rate of 12%. The construction of the plant completed on 31st March, 2022.

You are required to:

- Calculate the amount of interest to be capitalized as per the provision of AS 16 "Borrowing Cost".
- Pass a journal entry for capitalizing the cost and the borrowing cost in respect of the plant

SOLUTION:

Total expenses to be capitalized for borrowings as per AS 16 "Borrowing Costs":

	Rs.
Cost of Plant (10,00,000 + 24,00,000 + 4,00,000)	38,00,000
Add: Amount of interest to be capitalized (W.N.)	3,24,000
	41,24,000

Journal Entry

		Rs.	Rs.
31 st March, 2022	Plant A/c Dr. To Bank A/c [Being amount of cost of plant and borrowing cost thereon capitalized]	41,24,000	41,24,000

Working Note:**Computation of interest to be capitalized:**

	Expenditure			Rs.
1 st April, 2021	10,00,000	On specific borrowing	Rs. 10,00,000 x 10%	1,00,000
1 st August, 2021	24,00,000	On specific borrowing	Rs. 10,00,000 x 10%	1,00,000
1 st August, 2021		On non-specific borrowings	Rs. 14,00,000 x 8/12 x 12%	1,12,000
1 st January, 2022	4,00,000	On non-specific borrowings	Rs. 4,00,000 x 3/12 x 12%	12,000
				3,24,000

Alternatively, interest cost to be capitalized can be derived by computing average accumulated expenses in the following manner.

Computation of Average Accumulated Expenses:

1 st April, 2021	10,00,000 x 12/12	10,00,000
1 st August, 2021	10,00,000 x 12/12 14,00,000 x 8/12	10,00,000 9,33,333
1 st January, 2022	4,00,000 x 3/12	1,00,000
		30,33,333

Computation of interest to be capitalized:

		Rs.
On specific borrowing	Rs. 20,00,000 x 10%	2,00,000
On non-specific borrowing	Rs. (30,33,333- 20,00,000) x 12%	1,24,000
		3,24,000

NOTE:

Since specific borrowings are earmarked for construction of a particular qualifying asset, it cannot be used for construction of any other qualifying asset except for temporary investment. Therefore, once the commencement of capitalization of borrowing cost criteria are met, actual borrowing cost incurred on specific borrowing shall be capitalized irrespective of the fact that amount had been utilized in parts.

QUESTION 84: (Q.AS16.RMP.208 RTP SEP'24)

Loyal Ltd. has undertaken a project for expansion of capacity as per the following details:

	Plan (₹)	Actual (₹)
October, 2023	5,00,000	4,00,000
November, 2023	6,50,000	7,95,000
December, 2023	20,00,000	-
January, 2024	2,00,000	50,000
February, 2024	9,00,000	2,00,000
March, 2024	10,00,000	12,00,000

The company pays to its bank interest at a rate of 15% p.a., which is debited on a monthly basis. During the half year, company had ₹ 20 lakh overdraft up to 31st December, surplus cash in January and again overdraft of ₹ 14 lakh from 1.2.2024 and ₹ 30 lakh from 1.3.2024. The company

had a strike during December and hence could not continue the work during said period. However, the substantial administrative work related to the project was continued. Onsite work was again commenced on 1st January and all the work were completed on 31st March. Assume that expenditure was incurred on 1st day of each month. Calculate interest to be capitalized giving reason wherever necessary. Assume overdraft will be less, if there is no capital expenditure.

SOLUTION:

Month	Actual Expenditure (₹)	Interest on outstanding amount @ 15% p.a.	Interest capitalized (₹)	Outstanding amount	Cumulative amount (₹)
	1		2	3	
October, 2023	4,00,000	$4,00,000 \times 15\% \times 1/12$	5,000	4,05,000	4,05,000
November, 2023	7,95,000	$(4,05,000 + 7,95,000) \times 15\% \times 1/12$	15,000	$(4,05,000 + 7,95,000) + 15,000$	12,15,000
December, 2023	-	$(12,15,000) \times 15\% \times 1/12$	15,188	$12,15,000 + 15,188$	12,30,188
January, 2024	50,000		-	$12,30,188 + 50,000$	12,80,188
February, 2024	2,00,000	$14,00,000 \times 15\% \times 1/12$	17,500	$12,80,188 + 2,00,000 + 17,500$	14,97,688
March, 2024	<u>12,00,000</u>	$(14,97,688 + 12,00,000) \times 15\% \times 1/12$	<u>33,721</u>	$14,97,688 + 12,00,000 + 33,721$	27,31,409
	<u>26,45,000</u>		<u>86,409</u>		

Note:

- As per para 18 of AS 16, 'Borrowing Cost', capitalisation of borrowing costs is not normally suspended during a period when substantial technical and administrative work is being carried out. Therefore, the interest for that period i.e. for the month of December has also been capitalized.
- During January, the company did not incur any interest as there was surplus cash in January. Therefore, no amount should be capitalized during January as per para 14(b) of AS 16.
- During February, actual overdraft (borrowings) was ₹ 14 lakh only. Hence, interest of ₹ 17,500 on ₹14,00,000 has been calculated even though actual expenditure on project exceed ₹ 14 lakh.

QUESTION 85: (Q.AS16.RMP.209)

Expert Limited issued 12% secured debentures of ₹ 100 lakhs on 01.06.20X1. Money raised from debentures to be utilized as under:

Intended Purpose	Amount ₹ in lakhs
Construction of factory building	40
Working Capital	30
Purchase of Machinery	15

Purchase of Furniture	2
Purchase of truck	13

Additional Information:

- Interest on debentures for the Financial Year 20X1-20X2 was paid by the Company.
- During the year, the company invested idle fund of ₹ 5 lakhs (out of the money raised from debentures) in Bank's fixed deposit and earned interest of ₹ 50,000.
- In March, 20X2 construction of factory building was not completed (it is expected that it will take
- In March 20X2, Machinery was installed and ready for its intended use.
- Furniture was put to use at the end of March 20X2.
- Truck is going to be received in April, 20X2.

You are required to show the treatment of interest as per AS 16 in respect of borrowing cost for the year ended 31st March, 20X2 in the Books of Expert Limited.

SOLUTION:

According to AS 16 "Borrowing Costs", a qualifying asset is an asset that necessarily takes a substantial period of time to get ready for its intended use. As per the Standard, borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset should be capitalized as part of the cost of that asset. The amount of borrowing costs eligible for capitalization should be determined in accordance with this Standard. Other borrowing costs should be recognized as an expense in the period in which they are incurred. It also states that to the extent that funds are borrowed specifically for the purpose of obtaining a qualifying asset, the amount of borrowing costs eligible for capitalization 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.

Thus, eligible borrowing cost = ₹ 10,00,000 (100 lakhs x 12% x 10/12) – ₹ 50,000 = ₹ 9,50,000

Particulars	Nature of assets	Interest to be capitalized (₹)	Interest to be charged to Profit & Loss Account (₹)
Construction of factory building	Qualifying Asset	$9,50,000 \times 40/100 = ₹ 3,80,000$	NIL
Purchase of Machinery	Not a Qualifying Asset	NIL	$9,50,000 \times 15/100 = 1,42,500$
Purchase of and furniture	Not a Qualifying Asset	NIL	$9,50,000 \times 2/100 = 19,000$
Purchase of truck	Not a Qualifying Asset	NIL	$9,50,000 \times 13/100 = 1,23,500$
Working Capital	Not a Qualifying Asset	NIL	$9,50,000 \times 30/100 = ₹ 2,85,000$
Total		₹ 3,80,000	₹ 5,70,000

QUESTION 86: EXAMPLE 11: - (SPECIFIC & GENERAL BORROWING)

Entity took a Loan from Axis Bank for Rs. 2,00,000 for Building Construction @9% p.a. on 1/4/22.

Entity has other two general Borrowings as Under:

10% SBI Loan = 9,00,000

12% HDFC Loan = 6,00,000

Expenditure on Building Construction are as Under:

1/4/22 – 1,20,000; 1/5/22 – 4,00,000; 1/7/22 – 6,80,000 & 1/12/22 = 4,00,000

Calculate BC to be Capitalised

SOLUTION:

Whenever Specific & General both borrowings are applied to a Qualifying Asset. We shall assume that Specific borrowing is applied first

Working Note 1: Weighted Average Capitalisation Rate.

Borrowings	Borrowing Cost
9,00,000	90,000
6,00,000	72,000
15,00,000	1,62,000

$$1,62,000 / 15,00,000 \times 100 = 10.8\%$$

Working Note 2: Capitalisation

Date	Particular	Specific	General
1/4/22	Expenditure out of Specific Loan	$1,20,000 \times 9\% = 10,800$	-
1/5/22	Total Expenditure	$80,000 \times 9\% = 7,200$	$3,20,000 \times 10.8\% \times 11/12 = 31,680$
1/7/22	Expenditure out of General Loan	-	$6,80,000 \times 10.8\% \times 9/12 = 55,080$
1/12/22	Expenditure out of General Loan	-	$4,00,000 \times 10.8\% \times 4/12 = 14,400$
	Borrowing Cost to be Capitalised	18,0000	1,01,160

Borrowing Cost Charged to P&L A/c:

Out of Specific Loan = Nil

Out of General Loan = $1,62,000 - 1,01,160 = 60,840$

QUESTION 87: EXAMPLE 13:

Entity Borrowed on 1/4/22 9%, 30 lakhs for Construction of two Qualifying assets. Construction Begins from 1/4/22. The loan was availed on 1/4/22 & started utilizing in Qualifying Asset. Remaining funds were temporarily invested @7% p.a.

	QA 1	QA 2
Expenditure on 1/4/22	5,00,000	10,00,000
Expenditure on 1/10/22	5,00,000	10,00,000

Calculate Total Borrowing Cost & Capitalised Borrowing Cost.

SOLUTION:

Particulars	QA 1	QA 2
Borrowing Cost	$10,00,000 \times 9\% = 90,000$	$20,00,000 \times 9\% = 1,80,000$
(-) Investment Income	$5,00,000 \times 7\% \times 6/12 = (17,500)$	$10,00,000 \times 7\% \times 6/12 = (35,000)$
Net Borrowing Cost to be Capitalised	72,500	1,45,000
Total Cost of QA (After Capitalisation)	10,72,500	21,45,000

15. ACCOUNTING STANDARD - 19

LEASES

QUESTION 88: (RTP SEP'25)

On 1st April, 2024, Mansi Ltd. sold a plant for ₹ 8,52,800. The carrying amount of the plant on that date was ₹ 1,80,000. The sale was a part of the package under which Akash Ltd. leased the asset to Mansi Ltd. for eight years term.

The economic life of the asset is estimated as 8 years. The minimum lease rents payable by the lessee has fixed at ₹ 1,60,000 payable annually beginning from 31st March, 2025.

The incremental borrowing interest rate of Mansi Ltd. is estimated at 10% p.a.

Calculate the net effect on the Statement of profit and loss in the books of Mansi Ltd.

SOLUTION

Net effect on the Statement of Profit and Loss in the year of sale in the books of Lessee (Mansi Ltd.) For calculation of net effect on the statement of profit and loss on sale of equipment, it has to be judged whether lease is an operating lease or finance lease.

The lease term is for 8 years which covers the entire economic life of the equipment. At the inception of the lease, the present value of the minimum lease payments (MLP) is ₹ 8,53,600 [$₹ 1,60,000 \times 5.335$ (Annuity factor of ₹ 1 @10% for 8 years)] and amounts to at least substantially all of the fair value (sale price i.e. ₹ 8,52,800) of the leased equipment. Thus, lease is a finance lease.

As per para 48 of AS 19 "Leases", if a sale and leaseback transaction results in a finance lease, profit of ₹ 6,72,800 (Sale value ₹ 8,52,800 less carrying amount ₹ 1,80,000) will not be recognized as income in the year of sale in the books of lessee i.e. Mansi Ltd. It should be deferred and amortised over the lease term in proportion to the depreciation of the leased asset.

Therefore, assuming that depreciation is charged on straight line basis, Mansi Ltd. will recognize depreciation of ₹ 1,06,600 per annum for 8 years ($₹ 8,52,800/8$) and amortise profit of ₹ 6,72,800 over the lease term of 8 years, i.e. ₹ 84,100 p.a.

The net effect is a debit of ($₹ 1,06,600 - 84,100$) ₹ 22,500 p.a. to the Statement of Profit and Loss, for 8 years as covered under the lease term.

QUESTION 89: (Q.AS19.SM.101 MTP Nov21)

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 (estimated by lessor)

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.

SOLUTION

According to para 11 of AS 19 “Leases”, the lessee should recognise the lease as an asset and a liability at an amount equal to the lower of the fair value of the leased asset at the inception of the finance lease & the present value of the minimum lease payments from the standpoint of the lessee.

In calculating the present value of the minimum lease payments the discount rate is the interest rate implicit in the lease. Present value of minimum lease payments will be calculated as follows:

Year	MLP	Internal Rate of Return	Present Value
1	6,25,000	0.8696	5,43,500
2	6,25,000	0.7561	4,72,563
3	6,25,000	0.6575	4,10,937
4	6,25,000 + 1,25,000 GRV	0.5718	4,28,850
Total	26,25,000		18,55,850

Present value of minimum lease payments Rs.18,55,850 is less than fair value at the inception of lease i.e. Rs.20,00,000, therefore, the lease liability should be recognised at Rs.18,55,850 as per AS19.

QUESTION 90: (Q.AS19.RMP.201 RTP – May’19; May’20 & Exams Jan’25)**(Annual Lease Payment is Missing)**

Aksat International Limited has given a machinery on lease for 36 months, and its useful life is 60 months. Cost & fair market value of the machinery is Rs. 5,00,000. The amount will be paid in 3 equal annual installments and the lessee will return the machinery to lessor at termination of lease. The unguaranteed residual value at the end of 3 years is Rs. 50,000. IRR of investment is 10% and present value of annuity factor of Rs 1 due at the end of 3 years at 10% IRR is 2.4868 and present value of Rs. 1 due at the end of 3rd year at 10% IRR is 0.7513.

You are required to comment with reason whether the lease constitute finance lease or operating lease. If it is finance lease, calculate unearned finance income.

SOLUTION**Determination of Nature of Lease**

Present value of unguaranteed residual value at the end of 3rd year

$$= \text{Rs. } 50,000 \times 0.7513$$

$$= \text{Rs. } 37,565$$

Present value of lease payments = Rs. 5,00,000 – Rs. 37,565

$$= \text{Rs. } 4,62,435$$

The percentage of present value of lease payments to fair value of the equipment is

$$(\text{Rs. } 4,62,435 / \text{Rs. } 5,00,000) \times 100 = 92.487\%.$$

Since, lease payments substantially covers the major portion of the fair value; the lease constitutes a finance lease.

Calculation of Unearned Finance Income

Annual lease payment = Rs. 4,62,435 / 2.4868 = Rs. 1,85,956 (approx.)

Gross investment in the lease = Total minimum lease payments + unguaranteed residual value

$$= (\text{Rs. } 1,85,956 \times 3) + \text{Rs. } 50,000$$

$$= \text{Rs. } 5,57,868 + \text{Rs. } 50,000 = \text{Rs. } 6,07,868$$

Unearned finance income = Gross investment - Present value of minimum lease payments and unguaranteed residual value
 = Rs. 6,07,868 – Rs. 5,00,000 = Rs. 1,07,868

QUESTION 91: (Q.AS19.RMP.204 MTP Nov'22)

Sun Limited leased a machine to Moon Limited on the following terms:

	(Amount in Rs.)
Fair value at inception of lease	50,00,000
Lease Term	4 Years
Lease Rental per annum	16,00,000
Guaranteed residual value	3,00,000
Expected residual value	4,50,000
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 Lease Liability and ascertain Unearned Finance Income as per AS-19.

SOLUTION:

According to AS 19 “Leases”, the lessee should recognise the lease as an asset and a liability at an amount equal to the fair value of the leased asset at the inception of the finance lease. However, if the fair value of the leased asset exceeds the present value of the minimum lease payments from the standpoint of the lessee, the amount recorded as an asset and a liability should be the present value of the minimum lease payments from the standpoint of the lessee. In calculating the present value of the minimum lease payments, the discount rate is the interest rate implicit in the lease. Present value of minimum lease payments will be calculated as follows:

Year	Minimum Lease Payment Rs.	Internal rate of return (Discount rate @15%)	Present value Rs.
1	16,00,000	0.8696	13,91,360
2	16,00,000	0.7561	12,09,760
3	16,00,000	0.6575	10,52,000
4	19,00,000*	0.5718	10,86,420
Total	67,00,000		47,39,540

Present value of minimum lease payments i.e., Rs. 47,39,540 is less than fair value at the inception of lease i.e., Rs. 50,00,000, therefore, the value of lease is Rs. 47,39,540 and lease liability should be recognized in the books at Rs. 47,39,540 as per AS 19.

Calculation of Unearned Finance Income

As per AS 19 on Leases, unearned finance income is the difference between (a) the gross investment in the lease and (b) the present value of minimum lease payments under a finance lease from the standpoint of the lessor; and any unguaranteed residual value accruing to the lessor, at the interest rate implicit in the lease.

Where:

- (i) Gross investment in the lease is the aggregate of (i) minimum lease payments from the stand point of the lessor and (ii) any unguaranteed residual value accruing to the lessor.

Gross investment = Minimum lease payments + Unguaranteed residual value
 = [Total lease rent + Guaranteed residual value (GRV)] + Unguaranteed residual value (URV)
 = [(Rs. 16,00,000 x 4 years) + Rs. 3,00,000] + Rs. 1,50,000 = Rs. 68,50,000

(ii) Present value of minimum lease payment from Lessor's view point

Lease liability Rs. 47,39,540 + present value of (URV) unguaranteed residual value (Rs. 1,50,000 x 0.5718) = Rs. 48,25,310

Unearned Finance Income = (a) – (b) = Rs. 68,50,000 – Rs. 48,25,310 = Rs. 20,24,690

*Minimum Lease Payment of 4th year includes guaranteed residual value amounting i.e 16,00,000 + 3,00,000 = 19,00,000.

QUESTION 92: (Q.AS19.SM.302 MTP May21)

A machine was given on 3 years operating lease by a dealer of the machine for equal annual lease rentals to yield 30% profit margin on cost Rs. 1,50,000. Economic life of the machine is 5 years and output from the machine are estimated as 40,000 units, 50,000 units, 60,000 units, 80,000 units and 70,000 units consecutively for 5 years. Straight line depreciation in proportion of output is considered appropriate. Compute the following:

- (i) Annual Lease Rent
- (ii) Lease Rent income to be recognized in each operating year and
- (iii) Depreciation for 3 years of lease.

SOLUTION:

(i) Annual lease rent

Total lease rent

$$= 130\% \text{ of Rs. } 1,50,000 \times \frac{\text{output during lease period}}{\text{total output}}$$

$$= 130\% \text{ of Rs. } 1,50,000 \times (40,000+50,000+60,000) / (40,000+50,000+ 60,000+80,000+70,000)$$

$$= 1,95,000 \times 1,50,000 \text{ units} / 3,00,000 \text{ units} = \text{Rs. } 97,500$$

$$\text{Annual lease rent} = \text{Rs. } 97,500 / 3 = \text{Rs. } 32,500$$

(ii) Lease rent Income to be recognized in each operating year

Total lease rent should be recognised as income in proportion of output during lease period, i.e. in the proportion of 40:50:60.

Hence income recognised in years 1,2 and 3 will be as:

Year 1 Rs. 26,000,

Year 2 Rs. 32,500 and

Year 3 Rs. 39,000.

(iii) Depreciation for three years of lease

Since depreciation in proportion of output is considered appropriate, the depreciable amount Rs. 1,50,000 should be allocated over useful life 5 years in proportion of output, i.e. in proportion of 40:50:60:80:70

Depreciation for year 1 is Rs. 20,000, year 2 = 25,000 and year 3 = 30,000.

QUESTION 93: (Q.AS19.SM.401)

A Ltd. sold machinery having WDV of Rs. 40 Lacs to B Ltd. for Rs. 50 Lacs and the same machinery was leased back by B Ltd. to A Ltd. The lease back is operating lease.

Comment if-

- (a) Fair Market Value is Rs. 50 Lacs.
- (b) Fair Market Value is Rs. 60 Lacs.
- (c) Fair value is Rs. 45 Lacs and the sale price is Rs. 38 Lacs.
- (d) Fair value is Rs. 40 Lacs and the sale price is Rs. 50 Lacs.

- (e) Fair value is Rs. 46 Lacs and the sale price is Rs. 50 Lacs.
(f) Fair value is Rs. 35 Lacs and the sale price is Rs. 39 Lacs.

SOLUTION

Following will be the treatment in the given cases:

- a. When sales price of 50 lakhs is equal to fair value, A Ltd. should immediately recognise the profit of 10 lakhs (i.e. $50 - 40$) in its books.
- b. When fair value is 60 lakhs then also profit of 10 lakhs should be immediately recognised by A Ltd.
- c. When fair value of leased machinery is 45 lakhs & sales price is 38 lakhs, then loss of 2 lakhs ($40 - 38$) to be immediately recognised by A Ltd. in its books provided loss is not compensated by future lease payment.
- d. When fair value is 40 lakhs & sales price is 50 lakhs then, profit of 10 lakhs is to be deferred and amortised over the lease period.
- e. When fair value is 46 lakhs & sales price is 50 lakhs, profit of 6 lakhs ($46 - 40$) to be immediately recognised in its books & balance profit of 4 lakhs ($50 - 46$) is to be amortised/deferred over lease period.

When fair value is 35 lakhs & sales price is 39 lakhs, then the loss of 5 lakhs ($40 - 35$) to be immediately recognised by A Ltd. in its books and profit of 4 lakhs ($39 - 35$) should be amortised/deferred over lease period.

16. ACCOUNTING STANDARD - 26

INTANGIBLE ASSETS

QUESTION 94: (Q.AS26.SM.02 MTP May20 & Nov21)

During 20X1-X2, an enterprise incurred costs to develop and produce a routine low risk computer software product, as follows:

Particular	Rs.
Completion of detailed program and design (Phase 1)	50,000
Coding and Testing (Phase 2)	40,000
Other coding costs (Phase 3&4)	63,000
Testing costs (Phase 3&4)	18,000
Product masters for training materials (Phase 5)	19,500
Packing the products (1,500 units) (Phase 6)	16,500

After completion of phase 2, it was established that the product is technically feasible for the market.

You are required to state how the above referred cost to be recognized in the books of accounts.

SOLUTION:

As per AS 26, costs incurred in creating a computer software product should be charged to research and development expense when incurred until technological feasibility / asset recognition criteria has been established for the product. Technological feasibility / asset recognition criteria have been established upon completion of detailed program design, coding and testing. In this case, Rs. 90,000 would be recorded as an expense (Rs. 50,000 for completion of detailed program design and Rs. 40,000 for coding and testing to establish technological feasibility/asset recognition criteria). Cost incurred from the point of technological feasibility/asset recognition criteria until the time when products costs are incurred are capitalized as software cost (63,000+18,000+19,500)=Rs.1,00,500. Packing cost Rs.16,500 should be recognized as expenses and charged to P&LA/c.

QUESTION 95: (Q.AS26.RMP.03 Exam Jan21)

A Company acquired for its internal use a software on 01.03.2020 from U.K. for £ 1,50,000. The exchange rate on the date was as Rs. 100 per £. The seller allowed trade discount @ 2.5%. The other expenditures were:

- i) Import Duty 10%
 - ii) Additional Import Duty 5%
 - iii) Entry Tax 2% (Recoverable later from tax department).
 - iv) Installation expenses Rs. 1,50,000.
 - v) Professional fees for clearance from customs Rs. 50,000.
- Compute the cost of software to be Capitalized as per relevant AS.

SOLUTION:

Calculation of cost of software (intangible asset) acquired for internal use

Purchase cost of the software	£ 1,50,000
Less: Trade discount @ 2.5%	£ (3,750)
	£1,46,250
Cost in Rs. (UK £1,46,250 x Rs. 100)	146,25,000

Add: Import duty on cost @ 10% (Rs.)	<u>14,62,500</u>
	160,87,500
Add: Additional import duty @ 5% (Rs.)	<u>8,04,375</u>
	168,91,875
Add: Installation expenses (Rs.)	1,50,000
Add: Professional fee for clearance from customs (Rs.)	<u>50,000</u>
Cost of the software to be capitalized (Rs.)	<u>170,91,875</u>

Note: Since entry tax has been mentioned as a recoverable / refundable tax, it is not included as part of the cost of the asset.

QUESTION 96: (Q.AS26.OM.07 Old Course)

Vishnu Ltd. is engaged in research on a new process design for its product- It had incurred an expenditure of Rs. 265.37 lakhs on research upto 31st March, 2003. The development of the process began on 1st April, 2003 and the Development Phase Expenditure was Rs. 180 lakhs upto 31st March, 2004. From 1st April, 2004 the Company will implement the new process design which will result in a after-tax cost saving of Rs. 40 lakhs per annum for the next five years. The Company's Cost of Capital is 10%. At what cost should the asset be recorded and what is its amortisation amount?

SOLUTION

Research Expenditure: As per Para 41 of AS-26, the expenditure on research Rs. 265.37 lakhs should be expensed in the year in which it is incurred. It is presumed that the entire expenditure of Rs. 265.37 lakhs is incurred in financial year 2002-2003. Hence, it should be written off as an expense in that year itself.

Development Expenditure: As per para 44 of AS-26, the expenditure on development can be treated as an asset only if all the conditions listed in that paragraph are satisfied. It is presumed that the company has duly complied with this requirement.

Cost of internally generated intangible asset: Para 53 specifies the items which can be included in the cost of an internally generated intangible asset, while Para 54 specifies the exclusions there from. It is presumed that the expenditure of Rs.180 lakhs is determined in accordance with Para 53 and 54 of AS-26.

Discounting Future Cash Flows: As per Para 30 of AS-26, fair value of an intangible asset can be estimated by discounting estimated future net cash flows. Even if this paragraph is primarily related to estimation of fair value of an intangible asset acquired in the course of amalgamation in the nature of purchase, the concept can be extended for internally generated intangible asset also.

Cost savings from the new process design for five = Rs. 40 lakhs per year

Company's Cost of Capital = 10%

Annuity Factor at 10% for five years = 3.7908

(from the annuity tables)

Present value of future cash flows = Rs. 40 x 3.7908 = Rs. 151.63 lakhs

Carrying Amount of the Asset: Since the Present Value of Future Cash Flows is only Rs. 151.63 lakhs, (which is lower than the cost of Rs.180 lakhs), it is prudent to recognise an impairment loss of Rs. 180.00 lakhs - Rs. 151.63 lakhs = Rs. 28.37 lakhs in the financial year 2003-2004.

Amortisation Period and Amount: The Company can amortise Rs. 151.63 lakhs over a five-year period by charging Rs. 30.33 lakhs per annum from the financial year 2004-2005 onwards.

QUESTION 97: (Q.AS26.RMP.08 MTP Nov22) (EXAM Nov20)

Honey Ltd. is in the process of developing a new production method. During the financial year ended 31st March, 2021, total expenditure incurred on development of this production method was Rs. 98,00,000. On 1st Jan, 2021, the production method met the criteria as an intangible asset and expenditure incurred till this date was Rs. 68,00,000. Further expenditure incurred on the new method was Rs. 72,00,000 for the year ended 31st March, 2022 and recoverable amount of the know how embodied in the new method for this financial year is Rs. 52,00,000.

You are required to calculate:

- (1) The carrying amount of the Intangible asset on 31st March, 2021.
- (2) The expenditure to be shown in Statement of Profit and Loss for the year ended 31st March, 2022.
- (3) The carrying amount of the Intangible asset on 31st March, 2022.

SOLUTION

As per AS 26 'Intangible Assets'

- (i)** Carrying value of intangible asset as on 31.03.2021

At the end of financial year, on 31st March 2021, the production process will be recognized (i.e., carrying amount) as an intangible asset at a cost of Rs. 30 (98-68) lacs (expenditure incurred since the date the recognition criteria were met, i.e., from 1st January, 2021).

- (ii)** Expenditure to be charged to Profit and Loss account for the year ended 31.03.2022

	(Rs. in lacs)
Carrying Amount as on 31.03.2021	30
Expenditure during 2021-2022	72
Book Value	102
Recoverable Amount	(52)
Impairment loss	50

Rs. 50 lakhs to be charged to Profit and loss account for the year ending 31.03.2022.

- (iii)** Carrying value of intangible asset as on 31.03.2022

	(Rs. in lacs)
Book Value	102
Less: Impairment loss	(50)
Carrying amount as on 31.03.2022	52

QUESTION 98: (Q.AS26.RMP.09 RTP May21)

Naresh Ltd. had the following transactions during the financial year 2019 -2020:

- (i)** Naresh Ltd. acquired running business of Sunil Ltd. for Rs. 10,80,000 on 15th May, 2019. The fair value of Sunil Ltd.'s net assets was Rs. 5,16,000. Naresh Ltd. is of the view that due to popularity of Sunil Ltd.'s product in the market, its goodwill exists.
- (ii)** Naresh Ltd. had taken a franchise on July 2019 to operate a restaurant from Sankalp Ltd. for Rs. 1,80,000 and at an annual fee of 10% of net revenues (after deducting expenditure). The franchise expires after 6 years. Net revenues were Rs. 60,000 during the financial year 2019-2020.
- (iii)** On 20th August, 2019, Naresh Ltd, incurred costs of Rs. 2,40,000 to register the patent for its product. Naresh Ltd. expects the patent's economic life to be 8 years.

Naresh Ltd. follows an accounting policy to amortize all intangibles on straight line basis over the maximum period permitted by accounting standards taking a full year amortization in the year of

acquisition. Goodwill on acquisition of business to be amortized over 5 years (SLM) as per AS 14. Prepare a schedule showing the intangible assets section in Naresh Ltd. Balance Sheet at 31st March, 2020.

SOLUTION:**Naresh Ltd.****Balance Sheet (Extract relating to intangible asset) as on 31st March 2020**

	Note No.	Rs.
Assets	1	8,11,200
(1) Non-current assets		
Intangible assets		

Notes to Accounts (Extract)

		Rs.	Rs.
1.	Intangible assets		8,11,200
	Goodwill (Refer to note 1)	4,51,200	
	Franchise (Refer to Note 2)	1,50,000	
	Patents (Refer to Note 3)	2,10,000	

Working Notes:

		Rs.
(1)	Goodwill on acquisition of business	
	Cash paid for acquiring the business (purchase consideration)	10,80,000
	Less: Fair value of net assets acquired	(5,16,000)
	Goodwill	5,64,000
	Less: Amortisation as per AS 14 ie. over 5 years (as per SLM)	(1,12,800)
	Balance to be shown in the balance sheet	4,51,200
(2)	Franchise	1,80,000
	Less: Amortisation (over 6 years)	(30,000)
	Balance to be shown in the balance sheet	1,50,000
(3)	Patent	2,40,000
	Less: Amortisation (over 8 years as per SLM)	(30,000)
	Balance to be shown in the balance sheet	2,10,000

Note: Amortisation shall commence from the date when Asset is acquired or available for use. Hence, in this question, policy followed by company to charge full year amortization in the year of purchase is not justified.

17. ACCOUNTING STANDARD - 28

IMPAIRMENT OF ASSETS

QUESTION 99 (EXAM MAY'25)

A machine was acquired by Zest Ltd. on 01/04/2019 for ₹ 60 lakhs. It had a useful life of 6 years. The machine is depreciated on straight line basis and does not carry any residual value. On 01/04/2022, the carrying value of the machine was reassessed at ₹ 36 lakhs.

The surplus arising out of the revaluation being credited to revaluation reserve.

For the year ended March 2024, conditions indicating an impairment of the existed machine and the amount recoverable ascertained to be ₹ 9 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 Zest Ltd. The company had followed the policy of writing down the revaluatuon surplus by the increased charge of depreciation resulting from the revaluation.

SOLUTION

Statement showing impairment Loss

	(in lakhs)
Carrying amount of the machine as on 1 st April, 2019	60
Depreciation for 3 years i.e. 2019-2020 to 2021-2022 [$\frac{60 \text{ lakhs}}{6 \text{ years}} \times 3 \text{ years}$]	(30)
Carrying amount as on 31.03.2022	30
Add: Upward Revaluation (credited to Revaluation Reserve account)	6
Carrying amount of the machine as on 1 st April, 2022 (revalued)	36
Less: Depreciation for 2 years i.e. 2022-2023 & 2023-2024 [$\frac{36 \text{ lakhs}}{3 \text{ years}} \times 2 \text{ years}$]	(24)
Carrying amount as on 31.03.2024	12
Less: Recoverable amount	9
Impairment loss	3
Less: Balance in revaluation reserve as on 31.03.2024	6
Less: Enhanced depreciation met from revaluation reserve 2022-2023 & 2023-2024 = [(12-10) x 2 Years]	(4)
Impairment loss set off against revaluation reserve balance as per para 58 of AS 28 "Impairment of Assets"	(2)
Impairment Loss to be debited to profit and loss account	1

QUESTION 100: (Q.AS28.SM.102)

Ergo Industries Ltd. gives the following estimates of cash flows relating to Property, Plant and Equipment on 31-12-20X1. The discount rate is 15%

Year	Cash Flow (₹ in lakhs)
20×2	4000
20×3	6000
20×4	6000
20×5	8000
20×6	4000

CA Intermediate

Residual value at the end of 20X6
 Property, Plant and Equipment purchased on 1-1-20XX
 Useful life
 Net selling price on 31-12-20X1

Advanced Accounts

= ₹ 1000 lakhs
 = ₹ 40,000 lakh
 = 8 years
 = ₹20,000 lakhs

Calculate on 31-12-20X1:

- Carrying amount at the end of 20X1
- Value in use on 31-12-20X1
- Recoverable amount on 31-12-20X1
- Impairment loss to be recognized for the year ended 31-12-20X1
- Revised carrying amount.
- Depreciation charge for 20X2.

Note: The year 20XX is the immediate preceding year before the year 20X0.

SOLUTION:**Calculation of Value in Use**

Year	Cash flow	Discount as per 15%	Discounted cash flow
20×2	4,000	0.870	3,480
20×3	6,000	0.756	4,536
20×4	6,000	0.658	3,948
20×5	8,000	0.572	4,576
20×6	4,000	0.497	1,988
20×6	1,000 (Residual)	0.497	497
			19,025

a) Calculation of carrying amount:

- Original cost = ₹ 40,000 lakhs
- Depreciation for 3 years = $[(40,000 - 1000) \cdot 3 / 8] = ₹ 14,625$ lakhs
- Carrying amount on 31-12-20X1 = $[40,000 - 14,625] = ₹ 25,375$ lakhs

b) Value in use = ₹ 19,025 lakhs

c) Recoverable amount = higher of value in use and net selling price i.e. ₹ 20,000 lakhs

d) Impairment Loss = ₹ $(25,375 - 20,000) = ₹ 5,375$ lakhs

e) Revised carrying amount = ₹ $(25,375 - 5,375) = ₹ 20,000$ lakhs

f) Depreciation charge for 20X2 = $(20,000 - 1000) / 5 = ₹ 3,800$ lakhs

QUESTION 101: (Q.AS28.SM.106)

From the following details of an asset

- Find out impairment loss
- Treatment of impairment loss
- Current year depreciation

Particulars of Asset:

Cost of asset	₹ 56 lakhs
Useful life period	10 years
Salvage value	Nil
Current carrying value	₹27.30
Useful life remaining	lakhs
Recoverable amount	3 years

Upward revaluation done in last year	₹12 lakhs
	₹14 lakhs

SOLUTION

According to AS 28 "Impairment of Assets", an impairment loss on a revalued asset is recognised as an expense in the statement of profit and loss. However, an impairment loss on a revalued asset is recognised directly against any revaluation surplus for the asset to the extent that the impairment loss does not exceed the amount held in the revaluation surplus for that same asset.

Impairment Loss and its treatment	
Current carrying amount (including revaluation amount of ₹ 14 lakhs)	27,30,000
Less: Current recoverable amount	(12,00,000)
Impairment Loss	15,30,000
Impairment loss charged to revaluation Reserve	14,00,000
Impairment loss charged to profit and loss account	1,30,000

After the recognition of an impairment loss, the depreciation (amortization) charge for the asset should be adjusted in future periods to allocate the asset's revised carrying amount, less its residual value (if any), on a systematic basis over its remaining useful life.

In the given case, the carrying amount of the asset will be reduced to ₹ 12,00,000 after impairment. This amount is required to be depreciated over remaining useful life of 3 years (including current year). Therefore, the depreciation for the current year will be ₹ 4,00,000.

QUESTION 102: (Q.AS28.OM.202 CA FINAL)

A Ltd. gives following information

Asset	Carrying Amount	Cash generating unit
A	1,00,000	1
B	2,00,000	3
C	3,00,000	2
D	3,50,000	2
E	70,000	1
F	8,00,000	3
G	2,20,000	2
H	4,50,000	1
Goodwill X	90,000	Allocate in ratio 1:1:1
Goodwill Y	60,000	Unallocable
<u>Corporate:</u>		
Asset P	1,50,000	Allocate in ratio 3:2:1
Asset Q	2,00,000	Unallocable

Recoverable Amount of Cash generating Unit: 1 – 6,70,000; 2 – 8,40,000 and 3 – 10,30,000
 Recoverable Amount of Entity: Case A – 25,50,000; Case B – 25,40,000. Calculate impairment loss.

QUESTION 103: (Q.AS28.OM.301 CA FINAL)

Himalaya Ltd. which is in the business of manufacturing and exporting its product. Sometimes, back at the end of 20X4, the Government put restrictions on export of goods exported by Himalaya Ltd. and due to that restriction Himalaya Ltd. impaired its assets. Himalaya Ltd. acquired identifiable assets worth Rs 5,500 lakhs for Rs 6,000 lakh at the end of the year 20X0. The difference is treated as goodwill. The useful life of identifiable assets is 15 years and depreciated on a straight-line basis. When the Government put the restriction at the end of 20X4, the company recognised the impairment loss by determining the recoverable amount of assets for Rs 3,120 lakh. In 20X6 Government lifted the restriction imposed on the export and due to this favourable change, Himalaya Ltd. re-estimate recoverable amount, which was estimated at Rs 3,420 lakh.

Required:

- . Calculation and allocation of impairment loss in 20X4.
- . Reversal of impairment loss and its allocation as per AS 28 in 20X6.

SOLUTION

(Assuming goodwill is amortised over 5 years as per AS 14)

(i) Calculation and allocation of impairment loss in 20X4

(Amount in Rs.lakhs)

	Goodwill	Identifiable assets	Total
Historical cost	500	5,500	6,000
Accumulated depreciation/amortization (4 yrs.)	400	(1,467)	(1,467)
Carrying amount before impairment	100	4,033	4,133
Impairment loss*	(100)	(913)	(1013)
Carrying amount after impairment loss	0	3,120	3,120

***Notes:**

1. As per AS 28, an impairment loss should be allocated to reduce the carrying amount of the assets of the unit in the following order:
 - first, to goodwill allocated to the cash-generating unit (if any); and
 - then, to the other assets of the unit on a pro-rata basis based on the carrying amount of each asset in the unit.

Hence, first goodwill is impaired at full value and then identifiable assets are impaired to arrive at recoverable value.

(ii) Carrying amount of the assets at the end of 20X6 (Amount in Rs. lakhs)

End of 20X6	Goodwill	Identifiable assets	Total
Carrying amount in 20X6	0	2,553	2,553
Add: Reversal of impairment loss (W.N.2)	-	747	747
Carrying amount after reversal of impairment loss	-	3,300	3,300

Working Note:

1. **Calculation of depreciation after impairment till 20X6 and reversal of impairment loss in 20X6**

(Amount in Rs lakhs)			
	Goodwill	Identifiable assets	Total
A. Carrying amount after impairment loss in 20X4	0	3,120	3,120

CA Intermediate	Advanced Accounts		
B. Additional depreciation (i.e. $(3,120/11) \times 2$) refer Note	–	(567)	(567)
C. Carrying amount	0	2,553	2,553
D. Recoverable amount			3,420
E. Excess of recoverable amount over carrying amount (D-C)			867

Note: It is assumed that the restriction by the Government has been lifted at the end of the year 20X6. Therefore, depreciation for 2 years is calculated (2005, 2006).

2. Determination of the amount to be impaired by calculating depreciated historical cost of the identifiable assets without impairment at the end of 20X6

(Amount in Rs lakhs)

End of 20X6	Identifiable assets
Historical cost	5,500
Accumulated depreciation	$(366.67 \times 6 \text{ years}) = (2,200)$
Depreciated historical cost	3,300
Carrying amount (in W.N. 1)	2,553
Amount of reversal of impairment loss	747

Notes:

As per AS 28, in allocating a reversal of an impairment loss for a cash-generating unit, the carrying amount of an asset should not be increased above the lower of:

- its recoverable amount (if determinable); and
- the carrying amount that would have been determined (net of amortization or depreciation) had no impairment loss been recognised for the asset in prior accounting periods.

Hence impairment loss reversal is restricted to Rs 747 lakhs only.

Note:

Impairment Loss on Goodwill shall not be reversed except certain conditions.

QUESTION 104: (RTP MAY'26)

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.

Whether it will be a cash-generating unit as per AS 28?

SOLUTION

It is likely that the recoverable amount of an individual magazine title can be assessed. Even though the level of advertising income for a title is influenced, to a certain extent, by the other titles in the customer segment, cash inflows from direct sales and advertising are identifiable for each title. In addition, although titles are managed by customer segments, decisions to abandon titles are made on an individual title basis.

Therefore, it is likely that individual magazine titles generate cash inflows that are largely independent one from another and that each magazine title is a separate cash-generating unit.

18. ACCOUNTING STANDARD - 5

“NET PROFIT OR LOSS FOR THE PERIOD, PRIOR PERIOD ITEMS & CHANGE IN ACCOUNTING”

QUESTION 105 (RTP JAN'26)

Best Ltd. is engaged in the business of providing consultancy services. A few days back, it received a notice from GST department raising the demand of GST on consultancy services provided by it for ₹ 2,50,000.

Recently Best Ltd. paid the demand. In the books, the payment is recorded as an extraordinary expenditure.

Whether payment of tax demand raised by the taxation authority can be recognised as an extraordinary item?

ANSWER:

No, payment of tax cannot be recognised as an extraordinary item.

As per AS 5, "Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies", extraordinary items are income or expenses that arise from events or transactions which are clearly distinct from the ordinary activities of the enterprise and, therefore, are not expected to recur frequently or regularly.

In the instant case, providing consultancy services is the ordinary business activity of Best Ltd. The GST liability arises from these ordinary transactions. Payment of GST pursuant to a demand by the taxation authority is part of the normal business operations of the company.

Therefore, recording the payment of GST as an extraordinary expenditure is not correct. Such payments are ordinary expenses and should be recognised as part of the profit or loss from ordinary activities, and cannot be treated as an extraordinary item. Recognising such payments as an extra-ordinary item is contrary to AS 5.

QUESTION 106 (Q.AS5.SM.102)

- (i) During the year 20X1-20X2, a medium size manufacturing company wrote down its inventories to net realisable value by ₹ 5,00,000. Is a separate disclosure necessary?
- (ii) A company signed an agreement with the Employees Union on 1.9.20X2 for revision of wages with retrospective effect from 30.9.20X1. This would cost the company an additional liability of ₹ 5,00,000 per annum. Is a disclosure necessary for the amount paid in 20X2-X3?

ANSWER:

- (i) Although the case under consideration does not relate to extraordinary item, but the nature and amount of such item may be relevant to users of financial statements in understanding the financial position and performance of an enterprise and in making projections about financial position and performance. AS 5 on 'Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies' states that:

“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 require separate disclosure of items of income and expense in accordance with AS 5 include the write-down of inventories to net realisable value as well as the reversal of such write-downs.

- (ii) It is given that revision of wages took place on 1st September, 20X2 with retrospective effect

from 30.9.20X1. Therefore wages payable for the half year from 1.10.20X1 to 31.3.20X2 cannot be taken as an error or omission in the preparation of financial statements and hence this expenditure cannot be taken as a prior period item. Additional wages liability of ₹ 7,50,000 (for 1½ years @ ₹ 5,00,000 per annum) should be included in current year's wages.

It may be mentioned that additional wages is an expense arising from the ordinary activities of the company. Such an expense does not qualify as an extraordinary item. However, as per AS 5, 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.

QUESTION 107 (Q.AS5.SM.105)

In the current year, A Ltd. changed the depreciation method from the Straight Line Method (SLM) to Written Down Value (WDV) method. When A Ltd. recomputed depreciation retrospectively as per the new method, deficiency arose in depreciation in respect of past years. Therefore, it reduced the carrying amount of the asset by the amount of deficiency and such change in carrying amount (deficiency amount) has been debited to the statement of profit and loss as an extraordinary expense.

Whether the change in the carrying amount of assets due to the change in depreciation method should be treated as an extraordinary item?

SOLUTION

As per AS 5, "Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies" extraordinary items are 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.

A change in the method of charging depreciation is not an event that is clearly distinct from the ordinary activities of the entity. In the instant case, A Ltd. has changed the depreciation method and treated the reduction in carrying amount (or amount of deficiency in depreciation) of the asset as an extraordinary expense. This is not correct. Such deficiency should be treated as a normal expense.

A change in the estimated useful life of a depreciable asset (i.e. change in depreciation method) affects the depreciation in the current period and in each period during the remaining useful life of the asset. In both cases, the effect of the change relating to the current period is recognised as income or expense in the current period. The effect, if any, on future periods, is recognised in future periods.

The change in depreciation method is considered as a change in accounting estimate as per the provisions of AS 5.

QUESTION 108 (Q.AS5.RMP.201)

A limited company created a provision for bad and doubtful debts at 2.5% on debtors in preparing the financial statements for the year 20X1-X2.

Subsequently on a review of the credit period allowed and financial capacity of customers, the company decided to increase the provision to 8% on debtors as on 31.3.20X2. The accounts of the company were not approved by the Board of Directors till the date of decision. While applying the relevant accounting standard can this revision be considered as an extraordinary item or Prior Period Item?

ANSWER:

As per para 21 of AS 5 'Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies', the preparation of financial statements involves making estimates which are based on the circumstances existing at the time when the financial statements are prepared. It

may be necessary to revise an estimate in a subsequent period if there is a change in the circumstances on which the estimate was based. Revision of an estimate, by its nature, does not bring the adjustment within the definitions of a prior period item or an extraordinary item [para 21 of AS 5 (Revised) on Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies].

In the given case, a limited company created 2.5% provision for doubtful debts for the year 20X1-20X2. Subsequently in 20X2 the company revised the estimates based on the changed circumstances and wants to create 8% provision. As per AS-5 (Revised), this change in estimate is neither a prior period item nor an extraordinary item.

However, as per para 27 of AS 5 (Revised), a change in accounting estimate which has material effect in the current period, should be disclosed and quantified. Any change in the accounting estimate which is expected to have a material effect in later periods should also be disclosed and quantified.

QUESTION 109: (Q.AS5.RNP.202 RTP May18 & Nov22)

Bela Ltd. has a vacant land measuring 20,000 sq. mts, which it had no intention to use in the future. The Company decided to sell the land to tide over its liquidity problems and made a profit of Rs 10 Lakhs by selling the said land. Moreover, there was a fire in the factory and a part of the unused factory shed valued at Rs 8 Lakhs was destroyed. The loss from fire was set off against the profit from sale of land and profit of Rs 2 lakhs was disclosed as net profit from sale of assets.

You are required to examine the treatment and disclosure done by the company and advise the company in line with AS 5.

SOLUTION

As per AS 5 “Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies” 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.

In the given case the selling of land to tide over liquidation problems as well as fire in the Factory does not constitute ordinary activities of the Company. These items are distinct from the ordinary activities of the business. Both the events are material in nature and expected not to recur frequently or regularly. Thus, these are Extraordinary Items.

Therefore, in the given case, disclosing net profits by setting off fire losses against profit from sale of land is not correct. The profit on sale of land, and loss due to fire should be disclosed separately in the statement of profit and loss.

QUESTION 110: (Q.AS5.RMP.204 EXAM May22)

TQ Cycles Ltd. is in the manufacturing of bicycles, a labor-intensive manufacturing sector. In April 2022, the Government enhanced the minimum wages payable to workers with retrospective effect from the 1st January, 2022. Due to this legislative change, the additional wages for the period from January 2022 to March 2022 amounted to Rs. 30 lakhs. The management asked the Finance manager to charge Rs. 30 lakhs as prior period item while finalizing financial statements for the year 2022-23. Further, the Finance manager is of the view that this amount being abnormal should be disclosed as extra-ordinary item in the Profit and loss account for the financial year 2021-22.

Discuss with reference to applicable Accounting Standards.

SOLUTION

As per AS 5 “Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies” 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. The term does not include other adjustments necessitated by circumstances which though related to prior periods, are determined in the current period.

It is given that revision of wages took place in April, 2022 with retrospective effect from 1st January, 2022. Therefore, wages payable for the period from 1.01.2022 to 31.3.2022 cannot be taken as an error or omission in the preparation of financial statements and hence this expenditure cannot be taken as a prior period item. The full amount of wages payable to workers will be treated as an expense of current year and it will be charged to profit & loss account for the year 2022-23 as normal expenses.

It may be mentioned that additional wages is an expense arising from the ordinary activities of the company. Such an expense does not qualify as an extraordinary item. Therefore, finance manager is incorrect in treating increase as extraordinary item. However, as per AS 5, 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.

Therefore, additional wages liability of Rs. 30 lakhs should be disclosed separately in the financial statements of TQ Cycles Ltd. for the year ended 31st March, 2023.

QUESTION 111: (Q.AS5.RMP.205 RTP Nov18, Nov19, May22 & MTP May20, Nov22) (EXAM Nov22)

The Accountant of Mobile Limited has sought your opinion with relevant reasons, whether the following transactions will be treated as change in Accounting Policy or not for the year ended 31st March, 2017. You are required to advise him in the following situations in accordance with the provisions of AS 5

- (i) Provision for doubtful debts was created @ 2% till 31st March, 2016. From the Financial year 2016-2017, the rate of provision has been changed to 3%.
- (ii) During the year ended 31st March, 2017, the management has introduced a formal gratuity scheme in place of ad-hoc ex-gratia payments to employees on retirement.
- (iii) Till the previous year the furniture was depreciated on straight line basis over a period of 5 years. From current year, the useful life of furniture has been changed to 3 years.
- (iv) Management decided to pay pension to those employees who have retired after completing 5 years of service in the organization. Such employees will get pension of Rs. 20,000 per month. Earlier there was no such scheme of pension in the organization.
- (v) During the year ended 31st March, 2017, there was change in cost formula in measuring the cost of inventories.

SOLUTION

- (i) In the given case, Mobile limited created 2% provision for doubtful debts till 31st March, 2016. Subsequently in 2016-17, the company revised the estimates based on the changed circumstances and wants to create 3% provision. Thus, change in rate of provision of doubtful debt is change in estimate and is not change in accounting policy. This change will affect only current year.
- (ii) As per AS 5, the adoption of an accounting policy for events or transactions that differ in substance from previously occurring events or transactions, will not be considered as a change in accounting policy. Introduction of a formal retirement gratuity scheme by an employer in place of ad hoc ex-gratia payments to employees on retirement is a transaction which is substantially different from the previous policy, will not be treated as change in an accounting policy.

- (iii) Change in useful life of furniture from 5 years to 3 years is a change in estimate and is not a change in accounting policy.
- (iv) Adoption of a new accounting policy for events or transactions which did not occur previously should not be treated as a change in an accounting policy. Hence the introduction of new pension scheme is not a change in accounting policy.
- (v) Change in cost formula used in measurement of cost of inventories is a change in accounting policy.

QUESTION 112: (Q.AS5.RMP.208 EXAM Jan21) (RTP May23)

State whether the following items are an example of Change in Accounting policy / Change in Accounting Estimates / Extra-Ordinary Items / Prior Period Items / Ordinary Activity.

- i)** Actual Bad Debts turning out to be more than provisions.
- ii)** Change from Cost model to Revaluation model for Measurement of carrying amount of PPE.
- iii)** Government grant receivable as compensation for expenses incurred in previous accounting period.
- iv)** Treating Operating Lease as Finance Lease.
- v)** Capitalisation of borrowing cost on working capital.
- vi)** Legislative changes having long-term retrospective application.
- vii)** Change in method of depreciation from straight line to WDV.
- viii)** Government grant becoming refundable.
- ix)** Applying 10% depreciation instead of 15% on furniture.
- x)** Change in useful life of fixed asset.

SOLUTION

Classification of given items is as follows:

Sr. No.	Particulars	Remarks
(i)	Actual bad debts turning out to be more than provisions	Change in Accounting Estimates
(ii)	Change from Cost model to Revaluation model for measurement of carrying amount of PPE	Change in Accounting Policy
(iii)	Government grant receivable as compensation for expenses incurred in previous accounting period	Item of Ordinary Activity
(iv)	Treating operating lease as finance lease.	Prior- period Items
(v)	Capitalisation of borrowing cost on working capital	Prior-period Items (as interest on working capital loans is not eligible for capitalization)
(vi)	Legislative changes having long term retrospective application	Ordinary Activity
(vii)	Change in the method of depreciation from straight line to WDV	Change in Accounting Estimates
(viii)	Government grant becoming refundable	Extra -ordinary Items
(ix)	Applying 10% depreciation instead of 15% on furniture	Prior- period Items
(x)	Change in useful life of fixed assets	Change in Accounting Estimates

19. ACCOUNTING STANDARD – 9

REVENUE RECOGNITION

QUESTION 113 (RTP JAN'26)

Class Ltd. is a well-established real-estate developer and builder engaged in residential and commercial projects. In the financial year 2025, the company purchased a unit of land situated in a prime location for ₹ 225 crore, intending to develop a high-end residential complex. Within a few months of acquisition, due to a strategic decision to reallocate resources to another project and take advantage of favorable market conditions, Class Ltd. sold the land at a price of ₹ 360 crore. The company maintained proper books of accounts, and all legal formalities for the transfer were duly completed.

Advise Class Ltd. on the recognition of revenue from this transaction in the final statement of accounts for the year ended 31st March, 2025.

SOLUTION

AS 9 on 'Revenue Recognition' states that revenue is recognised when it is earned and there is reasonable certainty of its collection, arising from the ordinary activities of an enterprise.

In this case, Class Ltd. is in the business of buying and selling properties. **The land purchased and sold forms part of its inventory. The sale of land at ₹ 360 crore is a transaction arising from ordinary activities of the company. Therefore, the revenue is recognised when the sale is completed and collection is reasonably certain.**

In the light of AS 5, this transaction will **not be treated as an extraordinary item**, because it arises from the ordinary course of business. However, if the amount is of such size, nature, or incidence that its disclosure is relevant to explain the performance of the enterprise, the nature and amount of such items should be disclosed separately.

Hence, ₹ 360 crore realised from the sale of land shall be recognised as revenue in the year in which the sale is completed.

QUESTION 114: (Q.AS9.RMP.103 Exam Nov19, Nov22; RTP May22)

Indicate in each case whether revenue can be recognized and when it will be recognized as per AS-9.

- (1) Trade discount and volume rebate received.
- (2) Where goods are sold to distributors or others for resale.
- (3) Where seller concurrently agrees to repurchase the same goods at a later date.
- (4) Insurance agency commission for rendering services.
- (5) On 11-03-2019 cloths worth Rs 50,000 were sold to X mart, but due to refurbishing of their showroom being underway, on their request, clothes were delivered on 12-04-2019.

SOLUTION

- (1) Trade discounts and volume rebates received are not encompassed within the definition of revenue, since they represent a reduction of cost. Trade discounts and volume rebates given should be deducted in determining revenue.
- (2) When goods are sold to distributor or others, revenue from such sales can generally be recognized if significant risks of ownership have passed; however, in some situations the buyer may in substance be an agent and in such cases the sale should be treated as a consignment sale.
- (3) For transactions, where seller concurrently agrees to repurchase the same goods at a later

date that are in substance a financing agreement, the resulting cash inflow is not revenue as defined and should not be recognized as revenue.

- (4) Insurance agency commissions should be recognized on the effective commencement or renewal dates of the related policies.
- (5) On 11.03.2019, if X mart takes title and accepts billing for the goods then it is implied that the sale is complete and all risk and reward on ownership has been transferred to the buyers. Revenue should be recognized for year ended 31st March, 2019 notwithstanding that physical delivery has not been completed so long as there is every expectation that delivery will be made and items were ready for delivery to the buyer at the time.

QUESTION 115: (Q.AS.9.RMP.105 RTP May'24 & May'25)

Following information of BS Products Ltd. is given:

- I. Goods of ₹ 2,00,000 sold to Den Ltd. on 20-03-2023 but at the request of the buyer these were delivered on 10-04-2023.
- II. On 15-01-2023 goods of ₹ 3,00,000 were sent on consignment basis, of which 20% of the goods unsold are lying with the consignee as on 31-03-2023.
- III. ₹ 4,00,000 worth of goods were sold on approval basis on 01-12-2022. The period of approval was 3 months after which they were considered as sold. Buyer sent approval for 75% goods upto 31-01-2023 and no approval or disapproval received for the remaining goods till 31-03-2023.
- IV. Apart from the above, BS Products Ltd. sells goods to dealers also. One of the condition of sale is that interest is payable @ 2% p.m. for delayed payments by dealers. Percentage of interest recovery is only 10% i.e. ₹ 50,000 on such overdue outstanding due to various reasons. During the year 2022-23, company wants to recognize the entire interest receivable of ₹ 60,000.

You are required to advise the accountant of BS Products Ltd., with valid reasons, the amount to be recognized as revenue in above cases in the context of AS-9 and also determine the total revenue to be recognized for the year ending 31-03-2023.

SOLUTION:

- I. The seller of goods has transferred to the buyer the property in the goods for a price or all significant risks and rewards of ownership have been transferred to the buyer and the seller retains no effective control of the goods transferred to a degree usually associated with ownership; and
- II. No significant uncertainty exists regarding the amount of the consideration that will be derived from the sale of the goods.

Case (i)

The sale is complete but delivery has been postponed at buyer's request. BS Products Ltd. should recognize the entire sale of ₹ 2,00,000 for the year ended 31st March, 2023.

Case (ii)

20% goods lying unsold with consignee should be treated as closing inventory and sales should be recognized for ₹ 2,40,000 (80% of ₹ 3,00,000). In case of consignment sale revenue should not be recognized until the goods are sold to a third party.

Case (iii)

In case of goods sold on approval basis, revenue should not be recognized until the goods have been formally accepted by the buyer or the buyer has done an act adopting the transaction or the time period for rejection has elapsed or where no time has been fixed, a reasonable time has elapsed. Therefore, revenue should be recognized for the total sales amounting ₹ 4,00,000 as the time period for rejecting the goods had expired.

Case (iv)

As per the standard, “where the ability to assess the ultimate collection with reasonable certainty is lacking at the time of raising any claim, the revenue recognition is postponed to the extent of uncertainty involved. In such cases, the revenue is recognized only when it is reasonably certain that the ultimate collection will be made”. In this case, interest should be recognized only if the ultimate collection is certain and the company expects to realize interest for the delayed payments for ₹ 50,000 only. Hence, based on the past experience, the realization of interest for the delayed payments by the agent is certain only to the extent of this amount and not ₹ 60,000. Therefore, the interest income of ₹ 50,000 should be recognized in the books for the year ended 31st March, 2023.

Thus total revenue amounting ₹ 8,90,000 (2,00,000 + 2,40,000 + 4,00,000 + 50,000) will be recognized for the year ended 31st March, 2023 in the books of BS Products Ltd.

QUESTION 116: (Q.AS9.SM.106)

For the year ended 31st March 20X1, KY Enterprises has entered into the following transactions. On 31 March 20X1, KY supplied two machines to its customer ST. Both machines were accepted by ST on 31 March 20X1. Machine 1 was a machine that was routinely supplied by KY to many customers and the installation process was very simple.

Machine 1 was installed on 2 April 20X1 by ST's employees.

Machine 2 being more specialised in nature requires an installation process which is more complicated, requiring significant assistance from KY. Machine 2 was installed between 2 and 5 April 20X1. Details of costs and sales prices are as follows:

	Machine 1	Machine 2
Sale Price	3,20,000	3,00,000
Cost of production	1,60,000	1,50,000
Installation fee	Nil	10,000

How should above transactions be recognized by KY Enterprises for the year ended 31st March 20X1?

SOLUTION

Machine 1: As the installation process is simple, revenue from Machine 1 will be recognized on 31 March 20X1.

Revenue (Machine 1)	₹ 3,20,000
Cost of Goods Sold	₹ 1,60,000
Profit during the period	₹ 1,60,000

Since the question specifies that the machine is already accepted by ST on 31 March 20X1, the revenue arising from sale of the machine needs to be recognized for the year ending 31 March 20X1. This is because acceptance of the machine indicates that the risks and rewards pursuant to the ownership are transferred to ST.

Machine 2: Installation process for Machine 2 is more complicated, requiring significant assistance from KY Ltd. However, question specifies that the machine is already accepted by ST on 31 March 20X1. Assuming that there is no further approval/acceptance required from the buyer for the Machine sold, revenue from sale of Machine 2 can be recognized for the year ending 31 March 20X1.

Revenue (Machine 2)	₹ 3,00,000
Cost of Goods Sold	₹ 1,50,000
Profit during the period	₹ 1,50,000

However, installation fee which is for rendering installation services cannot be recognized until the

installation is complete. Since the machine is pending installation, the revenue in respect of installation charges ₹ 10,000 needs to be recognized on 5 April 20X1 once the installation process gets completed.

QUESTION 117: (Q.AS9.SM.107 Principle Agent)

Zigato runs a food-delivery business. As per the arrangement, Zigato allows customers to order food from local restaurants and is responsible the delivery of the food within stipulated time. During a particular year, it collects the money on orders made online as under:

Total price for the food item	-	₹ 200 lakhs
Delivery charges	-	₹ 60 lakhs
GST	-	₹ 40 lakhs
Total	-	₹ 300 lakhs

Zigato has received ₹ 300 lakhs for the above orders from customers and the orders were delivered to the customer in stipulated time.

How much revenue should be recognised by restaurants and how much revenue should be recognised by Zigato for the year?

SOLUTION

The risks and rewards associated with the food item are not with Zigato. When a customer has ordered a food item, whether the item will be prepared or not is the responsibility of the restaurant and not Zigato. Similarly, the responsibility to deliver the food item is with Zigato and the restaurant does not undertake responsibility for the same.

Therefore, the restaurant undertakes the principal's responsibility to prepare the food and ensure its quality. Zigato, on the other hand, is only responsible to deliver the food. Thus, Zigato is acting as an agent. Hence, it can only recognize revenue relating to that activity (which it does in the ordinary course of business). The revenue for Zigato, therefore, is ₹ 60 lakhs, whereas, the revenue for restaurants will be ₹ 200 lakhs.

It may be noted that the GST of ₹ 40 lakhs is a liability payable to the Government (third party), hence it does not form part of revenue.

QUESTION 118: (Q.AS9.SM.110 RTP Jan'25)

Mithya Ltd. Entered into agreement with Satya Ltd. For sale of goods costing ₹ 8 lakh at a profit of 20% on cost. The sale transaction took place on 1st February, 2024. On the same day, Satya Ltd. Entered into another agreement with Mithya Ltd. To resell the same goods at ₹ 10.80 lakh on 1st August, 2024. State the treatment of this transaction in the financial statements of Mithya Ltd. As on 31.03.2024. The pre- determined re-selling price covers the holding cost of Satya Ltd. Give the Journal Entries as on 31.03.2024 in the books of Mithya Ltd.

SOLUTION:

In the given case, Mithya Ltd. concurrently agreed to repurchase the same goods from Satya Ltd. on 1st February, 2024. Also the re-selling price is pre-determined and covers purchasing and holding costs of Satya Ltd. Hence, the transaction between Mithya Ltd. and Satya Ltd. on 1st February, 2024 should be accounted for as financing rather than sale. The resulting cash flow of ₹ 9.60 lakh received by Mithya Ltd., cannot be considered as revenue as per AS 9 "Revenue Recognition".

Journal Entries in the books of Mithya Ltd.

				₹ in lakh
1.2.2024	Bank Account To Advance from Satya Ltd*.	Dr.	9.60	9.60

	(Being advance received from Satya Ltd. amounting [₹ 8 lakh + 20% of ₹ 8 lakh = 9.60 lakh] under sale and re-purchase agreement)			
31.3.2024	Financing Charges Account To Satya Ltd. (Financing charges for 2 months [(10.80 – 9.60) x 2/6])	Dr.	0.40	0.40
31.3.2024	Profit and Loss Account To Financing Charges Account (Being amount of finance charges transferred to P& L Account)	Dr.	0.40	0.40

QUESTION 119: (Q.AS9.RMP.201 RTP Nov21)

How will you recognize revenue in the following cases:

1. Installation Fees;
2. Advertising and insurance agency commissions;
3. Subscriptions for publications.

SOLUTION

Installation Fees: In cases where installation fees are other than incidental to the sale of a product, they should be recognized as revenue only when the equipment is installed and accepted by the customer.

Advertising and insurance agency commissions: Revenue should be recognized when the service is completed. For advertising agencies, media commissions will normally be recognized when the related advertisement or commercial appears before the public and the necessary intimation is received by the agency, as opposed to production commission, which will be recognized when the project is completed. Insurance agency commissions should be recognized on the effective commencement or renewal dates of the related policies.

Subscription for publications: Revenue received or billed should be deferred and recognized either on a straight-line basis over time or, where the items delivered vary in value from period to period, revenue should be based on the sales value of the item delivered in relation to the total sales value of all items covered by the subscription.

QUESTION 120: (Q.AS9.SM.402)

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, 20X7 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, 20X7.

SOLUTION:

AS 9 on 'Revenue Recognition' states that where the ability to assess the ultimate collection with reasonable certainty is lacking at the time of raising any claim, revenue recognition is postponed to the extent of uncertainty involved. When recognition of revenue is postponed due to the effect of uncertainties, it is considered as revenue of the period in which it is properly recognised. In this case it may be assumed that collectability of claim was not certain in the earlier periods. This is supposed from the fact that only Rs 1,50,000 were collected against a claim of Rs 2,00,000. So, this transaction cannot be taken as a Prior Period Item.

In the light of AS 5, it will not be treated as extraordinary item. However, AS 5 states that 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. Accordingly, the nature and amount of this item should be disclosed separately.

20. ACCOUNTING STANDARD - 4

CONTINGENCIES & EVENTS OCCURRING

AFTER THE BALANCE SHEET DATE

QUESTION 121: (Q.AS4.SM.103)

A company **has filed a legal suit against the debtor** from whom Rs. 15 lakh is recoverable as on 31.03.2019. The chances of recovery by way of legal suit are not good as per the legal opinion by the counsel in April, 2019. Can the company provide for full amount of Rs. 15 lakh as provision for doubtful debts? Discuss in brief.

ANSWER:

As per AS 4 (Revised) "Contingencies and Events Occurring After the Balance Sheet Date", assets and liabilities should be adjusted for events occurring after the balance sheet date that provide additional evidence to assist the estimation of amounts relating to conditions existing at the balance sheet date.

In the given case, company should make the provision for doubtful debts, as legal suit has been filed on 31st March, 2019 and the chances of recovery from the suit are not good. Though, the actual result of legal suit will be known in future yet situation of non-recovery from the debtors exists before finalisation of financial statements. **Therefore, provision for doubtful debts should be made for the year ending on 31st March, 2019.**

QUESTION 122: (Q.AS4.SM.105)

A Limited Company closed its accounting year on 30.6.20X1 and the accounts for that period were considered and approved by the board of directors on 20th August, 20X1. The company was engaged in **laying pipeline for an oil company deep beneath the earth**. While doing the boring work on 1.9.20X1 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 30.6.20X1.

ANSWER

AS 4 (Revised) on Contingencies and Events Occurring after the Balance Sheet Date defines 'events occurring after the balance sheet date' as 'significant events, both favourable and unfavourable, that occur between the balance sheet date and the date on which financial statements are approved by the Board of Directors in the case of a company'. The given case is discussed in the light of the above mentioned definition and requirements given in AS 4 (Revised).

In this case the incidence, which was expected to push up cost, became evident after the date of approval of the accounts. So it is not an 'event occurring after the balance sheet date'. However, this may be mentioned in the Report of Approving Authority.

QUESTION 123: (Q.AS4.SM.108)

During the year 20X1-20X2, 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, 20X2. On 18th May, 20X2, the Court decided in favor 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, 20X2, and approved by the board on 30th May, 20X2.

ANSWER:

- 1) As per AS 4 (Revised), 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.
In the given case, **since Raj Ltd. was sued by a competitor for infringement of a trademark during the year 20X1-X2 for which the provision was also made by it, the decision of the Court on 18th May, 20X2, for payment of the penalty will constitute as an adjusting event** because it is an event occurred before approval of the financial statements. Therefore, Raj Ltd. should adjust the provision upward by Rs. 4 lakhs to reflect the award decreed by the Court to be paid by them to its competitor.
- 2) Had the judgment of the Court been delivered on 1st June, 20X2, it would be considered as an event occurring after the approval of the financial statements which is not covered by AS 4 (Revised). In that case, no adjustment in the financial statements of 20X1-X2 would have been required.

QUESTION 124: (Q.AS4.RMP.205 RTP May22)

Smart Ltd. closes its books of accounts every year on 31st March. The financial statements for the year ended 31st March, 2024 are to be approved by the approving authority on 30th June 2024. During the first quarter of 2024-2025, the following events / transactions has taken place. The accountant of the company seeks your guidance for the following:

- (i) Smart Ltd. has an inventory of 50 stitching machines costing at ₹ 5,500 per machine as on 31st March, 2024. The company is expecting a heavy decline in the demand in next year. The inventories are valued at cost or net realisable value, whichever is lower. During the month of April 2024, due to fall in demand, the prices have gone down drastically. The company has sold 5 machines during this month at a price of ₹ 4,000 per machine.
- (ii) A fire has broken out in the company's godown on 15th April, 2024. The company has estimated a loss of ₹ 25 lakhs of which 75% is recoverable from the Insurance company.
- (iii) The company has entered into a sale agreement on 30th March, 2024 to sell a property for a consideration of ₹ 7,50,000 which is being carried in the books at ₹ 5,50,000 at the year end. The transfer of risk and reward and sale is complete in the month of May 2024 when conveyance and possession get completed.
- (iv) The company has received, during the year 2022-2023, a government grant of ₹ 15 lakhs for purchase of a machine. The company has received a notice for refund of the said grant on 15th June, 2024 due to violation of some of the conditions of grant during the year 2023-2024.

You are required to state with reasons, how the above transactions will be dealt with in the financial statement for the year ended 31st March 2024.

SOLUTION:

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.

Assets and liabilities should be adjusted for events occurring after the balance sheet date that provide additional evidence to assist the estimation of amounts relating to conditions existing at the balance sheet date or that indicate that the fundamental accounting assumption of going concern is not appropriate.

In the given case, financial statements are approved by the approving authority on 30th June 2024.

On the basis of above principles, following will be the accounting treatment in the financial statements for the year ended at 31st March 2024:

- (i) Since on 31st March 2024, Smart Ltd. was expecting a heavy decline in the demand of the stitching machine. Therefore, decline in the value during April, 2024 will be considered as an adjusting event. Hence, Smart Ltd. needs to adjust the amounts recognized in its financial statements w.r.t. net realisable value at the end of the reporting period. Accordingly, inventory should be written down to ₹ 4,000 per machine. Total value of inventory in the books will be 50 machines x ₹ 4,000 = ₹ 2,00,000.
- (ii) A fire took place after the balance sheet date i.e. during 2024-2025 financial year. Hence, corresponding financials of 2023-2024 financial year should not be adjusted for loss occurred due to fire. However, in this circumstance, the going concern assumption will be evaluated. In case the going concern assumption is considered to be appropriate even after the occurrence of fire, no disclosure of the same is required in the financial statements.
- (iii) Since the transfer of risk and reward and sale was complete in the month of May, 2024 when conveyance and possession got complete, no revenue should be recognised with respect to it in the financial statements of 2023-2024. However, a disclosure for the same should be given by the entity.
- (iv) Since the notice has been received after 31 March but before 30 June 2024 (approval date), the said grant shall be adjusted in the financial statements for financial year 2023-2024 because the violation of the conditions took place in the financial year 2023-2024 and the company must be aware of it.

QUESTION 125: (Q.AS4.RMP.207 RTP Sep'24)

For five companies whose financial year ended on 31st March, 2023, the financial statements were approved by their approving authority on 15th June, 2023.

During 2023-2024, the following material events took place:

- (a) A Ltd. sold a major property which was included in the balance sheet at ₹ 1,00,000 and for which contracts had been exchanged on 15th March, 2023. The sale was completed on 15th May, 2023 at a price of ₹ 2,50,000.
- (b) On 30th April, 2023, a 100% subsidiary of B Ltd. declared a dividend of ₹3,00,000 in respect of its own shares for the year ended on 31st March, 2023.
- (c) On 31st May, 2023, the mail order activities of C Ltd. (a retail trading group) were shut down with closure costs amounting to ₹ 2.5 million.
- (d) On 1st July, 2023 the discovery of sand under D Ltd.'s major civil engineering contract site causes the cost of the contract to increase by 25% for which there would be no corresponding recovery from the customer.
- (e) A fire, on 2nd April, 2023, completely destroyed a manufacturing plant of E Ltd. It was expected that the loss of ₹ 10 million would be fully covered by the insurance company

You are required to state with reasons, how each of the above items numbered (a) to (e) should be dealt with in the financial statement of the various companies for the year ended 31st March, 2023.

SOLUTION:

Treatment as per AS 4 'Contingencies and Events Occurring After the Balance Sheet Date

(a)	A Ltd.	The sale of property should be treated as an adjusting event since contracts had been exchanged prior to the year-end. The effect of the sale would be reflected in the financial statements ended on 31.3.2023 and the profit on sale of property ₹ 1,50,000 would be treated as an extraordinary item.
-----	--------	--

(b)	B Ltd.	The declaration of dividend on 30 th April, 2023 of ₹ 3,00,000 would be treated as a non-adjusting event in the financial statements of 2022-2023. This is because, the dividend has been declared after the balance sheet date and no conditions existed on the balance sheet date for such declaration of dividend. Further as per AS 9, right to receive dividend is established when it is declared and not before that.
(c)	C Ltd.	A closure not anticipated at the year-end would be treated as a non-adjusting event. Memorandum disclosure would be required for closure of mail order activities since non disclosure would affect user's understanding of the financial statements.
(d)	D Ltd.	The event took place after the financial statements were approved by the approving authority and is thus outside the purview of AS 4. However, in view of its significance of the transaction, the directors may consider publishing a separate financial statement/additional statement for the attention of the members in general meeting.
(e)	E Ltd.	The event is a non-adjusting event since it occurred after the year-end and does not relate to the conditions existing at the year-end. However, it is necessary to consider the validity of the going concern assumption having regard to the extent of insurance cover. Also, since it is said that the loss would be fully recovered by the insurance company, the fact should be disclosed by way of a note to the financial statements.

21. ACCOUNTING STANDARDS – 7

CONSTRUCTION CONTRACTS

QUESTION 126: (Q.AS7.SM.106) (Contract Revenue)

AB contractors enters into a contract on 1st January 20X1 with XY to construct a 5-storied building. Under the contract, AB is required to complete the construction in 3 years (i.e., by 31st December 20X3). The following information is relevant:

Fixed price (agreed) ₹5 crore

Material cost escalation (to the extent of 20% of increase in material cost) Labour cost escalation (up to 30% of increase in minimum wages)

In case AB is able to complete the construction in less than 2 years and 10 months, it will be entitled for an additional incentive of ₹ 50 lakh. However, in case the construction is delayed beyond 3 years and 2 months, XY will charge a penalty of ₹ 20 lakh. At the start of the contract, AB has a reason to believe that construction will be completed in 2 years and 8 months. Assume that the construction was actually completed in 2 years 9 months.

Labour cost was originally estimated to be ₹1.20 crore (based on initial minimum wages). However, the costs have increased by 25% during the construction period.

Material costs have increased by 40% due to short-supply. The total increase in material cost due to the 40% escalation is ₹ 80 lakh.

You are required to suggest what should be the contract revenue in above case?

Assume that in year 20X2, XY has requested AB to increase the scope of the contract. An additional floor is required to be constructed and there is an increase in contract fee by ₹ 1 crore.

AB has incurred a cost of ₹ 20 lakh for getting the local authority approvals which it will be entitled to claim from XY in addition to the increase in the fixed fee.

Also measure the total contract revenue in this case.

SOLUTION

Total Revenue after considering the escalation costs, claims and incentives:

Fixed Price:	5.00 crore
Incentive for early completion	0.50 crore
Material costs recovery (to the extent of 20%)	0.40 crore
Labour costs recovery (Actual increase is less than 30%)	<u>0.30 crore</u> [1.20 crore x 25%]
Total Contract Revenue	6.20 crore
Add: Variation to the contract	1.00 crore
Add: Claims recoverable from XY	0.20 crore
Total Contract Revenue	7.40 crore

QUESTION 127: (Q.AS7.SM.107) (% of Completion)

RT Enterprises has entered into a fixed price contract for construction of a tower with its customer. Initial tender price agreed is ₹ 220 crore. At the start of the contract, it is estimated that total costs to be incurred will be ₹ 200 crore. At the end of year 1, this estimate stands revised to ₹ 202 crore. Assume that the construction is expected to be completed in 3 years.

During year 2, the customer has requested for a variation in the contract. As a result of that, the total contract value will increase by ₹ 5 crore and the costs will increase by ₹ 3 crore.

RT has decided to measure the stage of completion on the basis of the proportion of contract costs incurred to the total estimated contract costs. Contract costs incurred at the end of each year is:

Year 1: ₹ 52.52 crore

Year 2: ₹ 154.20 crore (including unused material of 2.5 crore)

Year 3: ₹ 205 crore.

You are required to calculate:

- Stage of completion for each year.
- Profit to be recognised for each year.

SOLUTION:

(a) Stage of completion = Costs incurred to date / Total estimated cost

Year 1 : 52.52 crore / 202 crore = 26%

Year 2: (154.20 crore – 2.50 crore) / 205 crore = 74%

Year 3: 205 crore / 205 crore = 100%

(b) Profit for the year

	Year 1	Year 2	Year 3
Contract Revenue (1)	57.20 crore (220 crore x 26%)	109.30 crore (225 crore x 74% - 57.20 crore)	58.50 crore (225 crore x 100% - 109.30 crore - 57.20 crore)
Contract Cost (2)	52.52 crore (202 crore x 26%)	99.18 crore (205 crore x 74% - 52.52 crore)	53.30 crore (205 crore x 100% - 99.18 crore - 52.52 crore)
Contract Profit (1)– (2)	4.68 crore	10.12 crore	5.20 crore

QUESTION 128: (Q.AS7.RMP.108) (Exam May 18 & May 23, MTP Nov21)

Sarita Construction Co. obtained a contract for construction of a dam. The following details are available in records of company for the year ended 31st March, 2018:

	Rs In Lakhs
Total Contract Price	12,000
Work Certified	6,250
Work not certified	1,250
Estimated further cost to completion	8,750
Progress payment received	5,500
Progress payment to be received	1,500

Applying the provisions of Accounting Standard 7 "Accounting for Construction Contracts" you are required to compute:

- Profit/Loss for the year ended 31st March, 2018.
- Contract work in progress as at end of financial year 2017-18.
- Revenue to be recognized out of the total contract value.
- Amount due from/to customers as at the year end.

SOLUTION:

(i)	Loss for the year ended, 31st March, 2018	(Rs in lakhs)
	Amount of foreseeable loss	
	Total cost of construction (6,250 + 1,250 + 8,750)	16,250
	Less: Total contract price	(12,000)
	Total foreseeable loss to be recognised as expense	4,250

According to AS 7, when it is probable that total contract costs will exceed total contract revenue, the expected loss should be recognised as an expense immediately.

Loss for the year ended, 31st March, 2018 amounting Rs 4,250 will be recognized.

(ii)	Contract work-in-progress as on 31.3.18	(Rs in lakhs)
	Contract work-in-progress i.e., cost incurred to date are Rs 7,500 lakhs:	6,250
	Work certified	1,250
	Work not certified	7,500

(iii) **Proportion of total contract value recognised as revenue**

Cost incurred till 31.3.18 is 46.15% ($7,500/16,250 \times 100$) of total costs of construction.

Proportion of total contract value recognised as revenue:

46.15% of Rs 12,000 lakhs = Rs 5,538 lakhs

(iv) **Amount due from/to customers at year end**

(Contract costs + Recognised profits – Recognised Losses) – (Progress payments received + Progress payments to be received)

= (7,500 + Nil – 4,250) – (5,500 + 1,500) Rs in lakhs

= [3,250 – 7,000] Rs in lakhs

Amount due to customers = Rs 3,750 lakhs

QUESTION 129: (Q.AS7.RMP.109) (RTP May'24) (% of Completion)

The following data is provided for M/s. Raj Construction Co.

- Contract Price - ₹ 85 lakhs
- Materials issued - ₹ 21 Lakhs out of which Materials costing ₹ 4 Lakhs is still lying unused at the end of the period.
- Labor Expenses for workers engaged at site - ₹ 16 Lakhs (out of which ₹ 1 Lakh is still unpaid)
- Further Cost estimated to be incurred to complete the contract - ₹ 35 Lakhs
- Specific Contract Cost – Rs. 5 Lakhs
- Sub-contract Cost (work done) – Rs. 7 Lakhs
- Advance to Sub-contractor – Rs. 4 Lakhs.

You are required to compute the Percentage of Completion, the Contract Revenue and Cost to be recognized as per AS-7.

SOLUTION:**Computation of Contract Cost**

	₹ Lakh	₹ Lakh
Material cost incurred on the contract (net of closing stock)	21-4	17
Add: Labour cost incurred on the contract (including outstanding amount)		16
Specified contract cost	given	5
Sub-contract cost (advances should not be considered)		7
Cost incurred (till date)		45
Add: further cost to be incurred		35
Total contract cost		80

- **Percentage of completion** = Cost incurred till date / Estimated total cost
= ₹ 45,00,000 / ₹ 80,00,000
= 56.25%

- **Contract revenue and costs to be recognized**

Contract revenue (₹ 85,00,000 × 56.25%) = ₹ 47,81,250

Contract costs = ₹ 45,00,000

22. ACCOUNTING STANDARD - 11

“EFFECTS OF CHANGES IN FOREIGN EXCHANGE RATES”

QUESTION 130: (Q.AS11.RMP.103 RTP Nov22)

A company had imported raw materials worth US Dollars 6,00,000 on 5th January, 2022, when the exchange rate was Rs. 43 per US Dollar. The company had recorded the transaction in the books at the above-mentioned rate. The payment for the import transaction was made on 5th April, 2022 when the exchange rate was Rs. 47 per US Dollar. However, on 31st March, 2022, the rate of exchange was Rs. 48 per US Dollar. The company passed an entry on 31st March, 2022 adjusting the cost of raw materials consumed for the difference between Rs. 47 and Rs. 43 per US Dollar.

In the background of the relevant accounting standard, is the company's accounting treatment correct? Discuss

SOLUTION

As per AS 11 (revised 2003), 'The Effects of Changes in Foreign Exchange Rates', monetary items denominated in a foreign currency should be reported using the closing rate at each balance sheet date. The effect of exchange difference should be taken into profit and loss account. Trade payables is a monetary item, hence should be valued at the closing rate i.e., Rs. 48 at 31st March, 2022 irrespective of the payment for the same subsequently at lower rate in the next financial year. The difference of Rs. 5 (Rs. 48 - Rs. 43) per US dollar should be shown as an exchange loss in the profit and loss account for the year ended 31st March, 2022 and is not to be adjusted against the cost of raw materials. In the subsequent year, the company would record an exchange gain of Rs. 1 per US dollar, i.e., the difference between Rs. 48 and Rs. 47 per US dollar. Hence, the accounting treatment adopted by the company is incorrect.

QUESTION 131: (Q.AS11.RMP.107 MTP May18, Nov21)

Om Ltd. purchased an item of property, plant and equipment for US \$ 50 lakh on 01.04.2019 and the same was fully financed by the foreign currency loan [US \$] repayable in five equal installments annually. (Exchange rate at the time of purchase was 1 US \$ = Rs. 60). As on 31.03.2020 the first installment was paid when 1 US \$ fetched ₹ 62.00. The entire loss on exchange was included in cost of goods sold. Om Ltd. normally provides depreciation on an item of property, plant and equipment at 20% on WDV basis and exercised the option to adjust the cost of asset for exchange difference arising out of loan restatement and payment. Calculate the amount of exchange loss, its treatment and depreciation on this item of property, plant and equipment.

SOLUTION

Exchange differences arising on restatement or repayment of liabilities incurred for the purpose of acquiring an item of property, plant and equipment should be adjusted in the carrying amount of the respective item of property, plant and equipment as Om Ltd. has exercised the option and it is long term foreign currency monetary item. Thus, the entire exchange loss due to variation of Rs. 20 lakhs on 31.03.2020 on payment of US \$ 10 lakh, should be added to the carrying amount of an item of property, plant and equipment and not to the cost of goods sold. Further, depreciation on the unamortized depreciable amount should also be provided.

Calculation of Exchange loss:

Foreign currency loan (in Rs.) = (50 lakh \$ x Rs. 60) = Rs. 3,000 lakhs

Exchange loss on outstanding loan on 31.03.2020 = Rs. 40 lakh US \$ x (62.00-60.00) = Rs. 80 lakhs.

So, Rs. 80 lakhs should also be added to cost of an item of property, plant and equipment with corresponding credit to outstanding loan in addition to Rs. 20 lakhs on account of exchange loss on payment of installment. The total cost of an item of property, plant and equipment to be increased by Rs. 100 lakh. Total depreciation to be provided for the year 2019-2020 = 20% of (Rs. 3,000 lakh + 100 lakh) = Rs. 620 lakhs.

QUESTION 132: (Q.AS11.SM.109)

A Ltd. has borrowed USD 10,000 in foreign currency on April 1, 20X1 at 5% p.a. annual interest and acquired a depreciable asset. The exchange rates are as under:

01/04/20X1 1 US\$ = ₹ 48.00

31/03/20X2 1 US\$ = ₹ 51.00

You are required to pass the journal entries in the following cases:

- (i) Option under Para 46A is not availed.
- (ii) Option under Para 46A is availed.
- (iii) The loan was taken to finance the operations of the entity (and not to procure a depreciable asset).

In all cases, assume interest accrued on 31 March 20X2 is paid on the same date.

SOLUTION

Journal Entries in the Books of A Ltd.

(i) Option under Para 46A is not availed

Date	Particulars	₹ (Dr.)	₹ (Cr.)
20X1			
Apr. 01	Bank Account (10,000 x 48) Dr.	4,80,000	
	To Foreign Loan Account		4,80,000
Mar 31	Finance Cost (USD 10,000 x 5% x ₹ 51) Dr.	25,500	
	To Bank Account		25,500
Mar 31	Foreign Exchange Difference Account (P/L) Dr.	30,000	
	To Foreign Loan Account [10,000 x (51-48)]		30,000

In this case, since the option under Para 46A is **NOT** availed, the Exchange Loss of ₹ 30,000 is recognised as an expense in the Statement of Profit and Loss for the year ending 31 March 20X2.

(ii) Option under Para 46A is availed

Date	Particulars	₹ (Dr.)	₹ (Cr.)
20X1			
Apr. 01	Bank Account (10,000 x 48) Dr.	4,80,000	
	To Foreign Loan Account		4,80,000
Mar 31	Finance Cost (USD 10,000 x 5% x ₹ 51) Dr.	25,500	
	To Bank Account		25,500
Mar 31	Foreign Exchange Difference Account (P/L) Dr.	30,000	
	To Foreign Loan Account [10,000 x (51-48)]		30,000
Mar 31	Property Plant & Equipment A/c Dr.	30,000	
	To Foreign Exchange Difference A/c		30,000

In this case, since the option under Para 46A is availed, the Exchange Loss of ₹ 30,000 is capitalized in the cost of Property, Plant and Equipment, which will indirectly get recognized in the Profit & Loss A/c by way of increased depreciation over the remaining useful life of the asset.

(iii) Option under Para 46A is availed

Date	Particulars	₹ (Dr.)	₹ (Cr.)
20X1			
Apr. 01	Bank Account (10,000 x 48) Dr.	4,80,000	
	To Foreign Loan Account		4,80,000
Mar 31	Finance Cost (USD 10,000 x 5% x ₹ 51) Dr.	25,500	
	To Bank Account		25,500
Mar 31	Foreign Exchange Difference Account (P/L) Dr.	30,000	
	To Foreign Loan Account [10,000 x (51-48)]		30,000
Mar 31	Foreign Currency Monetary Item Translation Difference A/c (FCMITDA) Dr.	30,000	
	To Foreign Exchange Difference A/c		30,000

In this case, since the option under Para 46A is availed, the Exchange Loss of ₹ 30,000 is accumulated in the FCMITD A/c, which will be subsequently spread over and debited to P&L A/c over the tenure of the loan.

QUESTION 133: (Q.AS11.SM.301)

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.

SOLUTION:

Since the forward contract was for speculation purpose the premium on contract i.e. the difference between the spot rate and contract rate will not be recorded in the books. Only when the contract is sold the difference between the contract rate and sale rate will be recorded in the Profit & Loss Account.

Sale Rate	Rs 47.18
Less: Contract Rate	(Rs 47.10)
Premium on Contract	<u>Rs 0.08</u>
Contract Amount	US\$ 1,00,000
Total Profit (1,00,000 x 0.08)	Rs 8,000

QUESTION 134: (Q.AS11.RMP.302 RTP May19, MTP March20)

Rau Ltd. purchased a plant for US\$ 1,00,000 on 01st February 20X1, payable after three months. Company entered into a forward contract for three months @ ₹49.15 per dollar. Exchange rate per dollar on 01st Feb. was ₹48.85. How will you recognise the profit or loss on forward contract in the books of Rau Ltd.?

SOLUTION

Forward Rate	₹49.15
Less: Spot Rate	<u>(₹48.85)</u>
Premium on Contract	₹0.30
Contract Amount	US\$ 1,00,000
Total Loss (1,00,000 x 0.30)	₹30,000

Contract period 3 months (2 months falling in the year ended 31st March, 20X1)

Loss to be recognised $(30,000/3) \times 2 = ₹20,000$ in the year ended 31st March, 20X1. Rest ₹10,000 will be recognised in the following year.

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.

23. ACCOUNTING STANDARD – 12

ACCOUNTING FOR GOVERNMENT GRANTS

QUESTION 135: (RTP JAN'26)

Mediwell Hospitals Ltd., a reputed healthcare company operating a chain of multi-specialty hospitals across India, had acquired 40 units of Doppler Scan Machines from Holiver Inc., USA, at a cost of US\$ 1,65,100 per unit at the beginning of the financial year 2022–23. The prevailing exchange rate at that time was ₹ 50 per US\$.

The acquisition was partly financed through a government grant amounting to ₹ 5 crores, which was sanctioned specifically for the purchase of these machines under a healthcare modernization scheme. The grant was sanctioned with a specific condition that, in the event of a change in management or ownership control of the company, the grant must be refunded to the government.

In April 2025, 51% of the company's shareholding was acquired by an overseas investor, thereby resulting in a change in management control. Consequently, the company became liable to refund the entire government grant.

The expected useful life of each Doppler scan machine is 5 years, and the company follows a Straight Line Method (SLM) of depreciation at 20% per annum. Additionally, Mediwell Hospitals Ltd. incurred the following directly attributable costs:

- Bank charges: US\$ 4,000 (for the import transaction as a whole)
- Sea freight: ₹ 7,500 per unit

You are further informed that the company has not maintained any Capital Reserve or Deferred Income Account in respect of the government grant received.

You are required to advise the accounting treatment in the books of Mediwell Hospitals Ltd. as a result of the return of the government grant, in the light of the relevant provisions of Accounting Standard (AS) 12 – Accounting for Government Grants.

SOLUTION:

The grant is received towards fixed asset. Capital approach is adopted.

Particulars	₹ in lakhs
Cost of asset (Doppler machines) (1,65,100*40 @ 50)	3,302
Add: Freight and other charges (4,000 @ 50+7,500 x 40)	<u>5</u>
	3,307
Less: Grants received	<u>(500)</u>
Cost as per AS-10	2,807
Less: Depreciation for 3 years (2,807 * 20% * 3)	<u>(1684.2)</u>
Carrying amount as on 1/4/2025	1,123
Add: Grant refunded	<u>500</u>
Revised carrying amount	1,623

QUESTION 136: (Q.AS12.RMP.02 RTP May'20, Nov'20; MTP Nov'22)

How would you treat the following in the accounts in accordance with AS 12 'Government Grants'?

- (i) Rs. 35 Lakhs received from the Local Authority for providing medical facilities to the employees.
- (ii) Rs. 100 Lakhs received as Subsidy from the Central Government for setting up a unit in a notified backward area.
- (iii) Rs. 10 Lakhs Grant received from the Central Government on installation of anti-pollution equipment.

SOLUTION

- (i) Rs. 35 lakhs received from the local authority for providing medical facilities to the employees is a grant received in the nature of revenue grant. Such grants are generally presented as a credit in the profit and loss statement, either separately or under a general heading such as 'Other Income'. Alternatively, Rs. 35 lakhs may be deducted in reporting the related expense i.e., employee benefit expenses.

- (ii) As per AS 12 'Accounting for Government Grants', where the government grants are in 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 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.

In the given case, the subsidy received from the Central Government for setting up a unit in notified backward area is neither in relation to specific fixed asset nor in relation to revenue. Thus, amount of Rs 100 lakhs should be credited to capital reserve.

- (iii) Rs 10 lakhs grant received for installation anti-pollution equipment is a grant related to specific fixed asset. Two methods of presentation in financial statements of grants related to specific fixed assets are regarded as acceptable alternatives. Under first method, the grant is shown as a deduction from the gross value of the asset concerned in arriving at its book value. The grant is thus recognised in the profit and loss statement over the useful life of a depreciable asset by way of a reduced depreciation charge. Under the second method, 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.

Thus, Rs 10 lakhs may either be deducted from the cost of equipment or treated as deferred income to be recognized on a systematic basis in profit & Loss A/c over the useful life of equipment.

QUESTION 137: (Q.AS12.SM.05 Refund)

A Ltd. purchased 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.

SOLUTION**IN THE BOOKS OF A LTD.****Journal Entries (at the time of refund of grant)**

- (1) **If the grant is credited to Fixed Assets Account:**

		Rs	Rs
I.	Fixed Assets A/c Dr.		16 lakhs
	To Bank A/c	16 lakhs	

	(Being grant refunded) The amount of refund should be Rs 16 Lakhs		
--	---	--	--

The balance of fixed assets after two years depreciation will be Rs 16 lakhs (W.N.1) and after refund of grant it will become (Rs 16 lakhs + Rs 16 lakhs) = Rs 32 lakhs on which depreciation will be charged for remaining two years. Depreciation = $(32-8)/2$ = Rs 12 lakhs p.a. will be charged for next two years.

(2) If the grant is credited to Deferred Grant Account:

As per para 14 of AS 12 'Accounting for Government Grants,' income from Deferred Grant Account is allocated to Profit and Loss account usually over the periods and in the proportions in which depreciation on related assets is charged. Accordingly, in the first two years (Rs 16 lakhs / 4 years) = Rs 4 lakhs p.a. x 2 years = Rs 8 lakhs were credited to Profit and Loss Account and Rs 8 lakhs was the balance of Deferred Grant Account after two years.

Therefore, on refund in the 3rd year, following entry will be passed:

		Rs	Rs
I.	Deferred Grant A/c Dr.	8 lakhs	
	Profit & Loss A/c Dr.	8 lakhs	
	To Bank A/c		16 lakhs
	(Being Government grant refunded)		

Deferred grant account will become Nil. The fixed assets will continue to be shown in the books at Rs 24 lakhs (W.N.2) and depreciation will continue to be charged at Rs 8 lakhs per annum for the remaining two years.

Working Notes:

i. Balance of Fixed Assets after two years but before refund (under first alternative)

Fixed assets initially recorded in the books = Rs 40 lakhs – Rs 16 lakhs = Rs 24 lakhs

Depreciation p.a. = $(Rs\ 24\ lakhs - Rs\ 8\ lakhs)/4\ years$ = Rs 4 lakhs per year

Value of fixed assets after two years but before refund of grant = Rs 24 lakhs – (Rs 4 lakhs x 2 years) = Rs 16 lakhs

ii. Balance of Fixed Assets after two years but before refund (under second alternative)

Fixed assets initially recorded in the books = Rs 40 lakhs

Depreciation p.a. = $(Rs\ 40\ lakhs - Rs\ 8\ lakhs)/4\ years$ = Rs 8 lakhs per year

Book value of fixed assets after two years = Rs 40 lakhs – (Rs 8 lakhs x 2 years)
= Rs 24 lakhs

Note: It is assumed that the question requires the value of fixed assets is to be given after refund of government grant.

QUESTION 138: (Q.AS12.RMP.08 RTP May'18, Nov'21)

D Ltd. acquired a machine on 01-04-2012 for Rs. 20,00,000. The useful life is 5 years. The company had applied on 01-04-2012, for a subsidy to the tune of 80% of the cost. The sanction letter for subsidy was received in November 2015. The Company's Fixed Assets Account for the financial year 2015-16 shows a credit balance as under:

Particulars	Rs
Machine (Original Cost)	20,00,000
Less: Accumulated Depreciation	12,00,000

(from 2012-13- to 2014-15 on Straight Line Method)	
	8,00,000
Less: Grant received	(16,00,000)
Balance	(8,00,000)

You are required to explain how should the company deal with this asset in its accounts for 2015-16?

SOLUTION

From the above account, it is inferred that the Company follows Reduction Method for accounting of Government Grants. Accordingly, out of the Rs. 16,00,000 that has been received, Rs. 8,00,000 (being the balance in Machinery A/c) should be credited to the machinery A/c. The balance Rs. 8,00,000 may be credited to P&L A/c, since already the cost of the asset to the tune of Rs. 12,00,000 had been debited to P&L A/c in the earlier years by way of depreciation charge, and Rs. 8,00,000 transferred to P&L A/c now would be partial recovery of that cost.

There is no need to provide depreciation for 2015-16 or 2016-17 as the depreciable amount is now Nil.

QUESTION 139: (Q.AS12.RMP.10 Exam May'23)

On 1st April 2021, Eleanor Limited purchased a manufacturing Plant for Rs. 60 lakhs, which has an estimated useful life of 10 years with a salvage value of Rs. 10 lakhs. On purchase of the Plant, a grant of Rs. 20 lakhs was received from the government.

You are required to calculate the amount of depreciation as per AS-12 for the financial year 2022-23 in the following cases:

- If the grant amount is deducted from the value of Plant.
 - If the grant is treated as deferred income.
 - If the grant amount is deducted from the value of Plant, but at the end of the year 2022-2023 grant is refunded to the extent of Rs. 4 lakhs, due to non-compliance of certain conditions.
 - If the grant is treated as the promoter's contribution.
- (Assume depreciation on the basis of Straight-Line Method.)

SOLUTION

Calculation of depreciation as per AS 12 for the financial year 2022-23:

- If the grant amount is deducted from the value of Plant, then the amount of deprecation will be Rs. 3,00,000 p.a. $(Rs. 60,00,000 - Rs. 10,00,000 - Rs. 20,00,000) / 10$ year.
- If the grant is treated as deferred income, then amount of depreciation will be Rs. 5,00,000 p.a. $(Rs. 60,00,000 - Rs. 10,00,000) / 10$ year.
- If the grant amount is deducted from the value of plant, but at the end of the year 2022-23 grant is refunded to the extent of Rs. 4 lakh then the amount of depreciation will be Rs. 3,00,000 p.a. $(Rs. 60,00,000 - Rs. 10,00,000 - Rs. 20,00,000) / 10$ year for year 2021-22 and for the year 2022-23 Depreciation will be Rs. 3,00,000 calculated as follows, $(Rs. 60,00,000 - Rs. 10,00,000 - Rs. 20,00,000 - Rs. 3,00,000) / 10$ years.

Note: It is assumed that the depreciation for the year has been charged on the book value on the plant before making adjustment for grant. Alternatively, if it is considered otherwise then the depreciation will be charged after making adjustment for grant. In that case depreciation for the year 2022-23 will be as Rs. 3,44,444 calculated as follows, $(Rs. 60,00,000 - Rs. 10,00,000 - Rs. 20,00,000 + 4,00,000 - Rs. 3,00,000) / 9$ years

- If the grant is treated as promoter's contribution, then the amount of depreciation will be Rs. 5,00,000 p.a. $(Rs. 60,00,000 - 10,00,000) / 10$ year.

Note:

It is assumed that the depreciation for the year has been charged on the book value on the plant before making adjustment for grant. Alternatively, if it is considered otherwise then the depreciation will be charged after making adjustment for grant. In that case depreciation for the year 2022-23 will be as:

Cost of Plant	60,00,000
Less: Salvage Value	10,00,000
Less: Grant	20,00,000
Add: Grant Refundable	4,00,000
	34,00,000
Less: Depreciation for 2021-22	3,00,000
	31,00,000
Useful Life (years)	9
Depreciation for 2022-23	3,44,4444

QUESTION 140: (Q.AS12.RMP.12 RTP May'21)

Hygiene Ltd. had received a grant of Rs. 50 lakhs in 2012 from a State Government towards installation of pollution control machinery on fulfilment of certain conditions. The company, however, failed to comply with the said conditions and consequently was required to refund the said amount in 2020. The company debited the said amount to its machinery account in 2020 on payment of the same. It also reworked the depreciation for the said machinery from the date of its purchase and passed necessary adjusting entries in the year 2020 to incorporate the retrospective impact of the same. State whether the treatment done by the company is correct or not.

ABC Ltd. received two acres of land received for set up of plant. It also received Rs.2 lakhs received for purchase of machinery of Rs. 10 lakhs. Useful life of machinery is 5 years. Depreciation on this machinery is to be charged on straight-line basis. How should ABC Ltd. recognize these government grants in its books of accounts?

SOLUTION:

As per the facts of the case, Hygiene Ltd. had received a grant of Rs. 50 lakh in 2012 from a State Government towards installation of pollution control machinery on fulfilment of certain conditions. However, the amount of grant has to be refunded since it failed to comply with the prescribed conditions. In such circumstances, AS 12, "Accounting for Government Grants", requires that 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 capital reserve or the deferred income balance, as appropriate, by the amount refundable. The Standard further makes it clear that in the first alternative, i.e., where the book value of the asset is increased, depreciation on the revised book value should be provided prospectively over the residual useful life of the asset. Accordingly, the accounting treatment given by Hygiene Ltd. of increasing the value of the plant and machinery is quite proper. However, the accounting treatment in respect of depreciation given by the company of adjustment of depreciation with retrospective effect is improper and constitutes violation of AS 12.

ABC Ltd. should recognize the grants in the following **manner:**

- As per AS 12, 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. Accordingly, land should be recognised at nominal value in the balance sheet.

- The standard provides option to treat the grant either as a deduction from the gross value of the asset or to treat it as deferred income as per provisions of the standard. Under first method, the grant is shown as a deduction from the gross value of the asset concerned in arriving at its book value. The grant is thus recognised in the profit and loss statement over the useful life of a depreciable asset by way of a reduced depreciation charge. Accordingly, the grant of Rs. 2 lakhs is deducted from the cost of the machinery. Machinery will be recognised in the books at Rs. 10 lakhs – Rs. 2 lakhs = Rs. 8 lakhs and depreciation will be charged on it as follows:

Rs. 8 lakhs / 5 years = Rs. 1.60 lakhs per year.

Under the second method, 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. Such allocation to income is usually made over the periods and in the proportions in which depreciation on related assets is charged. Rs. 2 lakhs should be recognised as deferred income and will be transferred to profit and loss over the useful life of the asset. In this case, Rs. 40,000 [Rs. 2 lakhs / 5 years] should be credited to profit and loss each year over the period of 5 years.

24. ACCOUNTING STANDARD – 15

EMPLOYEE BENEFITS

QUESTION 141 (Q.AS15.SM.101 Defined Benefit Obligation)

An employee Roshan has joined a company XYZ Ltd. in the year 20X1. The annual emoluments of Roshan as decided is ₹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)

SOLUTION

Calculation of Defined Benefit Obligation (DBO)

Expected last drawn salary	₹ 14,90,210 x 110% x 110% x 110% x 110% x 110%	₹24,00,000
Defined Benefit Obligation (DBO)	₹ 24,00,000 x 25% x 5	₹30,00,000

Amount of ₹ 6,00,000 will be charged to Profit and Loss Account of the company every year as cost for Defined Benefit Obligation.

Calculation of Current Service Cost

Year	Equal apportioned amount of DBO [i.e. ₹ 30,00,000/5 years]	Discounting @ 8% PV factor	Current service cost (Present Value)
a	b	c	d = b × c
1	6,00,000	0.735 (4 Years)	4,41,000
2	6,00,000	0.794 (3 Years)	4,76,400
3	6,00,000	0.857 (2 Years)	5,14,200
4	6,00,000	0.926 (1 Year)	5,55,600
5	6,00,000	1 (0 Year)	6,00,000

Calculation of Interest Cost to be charged per year

	Opening balance	Interest cost	Current service cost	Closing balance
a	b	C = b × 8%	d	e = b + c + d
1	0	0	4,41,000	4,41,000
2	4,41,000	35,280	4,76,400	9,52,680
3	9,52,680	76,214	5,14,200	15,43,094
4	15,43,094	1,23,447	5,55,600	22,22,141
5	22,22,141	1,77,859*	6,00,000	30,00,000

*Due to approximations used in calculation, this figure is adjusted accordingly

Assume in **Q. 101** at Beginning of 3rd year. There is a change in Actuarial Assumptions & due to such Change the Revised Estimated DBO Liability at Beginning of 3rd year is Rs.

10,10,000/-

Solution:

Carrying Amt of DBO Payable at 2 nd year. end/3 rd Year Beginning	9,52,680
Revised Balance of DBO Payable	10,10,000
Increase in DBO Liability (Actuarial Loss)	57,320
Actuarial Loss (P&L) Dr	57,230
To DBO Payable A/c	57,230

Further Current Service Cost and Interest Cost from 3rd Year onwards will also be Revised based on New Revised Liability.

QUESTION 142 (Q.AS15.SM.104 Plan Assets and Return on Plan Assets)

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

SOLUTION

Computation of Expected and Actual Returns on Plan Assets

	₹
Return on ₹ 1,00,000 held for 12 months at 10.25%	10,250
Return on ₹ 30,000 (49,000-19,000) held for six months at 5% (equivalent to 10.25% annually, compounded every six months)	1,500
Expected return on plan assets for 20X1-20X2	11,750
Fair value of plan assets as on 31 March, 20X2	1,50,000
Less: Fair value of plan assets as on 1 April, 20X1	1,00,000
Contributions received	<u>49,000</u>
	(1,49,000)
	1,000
Add: Benefits paid	19,000
Actual return on plan assets	20,000

Alternatively, the above question may be solved without giving compound effect to rate of return.

QUESTION 143 (Q.AS15.SM.106 Curtailment and Settlement)

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 ₹ 18 (10% of ₹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 ₹6,000 based on current actuarial assumption.
- (b) The fair value of plan assets on the date is estimated at ₹5,100.
- (c) The unamortized past service cost is ₹180.
- (d) Curtailment reduces the obligation by ₹600, which is 10% of the gross obligation.

SOLUTION

Gain from curtailment is estimated as under:

	₹
Reduction in gross obligation	600
Less: Proportion of un-amortised past service cost	(18)
Gain from curtailment	582

The liability to be recognised after curtailment in the balance sheet is estimated as under:

	₹
Reduced gross obligation (90% of ₹ 6,000)	5,400
Less: Fair value of plan assets	(5,100)
Less: Un-amortised past service cost (90% of ₹180)	300
Liability to be recognised in the balance sheet	(162)
Liability to be recognised in the balance sheet	138

QUESTION 144: (Q.AS15.RMP.109 Sep'24 EXAMS)

Pendora Ltd. Has given the following details in respect of employee benefit pension plan:

Particulars	Amount ₹
The fair value of plan assets as on 01-04-2023	5,00,000
The benefits paid out on 30-11-2023	63,000
Inward contributions received on 30-09-2023	1,42,000
The fair value of plan assets as on 31-03-2024	7,50,000

On 01.04.2023, the company made following estimates, based on its market studies and prevailing prices:

Particulars	%
Interest and dividend income (after tax) payable by fund	10.50
Realized gains on plan assets (after tax)	2.00
Fund administrative cost	-2.00
Expected rate of annual return (interest in compounded annually)	10.50

You are required to find the expected and actual returns on plan assets as on 31.03.2024 as per AS 15.

SOLUTION:

Computation of Expected and Actual Returns on Plan Assets

	₹
Return on ₹ 5,00,000 held for 12 months at 10.50%	52,500
Return on ₹ 1,42,000 for 6 months at 10.50%	7,455
Loss of interest on benefits paid for 4 months on ₹ 63,000 for 4 months @ 10.50%	(2,205)
Expected return on plan assets for 2023-2024	57,750
Fair value of plan assets as on 31 st March 2024	7,50,000
Less: Fair value of plan assets as on 1 April, 2023 5,00,000	
Contributions received on 30.9.2023 1,42,000	(6,42,000)
	1,08,000
Add: Benefits paid on 30 th Nov 2023	63,000
Actual return on plan assets	1,71,000

QUESTION 145: (Q.AS15.RMP.110 Jan'25 EXAMS)

What is the difference between Defined Contribution Plan and Defined Benefit Plan? From the following information calculate the amount of defined benefit liability / asset:

Particulars	₹ in lakhs
Present Value of Defined Benefit Obligation as on 31-3-2024	36.0
Fair Value of Plan asset	38.5
Past service cost not yet recognized	7.5
Present value of available future refund from the plan	6.0

SOLUTION:

Difference between Defined Contribution Plan and Defined Benefit Plan:

S No.	Defined Contribution Plan	Defined Benefit Plan
1	Fixed Contributions are paid by the employer into a separate fund and will have no obligation to pay further contributions.	Detailed actuarial calculation is performed to determine the charge.
2	The employer has no obligation to pay further contributions if the fund does not hold sufficient assets to pay all employee benefits and the employee has to bear the investment and actuarial risk.	The employer ensures that sufficient funds are available to meet the promised benefits regardless of fund performance and the actuarial and investment risk fall on the employer.

Computation of defined benefit liability / Asset:

Particulars	₹ in lakhs
Present value of the defined benefit obligation as on 31.3.2024	36.00
Less: Past service cost not yet recognized	(7.50)
	28.50
Less: The fair value of plan assets	(38.50)
Defined benefit Asset	10.00

In case where fair value of plan assets is high, it may so happen that the net amount under defined benefit liability turns negative (giving rise to net assets).

As per AS 15 the enterprise, in such a situation, should measure the resulting asset **at the lower of:**

- (i) the amount so determined, i.e. ₹ 10 lakh; and
- (ii) the present value of available future refunds from the plan i.e. ₹ 6 lakh. Therefore, defined benefit asset will be recognised at ₹ 6 lakhs.

QUESTION 146: (Q.AS15.SM.202 CA FINAL)

Mr. Rajan is working for Infotech Ltd. Consider the following particulars:

Annual salary of Mr. Rajan = ₹ 30,00,000

Total working days in 20X0-X1 = 300 days

Leaves allowed in 20X0-X1 as per company policy = 10 days

Leaves utilized by Mr. Rajan in 20X0-X1 = 8 days

The unutilized leaves are settled by way of payment and accordingly, carry forward of such leaves to the subsequent period is not allowed.

Compute the total employee benefit expense for Infotech Ltd. in respect of 20X0-X1.

SOLUTION

Mr Rajan is entitled to a salary of ₹ 30,00,000 for 300 total working days.

Thus, per day salary works out to ₹ 30,00,000 ÷ 300 days = Rs. 10,000 per day

In the year 20X0-20X1, Mr. Rajan availed 8 out of 10 leaves allowed by the company.

Accordingly, leaves unutilized = 10 – 8 = 2 days

In line with the company policy, Infotech Ltd. will pay Mr. Rajan for the unutilized leave.

Thus, total expense for 20X0-20X1 = ₹ 30,00,000 + (2 days unutilized leaves x ₹ 10,000 per day)
= ₹ 30,20,000.

QUESTION 147: Q.AS15.OM.108: (CA FINAL)

Balance of Present Value of Defined Benefit Obligations 15,00,000

Balance of Plan Assets 10,00,000

Actuary Report Specifies:

Current Service Costs 3,00,000

Interest Cost 20,000

Contributions to Plan Assets at the Mid of Year 1,50,000

Benefit Paid at the mid of year 2,40,000

Expected Return 12% p.a.

Closing Value of Present Value of Defined Benefit Obligations 17,00,000

Closing Value of Plan Assets at Fair Value 10,20,000

Journalise, Prepare ledgers and Extracts of Balance sheet and Profit and Loss account along with disclosures.

SOLUTION

DOB Payable a/c			
To Bank (Benefits)	2,40,000	By Opening Balance	15,00,000
		By Current Service Cost	30,00,000
		By Interest Cost	20,000
By Closing Balance	17,00,000	By Actuarial Loss (b/f)	1,20,000
Plan Asset			
To Opening Balance	10,00,000	By Bank A/c	2,40,000
To Bank	1,50,000	By Acturrial Loss B/F	
To Expected Return	1,14,753		
(a) 1,20,000			
(b) 5,247		By Closing Balance	10,20,000

25. ACCOUNTING STANDARD - 17

SEGMENT REPORTING

QUESTION 148: (MTP MAY'25)

Whether interest expense relating to overdrafts and other operating liabilities identified to a particular segment should be included in the segment expense or not?

In case interest is included as a part of the cost of inventories where it is so required as per AS 16, read with AS 2 and those inventories are part of segment assets of a particular segment, state whether such interest would be considered as a segment expense.

SOLUTION:

The interest expense relating to overdrafts and other operating liabilities identified to a particular segment should not be included as a part of the segment expense unless the operations of the segment are primarily of a financial nature or unless the interest is included as a part of the cost of inventories.

In case interest is included as part of the cost of inventories where it is so required as per AS 16 "Borrowing Costs", read with AS 2 "Valuation of Inventories", and those inventories are part of segment assets of a particular segment, such interest should be considered as a segment expense. In this case, the amount of such interest and the fact that the segment result has been arrived at after considering such interest should be disclosed by way of a note to the segment result.

QUESTION 149: (Q.AS17.RMP.104 RTP May20, Exam Jan21)

The Chief Accountant of Cotton Garments Limited gives the following data regarding its five segments:

(Rs in Crore)

Particulars	A	B	C	D	E	Total
Segment Assets	40	15	10	10	5	80
Segment Results	(95)	5	5	(5)	15	(75)
Segment Revenue	310	40	30	40	30	450

The Chief Accountant is of the opinion that segment "A" alone should be reported. Is he justified in his view? Examine his opinion in the light of provisions of AS 17 'Segment Reporting'.

SOLUTION

As per AS 17 'Segment Reporting', a business segment or geographical segment should be identified as a reportable segment if:

- (i) Its **revenue** from sales to external customers and from other transactions with other segments is 10% or more of the total revenue- external and internal of all segments; or
- (ii) Its segment **result** whether profit or loss is 10% or more of:
 - (1) The combined result of all segments in profit; or
 - (2) The combined result of all segments in loss,
 Whichever is greater in absolute amount; or
- (iii) Its segment **assets** are 10% or more of the total assets of all segments.

Further, if the total external revenue attributable to reportable segments constitutes less than 75% of total enterprise revenue, additional segments should be identified as reportable segments even if they do not meet the 10% thresholds until at least 75% of total enterprise revenue is included in reportable segments.

Accordingly,

- (a) On the basis of **revenue from sales** criteria, segment A is a reportable segment.
 (b) On the basis of the **result** criteria, segments A & E are reportable segments (since their results in absolute amount is 10% or more of Rs 100 crore).
 (c) On the basis of **asset** criteria, all segments except E are reportable segments.

Since all the segments are covered in atleast one of the above criteria, all segments have to be reported upon in accordance with AS 17.

Hence, the opinion of chief accountant that only segment 'A' is reportable is wrong.

QUESTION 150: (Q.AS17.SM.303)

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	<u>6,135</u>
	<u>10,800</u>
Bright Bar Division	
Sales to Fitting Division	45
Export Sales to Rwanda	<u>300</u>
	<u>345</u>
Fitting Division	
Export Sales to Maldives	<u>270</u>

Particulars	Head Office Rs.(‘000)	Forging Shop Division Rs. (‘000)	Bright Bar Division Rs. (‘000)	Fitting Division 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

SOLUTION

Diversifiers Ltd. Segmental Report

(Rs. '000)

Particulars	Divisions			Inter Segment Eliminatio ns	Consolidated Total
	Forging shop	Bright Bar	Fitting		
Segment Revenue Sales:					
Domestic	90	-	-	-	90

CA Intermediate**Advanced Accounts**

Export	<u>6,135</u>	<u>300</u>	<u>270</u>	-	<u>6,705</u>
External Sales	<u>6,225</u>	<u>300</u>	<u>270</u>	-	<u>6,795</u>
Inter-Segment Sales	<u>4,575</u>	<u>45</u>	-	<u>4,620</u>	-
Total Revenue	<u>10,800</u>	<u>345</u>	<u>270</u>	<u>4,620</u>	<u>6,795</u>
Segment Result (Given)	240	30	(12)		258
Head Office Expenses					<u>(144)</u>
Operating Profit					114
Interest Expense					<u>(16)</u>
Profit Before Tax					<u>98</u>
Information in Relation to Assets and Liabilities:					
Fixed Assets	300	60	180	-	540
Net Current Assets	<u>180</u>	<u>60</u>	<u>135</u>	-	<u>375</u>
Segment assets	<u>480</u>	<u>120</u>	<u>315</u>	-	915
Unallocated Corporate Assets (75 + 72)	-	-	-	-	<u>147</u>
Total assets					<u>1,062</u>
Segment liabilities	30	15	180	-	225
Unallocated corporate liabilities					<u>57</u>
Total liabilities					<u>282</u>

Sales Revenue by Geographical Market

	Home Sales	Export Sales (by forging shop division)	Export to Rwanda	Export to Maldives	(Rs. '000) Consolidated Total
External sales	90	6,135	300	270	6,795

26. ACCOUNTING STANDARD - 18

RELATED PARTY DISCLOSURES

QUESTION 151: (RTP JAN'26)

Mr. Rajiv KMP of Rajjada Limited received a cheque of ₹ 70,000 towards reimbursement of expenses incurred on stay in hotel, conference expenses etc. visiting some meeting on behalf of the company. You are required to guide whether the above transaction is covered under AS-18?

SOLUTION

As per AS 18 'Related Party Disclosures', enterprises over which KMP & its relatives are able to exercise significant influence are related party transactions (Clause D).

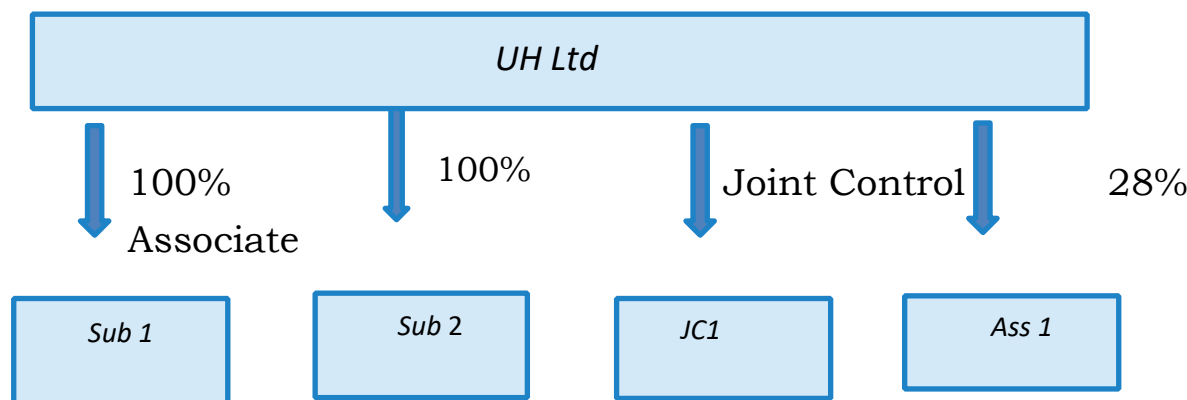
Thus, as per the facts of the case & provisions of AS, KMP is RP of the company.

But, reimbursement is not in the nature of remuneration. Hence, not to be disclosed in Financial Reporting.

QUESTION 152 (Q.AS18.SM.108)

Consider the following organization structure related to UH Ltd. (the ultimate parent company of a Group), wherein UH Ltd. has made the following investments:

- Investment in two of the wholly owned subsidiaries, viz. Sub 1 and Sub 2
- Investment in JC 1, in which UH Ltd. has a joint control
- 20% investment in Ass 1 (and hence, Ass 1 is an associate of UH Ltd.)



Given the above structure: Identify related party relationships for each of the above entities under AS-18

SOLUTION:

The following table identifies the related party relationships for each of the entities in the Group:

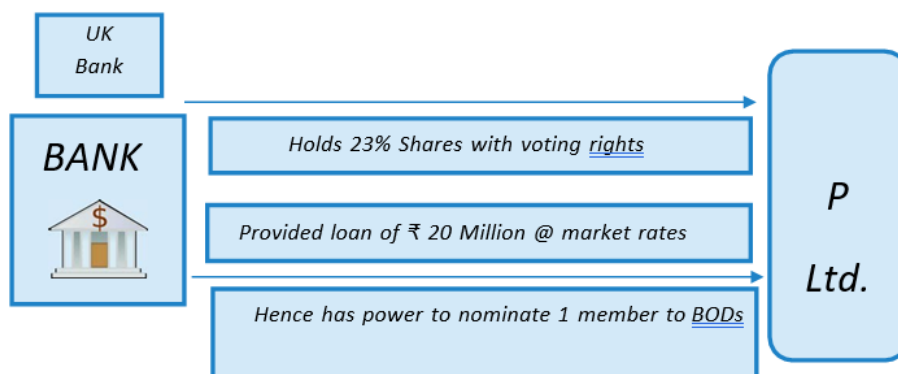
Reporting enterprise	Related Party as per AS-18
UH Ltd.	All the four entities (viz. Sub 1, Sub 2, JC 1 and Ass 1)
Sub 1	Only two of the entities in the Group (viz. UH Ltd. and Sub 2)
Sub 2	Only two of the entities in the Group (viz. UH Ltd. and Sub 1)

JC 1	Only UH Ltd.
Ass 1	Only UH Ltd.

QUESTION 153 (Q.AS18.SM.111)

Consider a scenario wherein:

- UK Bank holds 23% equity shares with voting rights in P Ltd.
- The bank has provided a loan of Rs. 20 million to P Ltd. at market interest rate
- As per the terms and conditions of the loan agreement, the bank has appointed one person as its nominee to the board of directors of P Ltd. and any major transaction to be entered into by P Ltd. will require the consent of the Bank



Determine: Whether under AS-18 - UK Bank is a related party to P Ltd. (the reporting enterprise)?

SOLUTION

In the instant case, the UK Bank holds 23% shares with voting rights in P Ltd. and hence **is deemed to exercise significant influence** over P Ltd.

The bank is also a provider of finance to P Ltd. (the reporting enterprise) and as per AS-18, parties **like providers of finance are deemed not to be considered** as a related party in the course of normal dealings with an enterprise by virtue **only of those dealings**.

However, **this exemption will not be available** to UK Bank in this case – since it exercises significant influence over P Ltd. (by virtue of holding 23% shares with voting rights in P Ltd.)

Accordingly, for P Ltd. (the reporting enterprise), the UK Bank is a related party and it will be required to disclose the transactions with UK Bank in its financial statements.

QUESTION 154 (Q.AS18.RMP.201: (RTP – May'24, Nov'22, Nov'19, May'19 & May'25 and Exam July'21))

SP hotels Limited enters into an agreement with Mr. A for running its hotel for a fixed return payable to the later every year. The contract involves the day-to-day management of the hotel, while all financial and operating policy decisions are taken by the Board of Directors of the company. Mr. A does not own any voting power in SP Hotels Limited. Would he be considered as a related party of SP Hotels Limited?

SOLUTION:

Mr. A will not be considered as a related party of SP Hotels Limited in view of paragraph 3(c) of AS 18 which states, “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”.

In the above case, in the absence of share ownership, Mr. A would not be considered to exercise significant influence on SP Hotels Limited, **even though there is an agreement giving him the power to manage the company**. Further, the fact that **Mr. A does not have the ability to direct or instruct the board of directors does not qualify him as a key management personnel**.

Question 155 (Q.AS18.RMP.207: (RTP Jan'25))

Will transactions with related parties, for services provided/received free of cost, be required to be disclosed?

A Limited has a corporate communications department, which centralises the public relations function for the whole group of A Limited and its subsidiaries. No charges are, however, levied by A Limited on its subsidiaries and accordingly, these transactions are not given accounting recognition. Would these constitute related party transactions requiring disclosure under AS 18 in the standalone financial statements of A Limited?

SOLUTION:

These transactions would require disclosure under AS 18 in the standalone financial statements of A Limited. As per paragraph 10 of AS 18, a related party transaction is “a transfer of resources or obligations between related parties, regardless of whether or not a price is charged”. In the given situation, there is a transfer of resources from A Limited to its subsidiaries, though no price is charged for the same. Hence, it will constitute as related party transaction and will require disclosure in the financial statements of A Ltd.

27. ACCOUNTING STANDARD - 20

EARNINGS PER SHARE

QUESTION 156: (RTP JAN'26)

Should appropriation to mandatory reserves be excluded from net profit attributable to equity shareholders? AB Limited is a company engaged in manufacturing industrial packaging equipment. As per the terms of an agreement entered into with its debenture holders, the company is required to appropriate adequate portion of its profits to a specific reserve over the period of maturity of the debentures such that, at the redemption date, the reserve constitutes at least half the value of such debentures. As such appropriations are not available for distribution to the equity shareholders, AB limited has excluded this from the numerator in the computation of Basic EPS. Is this treatment correct?

ANSWER:

The appropriation made to such a mandatory reserve created for the redemption of debentures would be included in the net profit attributable to equity shareholders for the computation of Basic EPS

Paragraph 11 of the Statement states that "For the purpose of calculating basic earnings per share, the net profit or loss for the period attributable to equity shareholders should be the net profit or loss for the period after deducting preference dividends and any attributable tax thereto for the period" With an emphasis on the phrase attributable to equity shareholders, it may be construed that such amounts appropriated to mandatory reserves, though not available for distribution as dividend, **are still attributable to equity shareholders**. Accordingly, these amounts should be included in the computation of Basic EPS. **In view of this, the treatment made by the company is not correct.**

Question 157 (Q.AS20.RMP.101: (RTP May 2021))

In the following list of shares issued, for the purpose of calculation of weighted average number of shares, from which date, weight is to be considered:

- (i) Equity Shares issued in exchange of cash,
- (ii) Equity Shares issued as a result of conversion of a debt instrument,
- (iii) Equity Shares issued in exchange for the settlement of a liability of the enterprise,
- (iv) Equity Shares issued for rendering of services to the enterprise,
- (v) Equity Shares issued in lieu of interest and/or principal of another financial instrument,
- (vi) Equity Shares issued as consideration for the acquisition of an asset other than in cash.

ANSWER:

The following dates should be considered for consideration of weights for the purpose of calculation of weighted average number of shares in the given situations:

- (i) Date of Cash receivable
- (ii) Date of conversion
- (iii) Date on which settlement becomes effective
- (iv) When the services are rendered
- (v) Date when interest ceases to accrue.
- (vi) Date when Asset is Recorded.

Question 158 (Q.AS20.SM.203: (Also in RTP May 22))

NAT, a listed entity, as on 1st April, 2021 had the following capital structure:

	Rs.
10,00,000 Equity Shares having face value of Rs. 1 each	10,00,000
10,00,000 8% Preference Shares having face value of Rs. 10 each	1,00,00,000

During the year 2021-2022, the company had profit after tax of Rs. 90,00,000

On 1st January, 2022, NAT made a bonus issue of one equity share for every 2 equity shares outstanding as at 31st December, 2021.

On 1st January, 2022, NAT issued 2,00,000 equity shares of Rs. 1 each at their full market price of Rs. 7.60 per share.

NAT's shares were trading at Rs. 8.05 per share on 31st March, 2022.

Further it has been provided that the basic earnings per share for the year ended 31st March, 2021 was previously reported at Rs. 62.30.

You are required to:

- Calculate the basic earnings per share to be reported in the financial statements of NAT for the year ended 31st March, 2022 including the comparative figure, in accordance with AS-20 Earnings Per Share.
- Explain why the bonus issue of shares and the shares issue at full market price are treated differently in the calculation of the basic earnings per share?

SOLUTION

- Calculation of Basic Earnings per share for the year ended 31st March, 2022 including the comparative figure:

- Earnings for the year ended 31st March, 2021 = EPS x Number of shares outstanding during 2020-2021

$$= \text{Rs. } 62.30 \times 10,00,000 \text{ equity shares}$$

$$= \text{Rs. } 6,23,00,000$$

- Adjusted Earnings per share after taking into consideration bonus issue

Adjusted Basic EPS = Earnings for the year 2020-2021 / Total outstanding shares + Bonus issue

$$= \text{Rs. } 6,23,00,000 / (10,00,000 + 5,00,000)$$

$$= \text{Rs. } 6,23,00,000 / 15,00,000$$

$$= \text{Rs. } 41.53 \text{ per share}$$

- Basic EPS for the year 2021-2022

Basic EPS = Total Earnings – Preference Shares Dividend / (Total shares outstanding at the beginning + Bonus issue + weighted average of the shares issued in January, 2022)

$$= (\text{Rs. } 90,00,000 - \text{Rs. } (1,00,00,000 \times 8\%) / (10,00,000 + 5,00,000 + (2,00,000 \times 3/12))$$

$$= \text{Rs. } 82,00,000 / 15,50,000 \text{ shares}$$

$$= \text{Rs. } 5.29 \text{ per share}$$

- In case of a bonus issue, 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. Since the bonus issue is an issue without consideration, the issue is treated as if it had occurred prior to the beginning of the year 2021, the earliest period reported.

However, the share issued at full market price does not carry any bonus element and usually

results in a proportionate change in the resources available to the enterprise. Therefore, it is taken into consideration from the time it has been issued i.e., the time-weighting factor is considered based on the specific shares outstanding as a proportion of the total number of days in the period

Question 159 (Q.AS20.SM.405: (Jan'25 Exam))

XYZ Limited has provided you the following information as on 31st March, 2024:

Particular	₹
Net profit (After Tax)	₹ 31,20,000
No. of shares outstanding as on 31-3-2024 of ₹ 10 each	8,00,000
Average fair value of one equity share during the year 2023-24	₹ 25
Weighted average no. of shares under option during the year 2023-24	80,000
Exercise price for shares under option during the year 2023-24	₹ 20
12% Debentures of ₹ 100 each	₹ 30,00,000
(Each debenture is convertible into 4 equity shares)	
Tax rate	30%

The company issued one equity share as bonus for every 5 equity shares outstanding as on 1st October, 2023. It further issued 2,00,000 equity shares of ₹ 10 each as on 1st January, 2024. Financial year of the company ends on 31st March each year.

You are required to calculate Basic and Diluted earnings per share as on 31st March, 2024 (round off your answer to 2 decimal places)

SOLUTION

Computation of Basic Earnings per Share

	Earnings ₹	No. of Shares	EPS ₹
Earnings per share for the year 2023- 2024	31,20,000	6,50,000 (W.N 2)	4.80

Computation of Dilutive Earnings per Share			
	Earnings ₹	Shares	EPS ₹
Net profit for the year	31,20,000		
Weighted average number of shares (W.N. 2) outstanding during year on 31.3.2024 (i)		6,50,000	
Number of shares under option		80,000	
Number of shares that would have been issued at fair value: $(80,000 \times 20.00)/25.00$		(64,000)	
No. of incremental shares issued for no consideration (ii)		16,000	
Diluted earnings per share after options	31,20,000	6,66,000 (i + ii)	4.68

12% Convertible Debentures (W.N. 3)	2,52,000	1,20,000	-
Diluted earnings	<u>33,72,000</u>	<u>7,86,000</u>	4.29

Working notes:**1. Computation of shares issued on bonus**

No. of shares outstanding as on 31 st March 2024	8,00,000
Less: Shares issued on 1 st Jan 2024	<u>(2,00,000)</u>
Outstanding shares as on 31 st December 2023	<u>6,00,000</u>
Bonus shares (6,00,000 x 1/(1+5))	1,00,000
Outstanding shares before bonus issue as on 1 st April 2023 (6,00,000x5/6)	5,00,000

2. Weighted Average number of Equity shares

	Shares	Months	Weighted average
Opening balance as on 1.4.2023	5,00,000(W.N.1)	12/12	5,00,000
Bonus	1,00,000	12/12	1,00,000
Further issue of shares on 1.1.2024	2,00,000	3/12	<u>50,000</u>
			<u>6,50,000</u>

3. 12% Convertible Debentures

Increase in net profit {₹ 30,00,000 x 0.12 x (1 - 0.30)}	₹ 2,52,000
No. of incremental shares {30,000 x 4}	1,20,000

Question 160 (Q.AS20.SM.502: (RTP Jan'25))

XYZ Limited has a wholly owned subsidiary BC Limited. The Group prepares consolidated Financial Statements for the year ended 31st March, 2024. XYZ Limited (in its separate financial statements) has incurred a loss of ₹ 2 crore during the year, while the consolidated profit for the group during the year is ₹ 40 lakh.

XYZ Limited has 5,00,000 shares outstanding as at 31st March, 2024. Further, it has granted options to issue equity shares as at that date. In respect of such options, 1,00,000 shares are considered to be the shares issued for no consideration. There are no changes in income or expenses that are expected from the issue of equity shares on exercise of these options.

Calculate Basic and Diluted EPS for XYZ Limited for separate financial statements and for the Group.

SOLUTION

Computation of earnings per share

Particulars	Consolidated financial statements	Standalone financial statements of XYZ Limited
-------------	-----------------------------------	--

Basic earnings/(loss) per share	₹ 8 [40,00,000/5,00,000]	(₹ 40) [2,00,00,000/5,00,000]
Diluted earnings/ (loss) per share	₹ 6.66	[40,00,000/ 6,00,000]

As per paragraph 39 of AS 20 "Potential equity shares should be treated as dilutive when, and only when, their conversion to equity shares would decrease net profit per share from continuing ordinary operations.

In the above case, if the exercise of options was considered for separate financial statements of XYZ Limited, the diluted loss per share would have reduced to ₹ 33.33 [2,00,00,000/6,00,000]. As this is antidilutive, the options would not be treated as potentially dilutive equity shares. Accordingly, in the separate financial statements of XYZ Limited, the Diluted EPS would be same as Basic EPS.

Question 161 (EXAMPLE 7 (Bonus))

Previous Year EAESH = 12,00,000

Current Year EAESH = 15,00,000

Current Year Outstanding no. in Beginning = 2,00,000 no.

Current Year Bonus issue in 1/7 = 50,000 no.

Current Year Public Issue in 1/9 = 30,000 no.

Current Year Buy Back in 1/11 = 10,000 no.

Calculate EPS of Current Year & Restated Eps of Previous year.

SOLUTION

Working Note 1: Calculation of weighted Average Outstanding no.

1/4	2,00,000 x 12/12	2,00,000
+ 1/7 Bonus	50,000 x 12/12	50,000
+ 1/9 Public issue	30,000 x 7/12	17,500
- 1/11 Buy Back	(10,000 x 5/12)	(4,167)
		2,63,333

Current Year Eps = 15,00,000/2,63,333 = 5.696/-

Restated Eps of Previous Year = 12,00,000/2,00,000+50,000 = 4.8/-

Question 162 (EXAMPLE 11 - Partly Paid Shares)

As on 1/4/23	Opening Outstanding Equity Shares 50,000 of 10/- each, 6/- Paid-up.
On 1/9/23	Public Issue of 30,000 shares made at 10/- each, 7/- Paid up
On 1/10/23	Amount Called @4/- on Opening but Shareholders holding 48,000 Shares have paid.
On 1/12/23	Amount Called @3/- on public issue, all Share Holders have paid.

Note: Partly paid shares are also entitled for Dividend

Calculate Weighted Average Outstanding Equity Shares.

Solution:

Calculation of Weighted Average Outstanding Share Capital (in ₹)

Date	Particulars	Working	Weighted Avg. Amount
1/4/23	Opening Balance	50,000 x 6 x 12/12	3,00,000
1/9/23	Public issue	30,000 x 7 x 6/12	1,22,500

1/10/23	Called @4/-	4,80,000 x 4 x 6/12	96,000
1/12/23	Called @3/-	30,000 x 3 x 4/12	30,000
Weighted Average Outstanding Share Capital			5,48,500
Weighted Avg Outstanding No. of Shares (5,48,500/10)			54,850 No.

Question 163 (EXAMPLE 13 (Right Issue))

EAESH = 21,00,000

As on 1/4	Outstanding Shares are 1,50,000 No.
On 1/7	Public Issue of 30,000 No.
On 1/10	Right issue @90/- at ratio of 1:2
On 1/1	Public issue of 50,000 No.

Cum-Right Price = 100/-

Solution:**Step 1:**Ex-Right Price = $(1,50,000 + 30,000) \times 100 + (90,000 \times 90) / 2,70,000 = 96.67/-$ **Step 2:**Right Factor = Cum-Right Price / Ex-Right Price = $100/96.67$ **Step 3:****Weighted Average: - Apply Right Factor only on No. of Shares Outstanding before Right Issue**

Date	Working	Weighted Avg. Amount
1/4	$1,50,000 \times 3/12 \times 100/96.67$	38,792
1/7	$1,80,000 \times 3/12 \times 100/96.67$	46,550
1/10	$2,70,000 \times 3/12$	67,500
1/1	$3,20,000 \times 3/12$	80,000
		2,32,842

BEPS = $21,00,000 / 2,32,842 = 9.02/-$ per Share.

28. ACCOUNTING STANDARD - 22

ACCOUNTING FOR TAXES ON INCOME

QUESTION 164: (EXAM SEP'25)

Amber Limited purchases a building at a cost of ₹ 20,00,000 on 1st April 2021 its useful life is four years and an expected scrap value is zero. Depreciation is allowed @ 50% in 1st year and rest balance in 2nd year for Tax purpose. Straight-line method is considered for accounting purpose. Amber Limited profit before depreciation and taxes are as follow:

Year	Profit (in ₹)
2021-2022	18,00,000
2022-2023	22,00,000
2023-2024	25,00,000
2024-2025	30,00,000

The corporate tax rate is 30% in all 4 years.

You are required to calculate Current Tax, Deferred Tax Assets/Liability and Tax Expense for each year.

SOLUTION

- (a) As per AS 22 “Accounting for Taxes on Income”, computation of Current Tax, Deferred Tax Liability (DTL), and Total Tax Expense of Amber Limited is as under:

	21-22 (₹)	22-23 (₹)	23-24 (₹)	24-25 (₹)
Profit before depreciation and taxes	18,00,000	22,00,000	25,00,000	30,00,000
Less: Depreciation for accounting purposes	5,00,000	5,00,000	5,00,000	5,00,000
Profit before Taxes (i)	13,00,000	17,00,000	20,00,000	25,00,000
Less: Tax Expenses				
(a) Current tax for the year	2,40,000	3,60,000	7,50,000	9,00,000
(b) Deferred Tax Liability/Asset (b)	1,50,000	1,50,000	(1,50,000)	(1,50,000)
Tax expense (a+b) (ii)	3,90,000	5,10,000	6,00,000	7,50,000
Profit after tax (i) – (ii)	9,10,000	11,90,000	14,00,000	17,50,000

Working notes:

1. Calculation of current tax at 30%

Year	Taxable Income	Current Tax (₹)
2021-22	8,00,000 (18,00,000-10,00,000)	2,40,000
2022-23	12,00,000 (22,00,000-10,00,000)	3,60,000

2023-24	25,00,000	7,50,000
2024-25	30,00,000	9,00,000

2. Calculation of Timing Difference and Deferred Tax Assets/Liability

Year	Timing Difference (Tax Depreciation- Accounting Depreciation)	DTL/(DTA) Deferred Tax = Timing Difference × 30%
2021-22	10,00,000 – 5,00,000 = 5,00,000	1,50,000
2022-23	10,00,000 – 5,00,000 = 5,00,000	1,50,000
2023-24	0 – 5,00,000 = (5,00,000)	(1,50,000)
2024-25	0 – 5,00,000 = (5,00,000)	(1,50,000)

QUESTION 165: (Q.AS22.OM.202) (CA Final)

From the following information given below you are required to compute Deferred Tax Assets and Deferred Tax Liability for Ramanujam Ltd. as on 31st March, 20X1. The tax applicable is 35%.

1. The company has charged Rs. 7,42,900 in the books of accounts while as per Income Tax Computation, the depreciation available for the company is Rs. 8,65,400.
2. The Company has made provision for doubtful debts for Rs. 54,300 during the year.
3. The company has debited share issue expenses of Rs. 6,23,500 which will be available for deduction under the income tax Act from the next year.
4. The expenses of Rs. 7,84,500 has been charged to profit and loss account which are disallowed under the income tax act.
5. The company has made donation of Rs. 2,00,000 which has been debited to Profit and loss account and only 50% thereof will be allowed as deduction as per Income Tax law.

SOLUTION:

Timing Difference Amount	DTA/DTL	Remarks
122500 Liability	42875 DTL	-
54300 Assets	19005 DTA	
623500 Assets	218225 DTA	
-	-	Permanent Difference
-	-	Permanent Difference of Rs. 100000
	194355	Net DTA

QUESTION 166: (Q.AS22.RMP.203) (Exam July21)

The following particulars are stated in the Balance Sheet of Deep Limited as on 31st March, 2020:

	(Rs. In Lakhs)
Deferred Tax Liability (Cr.)	28.00
Deferred Tax Assets (Dr.)	14.00

The following transactions were reported during the year 2020 -2021:

- i. Depreciation as per books was Rs. 70 Lakhs whereas Depreciation for Tax purposes was Rs. 42 Lakhs. There were no additions to Fixed Assets during the year.
- ii. Expenses disallowed in 2019-20 and allowed for tax purposes in 2020-21 were Rs. 14 Lakhs.
- iii. Share issue expenses allowed under section 35(D) of the Income Tax Act, 1961 for the year 2020-21 (1/10th of Rs. 70.00 lakhs incurred in 2019-20).
- iv. Repairs to Plant and Machinery were made during the year for Rs. 140.00 Lakhs and was spread over the period 2020-21 and 2021-22 equally in the books. However, the entire expenditure was allowed for income-tax purposes in the year 2020-21.

Tax Rate to be taken at 40%.

You are required to show the impact of above items on Deferred Tax Assets and Deferred Tax Liability as on 31st March, 2021.

SOLUTION

Impact of various items in terms of deferred tax liability/deferred tax asset on 31.3.21

Transactions	Analysis	Nature of difference	Effect	Amount (Rs.)
Difference in depreciation	Generally, written down value method of depreciation is adopted under IT Act which leads to higher depreciation in earlier years of useful life of the asset in comparison to later years.	Responding timing difference	Reversal of DTL	28 lakhs · 40% = Rs. 11.20 lakhs
Disallowances, as per IT Act, of earlier years	Tax payable for the earlier year was higher on this account.	Responding timing difference	Reversal of DTA	14 lakhs · 40% = 5.6 lakhs
Share issue expenses	Due to disallowance of full expenditure under IT Act, tax payable in the earlier years was higher.	Responding timing difference	Reversal of DTA	7 lakhs · 40% = Rs. 2.8 lakhs
Repairs to plant and machinery	Due to allowance of full expenditure under IT Act, tax payable of the current year will be less.	Originating timing difference	Increase in DTL	70 lakhs · 40% = 28 lakhs

QUESTION 167: (Q.AS22.RMP.206) (RTP – May21 & EXAM Nov22)

(a) The following information is furnished in respect of Slate Ltd. for the year ending 31-3-2019:

- | | |
|------------------------------|--------------|
| i) Depreciation as per books | Rs. 2,80,000 |
| Depreciation for tax purpose | Rs. 1,90,000 |

The above depreciation does not include depreciation on new additions.

- ii) A new machinery purchased on 1.4.18 costing Rs. 1,20,000 on which 100% depreciation is allowed in the 1st year for tax purpose whereas Straight-line method is considered appropriate for accounting purpose with a life estimation of 4 years.
- iii) The company has made a profit of Rs. 6,40,000 before depreciation and taxes.
- iv) Corporate tax rate of 40%.

Prepare relevant extract of statement of Profit and Loss for the year ending 31-3-2019 and also show the effect of above items on deferred tax liability/asset as per AS 22.

- (b) What are the disclosure requirements for deferred tax assets and deferred tax liabilities in the balance sheet as per AS 22?

ANSWER:**(a)** Statement of Profit and Loss for the year ended 31st March, 2019 (Extract)

		Rs.
Profit before depreciation and taxes		6,40,000
Less: Depreciation for accounting purposes (2,80,000 + 30,000)		(3,10,000)
Profit before taxes (A)		3,30,000
Less: Tax expense (B)		
Current tax (W.N.1) (3,30,000 x 40%)	1,32,000	
Deferred tax (W.N.2)	NIL	(1,32,000)
Profit after tax (A-B)		1,98,000

Working Notes:**1.** Computation of taxable income

	Amount (Rs.)
Profit before depreciation and tax	6,40,000
Less: Depreciation for tax purpose (1,90,000 + 1,20,000)	(3,10,000)
Taxable income	3,30,000
Tax on taxable income @ 40%	1,32,000

2. Impact of various items in terms of deferred tax liability / deferred tax asset

S. No.	Transactions	Analysis	Nature of difference	Effect	Amount (Rs.)
(i)	Difference in depreciation	Generally, written down value method of depreciation is adopted under IT Act which leads to higher depreciation in earlier years of useful life of the asset in comparison to later years.	Responding timing difference	Reversal of DTL	(2,80,000 - 1,90,000) x 40% = (36,000) (1,20,000 - 30,000) x 40% = 36,000
(ii)	Depreciation on new Machinery Net impact	Due to allowance of full amount as expenditure under IT Act, tax payable in the earlier years is less.	Timing difference	Creation of DTL	NIL

(b) 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.

QUESTION 168: (Q.AS22.SM.208) (RTP Jan'25)

ABC Ltd. prepares its accounts annually on 31st March. On 1st April, 2022, it purchases a machine at a cost of ₹ 1,50,000. The machine has a useful life of three years and an expected scrap value of zero. Although it is eligible for a 100% first year depreciation allowance for tax purposes, the straight line method is considered appropriate for accounting purposes. ABC Ltd. has profits before depreciation and taxes of ₹ 2,00,000 each year and corporate tax rate is 40 percent each year.

The purchase of machine at a cost of ₹ 1,50,000 in 2022 gives rise to a tax saving of ₹ 60,000. The corporate tax rate has been assumed to be same in each of the three years. Calculate deferred tax and pass necessary journal entries.

What will be the amount of deferred tax, if the substantively enacted tax rates for 2022, 2023 and 2024 are 40%, 35% and 38% respectively.

SOLUTION

If the cost of machine is spread over three years of its life for accounting purposes, the amount of the tax saving should also be spread over the same period as shown below:

Statement of Profit and Loss
(for the three years ending 31st March, 2022, 2023, 2024)

		(₹ in thousand)		
		2022	2023	2024
	Profit before depreciation and taxes	200	200	200
Less:	Depreciation for accounting purposes	50	50	50
	Profit before taxes	150	150	150
Less:	Tax expense			
	Current tax:			
	0.40 x (200 - 150)	20		
	0.40 x 200		80	80
	Deferred tax:			
	Tax effect of timing differences originating during the year leading to DTL			
	0.40 (150-50)	40		
	Tax effect of timing differences reversing during the year			
	0.40 (0-50)	-	(20)	(20)
	Tax expense	60	60	60
	Profit after tax	90	90	90
	Net timing differences	100	50	0
	Deferred tax liability balance	40	20	0

In 2022, the amount of depreciation allowed for tax purposes exceeds the amount of depreciation charged for accounting purpose by ₹ 1,00,000 and, therefore, taxable income is lower than the accounting income. This gives rise to a deferred tax liability of ₹ 40,000. In 2023 and 2024 accounting income is lower than taxable income because the amount of depreciation charged for accounting purposes exceeds the amount of depreciation allowed for tax purposes by ₹ 50,000 each year. Accordingly, deferred tax liability is reduced by ₹ 20,000 each in both the years. As may be seen, tax expense is based on the accounting income of each period.

In 2022, the profit and loss account is debited and deferred tax liability account is credited with the amount of tax on the originating timing difference of ₹ 1,00,000 while in each of the following two years, deferred tax liability account is debited and profit and loss account is credited with the amount of tax on the reversing timing difference of ₹ 50,000.

The following Journal entries will be passed:

Year 2022			
Profit and Loss A/c To Current tax A/c (Being the amount of taxes payable for the year 2022 provided for)	Dr.	20,000	20,000
Profit and Loss A/c To Deferred tax liability A/c (Being the deferred tax liability created for originating timing difference of ₹ 1,00,000)	Dr.	40,000	40,000
Year 2023			
Profit and Loss A/c To Current tax A/c (Being the amount of taxes payable for the year 2023 provided for)	Dr.	80,000	80,000
Deferred tax liability A/c To Profit and Loss A/c (Being the deferred tax liability adjusted for reversing timing difference of ₹ 50,000)	Dr.	20,000	20,000
Year 2024			
Profit and Loss A/c To Current tax A/c (Being the amount of taxes payable for the year 2024 provided for)	Dr.	80,000	80,000
Deferred tax liability A/c To Profit and Loss A/c (Being the deferred tax liability adjusted for reversing timing difference of ₹ 50,000)	Dr.	20,000	20,000

Presentation:

In the year 2022, the balance of deferred tax account i.e. ₹ 40,000 would be shown separately from the current tax payable for the year in terms of paragraph 30 of AS 22. In the year 2023, the balance of deferred tax liability account would be ₹ 20,000 and be shown separately from the current tax payable for the year as in year 2022. In year 2024, the balance of deferred tax liability account would be nil.

If the rate of tax changes, it would be necessary for the enterprises to adjust the amount of deferred tax liability carried forward by applying the tax rate that has been enacted or substantively enacted by the balance sheet date on accumulated timing differences at the end of the accounting year

The amount of deferred tax liability would be computed as follows:

The deferred tax liability carried forward each year would appear in the balance sheet as under:

31st March, 2022 = 0.40 (1,00,000) = ₹ 40,000

31st March, 2023 = 0.35 (50,000) = ₹ 17,500

31st March, 2024 = 0.38 (Zero) = ₹ Zero

Accordingly, the amount debited (credited) to the profit and loss account (with corresponding credit or debit to deferred tax liability) for each year would be as under:

31st March, 2022 Debit = ₹ 40,000

31st March, 2023 (Credit) = ₹ (22,500)

31st March, 2024 (Credit) = ₹ (17,500)

QUESTION 169: (Q.AS22.SM.301)

From the following details of A Ltd. for the year ended 31-03-20X1, 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.

Book Profit for MAT purpose	Rs. 3,50,000	
Accounting Income	Rs. 6,00,000	
Taxable Income	Rs.60,000	
Rate of Tax	Regular	20%
	MAT	7.5%

SOLUTION

Tax as per accounting profit	6,00,000×20%	Rs. 1,20,000
Tax as per Income-tax Profit	60,000×20%	Rs. 12,000
Tax as per MAT	3,50,000 × 7.50%	Rs. 26,250

Tax expense= Current Tax +Deferred Tax Liability

Rs. 1,20,000 = Rs.12,000 + Deferred tax Liability

Therefore, Deferred Tax liability as on 31-03-2017 = 1,20,000 – 12,000 = 1,08,000

Amount of tax to be debited in Profit and Loss account for the year 31-03-2017

Current Tax + Deferred Tax liability + Excess of MAT over current tax

= 12,000 + 1,08,000 + 14,250 (26,250 – 12,000)

= 1,34,250

QUESTION 170: (Q.AS22.SM.401)

Y Ltd. is a Full Tax Free enterprise for the first ten years of its existence and is in the second year of its operation. Depreciation timing difference resulting in a tax liability in year 1 and 2 is Rs.200 lakhs and Rs. 400 lakhs respectively. From the third year it is expected that the timing difference would reverse each year by Rs.10 lakhs. Assuming tax rate of 40%, find out the deferred tax liability at the end of the second year and any charge to the Profit and Loss account.

SOLUTION

As per AS 22, 'Accounting for Taxes on Income', 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 Income-tax 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. For

this purpose, the timing differences which originate first should be considered to reverse first. Out of Rs. 200 lakhs timing difference due to depreciation, difference amounting Rs. 80 lakhs (Rs. 10 lakhs x 8 years) will reverse in the tax holiday period and therefore, should not be recognised. However, for Rs. 120 lakhs (Rs. 200 lakhs – Rs. 80 lakhs), deferred tax liability will be recognised for Rs. 48 lakhs (40% of Rs. 120 lakhs) in first year. In the second year, the entire amount of timing difference of Rs. 400 lakhs will reverse only after tax holiday period and hence, will be recognised in full. Deferred tax liability amounting Rs. 160 lakhs (40% of Rs. 400 lakhs) will be created by charging it to profit and loss account and the total balance of deferred tax liability account at the end of second year will be Rs. 208 lakhs (48 lakhs + 160 lakhs).

QUESTION 171: (Q.AS22.SM.502)

ABC Company limited had an investment in Venture Capital amounting ₹10 Crores. Venture capital in turn had invested in the below portfolio companies (New Start-ups) on behalf of ABC Limited:

Portfolio Companies	Amount of investment (₹ in Crores)
Oscar Limited	2
Zee Limited	3
Star Limited	4
Sony Limited	1
Total	10

During the FY 2019-2020, Venture Capital had sold their investment in Star Limited and realised an amount of ₹8 Crores on sale of shares of star Limited and entire proceeds of ₹8 Crores have been transferred by Venture Capital to ABC Company Limited.

The accounts manager has received the following additional information from venture capital on 31.03.2020:

- (1) 8 Crores has been deducted from the cost of investment and carrying amount of investment as at year end is 2 Crores.
- (2) Company had to pay a capital gain tax @20% on the net sale consideration of ₹ 4 Crores.
- (3) Due to COVID-19, the remaining start-ups (i.e. Oscar Limited, Zee Limited, and Sony Limited) are not performing well and will soon wind up their operations. Venture capital is monitoring the situation and if required they will provide an impairment loss in June 2020 Quarter.

You need to suggest the accounts manager what should be the correct accounting treatment as per AS 22 “Accounting for Taxes on Income”.

SOLUTION

As company had to pay capital gain tax @20% on the net sale consideration as per income tax laws, the company has to recognise a current tax liability of 0.8 Crores computed as under:

Particulars	Amount (₹ in Crores)
Sales Consideration	8
Cost of Investment	4
Net gain on Sale	4
Tax@20%	0.8

As per AS 22, Timing differences are those 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.

Particulars	Amount (₹ in Crores)	Rationale
--------------------	-----------------------------	------------------

Taxable Income	4	As per income tax laws
Accounting Income	Nil	As the same is deducted from the cost of investment
Timing Difference	4	

As per AS 22, deferred tax assets should be recognised and carried forward only to the extent that there is a reasonable certainty that sufficient future taxable income will be available against which such deferred tax assets can be realised.

Since in current scenario, due to Covid 19 the portfolio companies are not performing well, thus the company may not have sufficient future taxable income which will reverse deferred tax assets. Therefore, the company should not recognise DTA of ₹ 0.8 Crores and company should recognise only current tax liability of ₹ 0.8 Crores.

29. ACCOUNTING STANDARD – 23

ACCOUNTING FOR INVESTMENTS IN ASSOCIATES IN CONSOLIDATED FINANCIAL STATEMENTS

QUESTION 172: (Q.AS23.SM.06)

Bright Ltd. acquired 30% of East India Ltd. shares for ₹ 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 ₹ 80,000 and declared a dividend of ₹ 50,000 on 12-08-20X1. East India reported earnings of ₹ 3,00,000 for the financial year ending on 31-03-20X2 (assume profits to accrue evenly) and declared dividends of ₹ 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?

SOLUTION

- (i) **Carrying amount of investment in Separate Financial Statement of Bright Ltd. as on 31.03.20X2**

	₹
Amount paid for investment in Associate (on 1.06.20X1)	2,00,000
Less: Pre-acquisition dividend (₹ 50,000 x 30%)	<u>(15,000)</u>
Carrying amount as on 31.3.20X2 as per AS 13	<u>1,85,000</u>

- (ii) **Carrying amount of investment in Consolidated Financial Statements of Bright Ltd. as on 31.3.20X2 as per AS 23**

	₹
Carrying amount as per separate financial statements	1,85,000
Add: Proportionate share of 10-month profit of investee as per equity method (30% of ₹ 3,00,000 x 10/12)	<u>75,000</u>
Carrying amount as on 31.3.20X2	<u>2,60,000</u>

- (iii) **Carrying amount of investment in Consolidated Financial Statement of Bright Ltd. as on 30.6.20X2 as per AS 23**

	₹
Carrying amount as on 31.3.20X2	2,60,000
Less: Dividend received (₹ 60,000 x 30%)	<u>(18,000)</u>
Carrying amount as on 30.6.20X2	<u>2,42,000</u>

QUESTION 173: (Q.AS23.SM.07)

A Ltd. acquired 25% of shares in B Ltd. as on 31.3.20X1 for ₹ 3 lakhs. The Balance Sheet of B Ltd. as on 31.3.20X1 is given below:

	₹
Share Capital	5,00,000
Reserves and Surplus	<u>5,00,000</u>
	<u>10,00,000</u>
Fixed Assets	5,00,000

Investments	2,00,000
II. Current Assets	<u>3,00,000</u>
	<u>10,00,000</u>

During the year ended 31.3.20X2 the following are the additional information available:

- 1) A Ltd. received dividend from B Ltd., for the year ended 31.3.20X1 at 40% from the Reserves.
- 2) B Ltd., made a profit after tax of ₹ 7 lakhs for the year ended 31.3.20X2.
- 3) 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?

SOLUTION

In terms of AS 23, B Ltd. will be considered as an associate company of A Ltd. as shares acquired represent to more than 20%.

(i) Calculation of Goodwill	(₹ in lakhs)
Amount paid towards acquisition of stake in B Ltd.	3.00
Less: Pre-acquisition dividend (₹ 5,00,000 x 40% x 25%)	<u>0.50</u>
Cost of Investment in B Ltd.	2.50
Less: Share in the value of Equity of B Ltd. as at the date of investment [25% of ₹ 10 lakhs (₹ 5 lakhs + ₹ 5 lakhs)]	<u>(2.50)</u>
Goodwill	<u>NIL</u>

(ii) A Ltd.

Consolidated Profit and Loss Account for the year ended 31st March, 20X2 (An extract)

		₹ in lakhs
Other income:		
Share of profits in B Ltd.		1.75
Pre-acquisition Dividend received from B Ltd.	0.50	
Transfer to investment A/c	<u>(0.50)</u>	Nil

Consolidated Balance Sheet as on 31.3.20X2 (An extract)

		₹ in lakhs
Non-current investments		
Investment in B Ltd.		
Cost of Investment in B Ltd.	2.50	
Share of profit for year 20X1 – 20X2	<u>1.75</u>	
	4.25	
Add: Goodwill	<u>NIL</u>	4.25

Working Notes:

1. Pre-acquisition dividend received from B Ltd. amounting to ₹ 0.50 lakhs will be reduced from investment value in the books of A Ltd.
2. B Ltd. made a profit of ₹ 7 lakhs for the year ended 31st March, 20X2. A Ltd.'s share in the

profits of ₹ 7 lakhs is ₹ 1.75 lakhs.

3. Investment in B Ltd. will be increased by ₹ 1.75 lakhs and consolidated profit and loss account of A Ltd. will be credited with ₹ 1.75 lakhs in the consolidated financial statement of A Ltd.
4. Dividend declared on 30th April, 20X2 will not be recognized in the consolidated financial statement of A Ltd.

QUESTION 174: (Q.AS23.RMP.10) (Exam Sep'24)

On 1st February, 2024, Best Ltd. acquired 80% Equity shares of Cool Ltd. For ₹ 14,80,000.

On 31st March, 2024, Best Ltd. also acquired 25% Equity shares of Good Ltd. For ₹ 3,80,000.

The following are the balances extracted from the books of Best Ltd., Cool Ltd., and Good Ltd. as on 31st March, 2024 :

Particulars	Best Ltd. Amount in ₹	Cool Ltd. Amount in ₹	Good Ltd. Amount in ₹
Equity Shares of ₹ 100 each fully paid	30,00,000	20,00,000	10,00,000
Securities Premium	-	2,20,000	-
9% Debentures	6,30,000	-	2,40,000
General Reserve	2,69,000	84,000	1,20,000
Profit & Loss Account (Credit Balance)	3,26,000	2,70,000	50,000
Investments	17,50,000	6,10,000	-
Property, Plant, and Equipment	18,90,000	18,14,000	12,10,000
Current Assets	9,65,000	5,60,000	2,25,000
Trade Payable (Including Bills Payable)	3,80,000	4,10,000	25,000
Sales and other income	56,00,000	38,00,000	27,00,000
Raw material consumed	36,50,000	31,20,000	22,30,000
Wages and Salaries	5,07,000	4,01,000	2,69,000
Production expenses	1,35,000	1,06,000	98,000

Additional information :

- The Profit and Loss account of Cool Ltd. showed a credit balance of ₹ 30,000 on 1st April, 2023.
- The General Reserve balance is brought forward from the previous year.
- On 31st March, 2024, all the bills payable in Cool Ltd.'s balance sheet were acceptances in favour of Best Ltd. However, on the date, Best Ltd. held only ₹ 3,00,000 of these acceptances in hand, the rest having been endorsed in favour of its creditor.
- Best Ltd. purchased goods costing ₹ 5,00,000 from Cool Ltd. on 1st June, 2023 at a price of ₹ 6,50,000. The entire goods remain unsold with Best Ltd. at the end of the financial year.
- Best Ltd. is preparing Consolidated Financial Statements for the year ending 31.03.2024.

You are required to calculate :

- (1) Trade Payable (Consolidated)
- (2) Current Assets (Consolidated)
- (3) Minority Interest
- (4) Goodwill/Capital Reserve on the acquisition of Cool Ltd.'s shares
- (5) Goodwill/Capital Reserve on the acquisition of Good Ltd.'s shares
- (6) Profit & Loss Account (Consolidated)
- (7) General Reserve (Consolidated)
- (8) Revenue from Operations (Consolidated)
- (9) Cost of material purchased/consumed (Consolidated)

SOLUTION

1. Trade payable (Consolidated)

Best limited	3,80,000
Add: Cool Ltd	4,10,000
Less: Elimination	(3,00,000)
Total	4,90,000

2. Current assets (Consolidated)

Best limited		9,65,000
Add: Cool Ltd		5,60,000
Less: Elimination of inter company owing	(3,00,000)	
Less: Unrealized stock profit	(1,50,000)	(4,50,000)
Total		10,75,000

3. Minority interest Cool Ltd

Share Capital (20,00,000 x 20%)		4,00,000
Add: Securities premium (2,20,000 x 20%)		44,000
Add: General Reserve (84,000 x 20%)		16,800
Add: Profit and loss balance	2,70,000	
Less: Adjustment of unrealised profit stock	(1,50,000)	
Balance	1,20,000	
20% of above balance		24,000
Total		4,84,800

4. Goodwill/Capital Reserve on Acquisition of Cool Ltd.:

Purchase Consideration		14,80,000
Less: Share Capital (20,00,000 x 80%)		16,00,000
Less: Securities premium (2,20,000 x 80%)		1,76,000
Less: General Reserve (84,000 x 80%)		67,200
Less: Profit and loss balance opening (30,000 x 80%)		24,000
Less: Pre acquisition profits		
(2,70,000-30,000) x 10/12 x 80%	1,60,000	
Less: Unrealised profit stock (1,50,000 x 80%)	1,20,000	40,000
Capital Reserves		4,27,200

5. Goodwill/Capital Reserve on Acquisition of Good Ltd.

Purchase Consideration	3,80,000
Less: Share Capital (10,00,000 x 25%)	2,50,000
Less: General Reserve (1,20,000 x 25%)	30,000
Less: Profit and loss balance (50,000 x 25%)	12,500
Goodwill	87,500

6. Profit and Loss Account (Consolidated)

Best limited	3,26,000
Add: Post acquisition profit of Cool Ltd	
{(2,70,000-30,000) x 2/12}80%	32,000
Total	3,58,000

7. General Reserve (Consolidated)

Best limited 2,69,000

With reference to para no 15 of AS 21

If an enterprise makes two or more investments in another enterprise at different dates and eventually obtains control of the other enterprise, the consolidated financial statements are presented only from the date on which holding-subsidiary relationship comes in existence. If two or more investments are made over a period of time, the equity of the subsidiary at the date of investment, for the purposes of paragraph 13 above, is generally determined on a step-by-step basis; however, if small investments are made over a period of time and then an investment is made that results in control, the date of the latest investment, as a practicable measure, may be considered as the date of investment.

And para no 22 of AS 21 The results of operations of a subsidiary are included in the consolidated financial statements as from the date on which parent-subsidiary relationship came in existence. The results of operations of a subsidiary with which parent- subsidiary relationship ceases to exist are included in the consolidated statement of profit and loss until the date of cessation of the relationship. The difference between the proceeds from the disposal of investment in a subsidiary and the carrying amount of its assets less liabilities as of the date of disposal is recognised in the consolidated statement of profit and loss as the profit or loss on the disposal of the investment in the subsidiary. In order to ensure the comparability of the financial statements from one accounting period to the next, supplementary information is often provided about the effect of the acquisition and disposal of subsidiaries on the financial position at the reporting date and the results for the reporting period and on the corresponding amounts for the preceding period.

8. Revenue (Consolidated) as per para no 15 and 22 of AS 21

Revenue of Best Ltd	56,00,000
Add: Revenue of Cool Ltd. (38,00,000 × 2/ 12)	6,33,333
	62,33,333

9. Cost of materials purchased/consumed (Consolidated) as per para no 15 and 22 of AS 21

Raw material of Best Ltd	36,50,000
Add: Raw material of Cool Ltd (31,20,000x 2/12)	5,20,000
	41,70,000

30. ACCOUNTING STANDARD - 24

DISCONTINUING OPERATION

QUESTION 175: (MTP MAY'25)

Arzoo Ltd. is in the business of manufacture of Passenger cars and commercial vehicles. The company is working on a strategic plan to shift from the Passenger car segment 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 plan it will reduce the production of passenger cars by 20% annually. It also plans to commence another new factory for the manufacture of commercial vehicles plus transfer of employees in a phased manner.

- (i) You are required to comment if mere gradual phasing out in itself can be considered as a 'Discontinuing Operation' within the meaning of AS 24.
- (ii) 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?
- (iii) Would your answer to the above be different if the company resolves to sell the assets of the Passenger Car Division in a phased but time bound manner?

ANSWER:

Mere gradual phasing out is not considered as discontinuing operation as defined under para 3 of AS 24, 'Discontinuing Operations'.

Examples of activities that do not necessarily satisfy criterion of the definition, but that might do so in combination with other circumstances, include:

- (1) Gradual or evolutionary phasing out of a product line or class of service;
- (2) Discontinuing, even if relatively abruptly, several products within an ongoing line of business;
- (3) Shifting of some production or marketing activities for a particular line of business from one location to another; and
- (4) Closing of a facility to achieve productivity improvements or other cost savings.

A Reportable business segment or geographical segment as defined in AS 17, would normally satisfy criteria (b) of the definition.

In view of the above the answers are:

- (i) **No**, the companies' strategic plan has no final approval from the board through a resolution and there is no specific time bound activities like shifting of assets and employees. Above all, the new segment i.e. commercial vehicle production line in a new factory has not started.
- (ii) **No**, the resolution is salient about stoppage of the Car segment in definite time period. Though, sale of some assets and some transfer proposal were passed through a resolution to the new factory, closure road map and new segment starting roadmap are missing. Hence, AS 24 will not be applicable.
- (iii) **Yes**, phased and time bound programme resolved in the board clearly indicates the closure of the passenger car segment in a definite time frame and will constitute a clear roadmap. Hence, this action will attract compliance of AS 24.

Question 176 (Q.AS22.SM.01: (RTP May18, May23 & MTP April19, Aug18)

A consumer goods producer has changed the product line as follows:

	Dish washing Bar (Per month)	Clothes washing Bar (Per month)
January 2016 - September 2016	2,00,000	2,00,000
October 2016 - December 2016	1,00,000	3,00,000
January 2017 - March 2017	Nil	4,00,000

The company has enforced a gradual enforcement of change in product line on the basis of an overall plan. The Board of Directors has passed a resolution in March 20X6 to this effect. The company follows the calendar year as its accounting year.

You required advising the company whether it should be treated as discontinuing operation or not as per AS 24?

ANSWER:

As per AS 24 'Discontinuing Operations', a discontinuing operation is a component of an enterprise:

- (i) that the enterprise, pursuant to a **single plan**, is:
 - (1) disposing of substantially in its entirety,
 - (2) disposing of piecemeal, or
 - (3) terminating through abandonment; and
- (ii) that represents a separate **major line** of business or geographical area of operations; and
- (iii) that can be distinguished operationally and for financial reporting purposes.

As per provisions of the standard, business enterprises frequently close facilities, abandon products or even product lines, and change the size of their work force in response to market forces. While those kinds of terminations generally are not, in themselves, discontinuing operations, they can occur in connection with a discontinuing operation. Examples of activities that do not necessarily satisfy criterion of discontinuing operation are gradual or evolutionary phasing out of a product line or class of service, discontinuing, even if relatively abruptly, several products within an ongoing line of business;

In the given case, the company has enforced a gradual enforcement of change in product line and does not represent a separate major line of business and hence is not a discontinued operation. If it were a discontinuing operation, the initial disclosure event is the occurrence of one of the following, whichever occurs earlier:

- (i) the enterprise has entered into a binding sale agreement for substantially all of the assets attributable to the discontinuing operation; or
- (ii) The enterprises board of directors or similar governing body has both approved a detailed, formal plan for discontinuance and made an announcement of the plan.

Question 177 (Q.AS24.SM.07)

- (i) What are the disclosure and presentation requirements of AS 24 for discontinuing operations?
- (ii) Give four examples of activities that do not necessarily satisfy criterion (a) of paragraph 3 of AS 24, but that might do so in combination with other circumstances.

Solution

- (i) An enterprise should include prescribed information relating to a discontinuing operation in its financial statements beginning with the financial statements for the period in which the initial disclosure event (as defined in paragraph 15 of AS 24) occurs. For details, please refer Section 6.5 of this Chapter above.
- (ii) Examples of activities that do not necessarily satisfy criterion (a) of the definition, but that might do so in combination with other circumstances, include:
 - (a) Gradual or evolutionary phasing out of a product line or class of service;
 - (b) Discontinuing, even if relatively abruptly, several products within an ongoing line of business;

- (c) Shifting of some production or marketing activities for a particular line of business from one location to another; and
- (d) Closing of a facility to achieve productivity improvements or other cost savings.

31. ACCOUNTING STANDARD – 25

INTERIM FINANCIAL REPORTING

QUESTION 178

Sincere Corporation is dealing in seasonal product. Sales pattern of the product quarter-wise is as follows:

1 st quarter 30 th June	10%
2 nd quarter 30 th September	10%
3 rd quarter 31 st December	60%
4 th quarter 31 st March	20%

Information regarding the 1st quarter ended on 30th June, 20X1 is as follows:

Sales	80 crores
Salary and other expenses	60 crores
Advertisement expenses (routine)	4 crores
Administrative and selling expenses	8 crores

While preparing interim financial report for first quarter Sincere Corporation wants to defer ₹ 10 crores expenditure to third quarter on the argument that third quarter is having more sales, therefore, the third quarter should be debited by more expenditure. Considering the seasonal nature of business and the expenditures are uniform throughout all quarters, calculate the result of the first quarter as per AS 25. Also give a comment on the company's view.

SOLUTION

Particulars	(₹ In crores)	
Result of first quarter ended 30 th June, 20X1	80	
Turnover Other Income	<u>Nil</u>	
Total (a)		<u>80</u>
Less: Changes in inventories		<u>Nil</u>
Salaries and other cost		<u>60</u>
Administrative and selling Expenses (4+8)		<u>12</u>
Total (b)		<u>72</u>
Profit (a)-(b)		<u>8</u>

According to AS 25, the Income and Expense should be recognized when they are earned and incurred respectively. Therefore, seasonal incomes will be recognized when they occur. Thus, the company's view is not as per AS 25.

QUESTION 179: (Q.AS25.SM.09)

On 30th June, 20X1, Asmitha Ltd. incurred ₹ 2,00,000, net loss from disposal of a business segment. Also, on 31st July, 20X1, the company paid ₹ 60,000 for property taxes assessed for the calendar year 20X1. How the above transactions should be included in the determination of net income of Asmitha Ltd. for the six months interim period ended on 30th September, 20X1.

SOLUTION

According to Para 10 of AS 25 "Interim Financial Reporting", if an enterprise prepares and presents a complete set of financial statements in its interim financial report, the form and content of those statements should conform to the requirements as applicable to annual complete set of financial statements. As at 30th September, 20X1, Asmitha Ltd would report the entire amount of ₹ 2,00,000 as loss on the disposal of its business segment since the loss was incurred during interim period.

A cost charged as an expense in an annual period should be allocated to interim periods on accrual basis.

Since ₹ 60,000 Property tax payment relates to entire calendar year 20X1, ₹ 30,000 would be reported as an expense for six months ended on 30th September, 20X1 while out of the remaining ₹ 30,000, ₹ 15,000 for January, 20X1 to March, 20X1 should be shown as payment of the outstanding amount of previous year and another ₹ 15,000 related to quarter October, 20X1 to December, 20X1 would be reported as prepaid expenses.

QUESTION 180: (Q.AS25.SM.10)

An enterprise reports quarterly, estimates an annual income of ₹ 10 lakhs. Assume tax rates on 1st ₹ 5,00,000 at 30% and on the balance income at 40%. The estimated quarterly income are ₹ 75,000, ₹ 2,50,000, ₹ 3,75,000 and ₹ 3,00,000.

Calculate the tax expense to be recognized in each quarter.

SOLUTION

As per para 29 of AS 25 'Interim Financial Reporting', income tax expense is recognised in each interim period based on the best estimate of the weighted average annual income tax rate expected for the full financial year.

	₹
Estimated Annual Income (A)	<u>10,00,000</u>
Tax expense:	
30% on ₹ 5,00,000	1,50,000
40% on remaining ₹ 5,00,000	<u>2,00,000</u>
(B)	<u>3,50,000</u>

Weighted average annual income tax rate = $3,50,000 / 10,00,000 = 35\%$

Tax expense to be recognized in each of the quarterly reports	₹
Quarter I - ₹ 75,000 x 35%	26,250
Quarter II - ₹ 2,50,000 x 35%	87,500
Quarter III - ₹ 3,75,000 x 35%	1,31,250
Quarter IV - ₹ 3,00,000 x 35%	<u>1,05,000</u>
₹ 10,00,000	<u>3,50,000</u>

QUESTION 181: (Q.AS25.SM.11)

Antarbarti Limited reported a Profit Before Tax (PBT) of ₹ 4 lakhs for the third quarter ending 30-09-20X1. On enquiry you observe the following. Give the treatment required under AS 25:

- The dividend income of ₹ 4 lakhs received during the quarter has been recognized to the extent of ₹ 1 lakh only.
- 80% of sales promotion expenses ₹ 15 lakhs incurred in the third quarter has been deferred to the fourth quarter as the sales in the last quarter is high.
- In the third quarter, the company changed depreciation method from WDV to SLM, which resulted in excess depreciation of ₹ 12 lakhs. The entire amount has been debited in the third quarter, though the share of the third quarter is only ₹ 3 lakhs.
- ₹ 2 lakhs extra-ordinary gain received in third quarter was allocated equally to the third and fourth quarter.
- Cumulative loss resulting from change in inventory valuation was recognized in the

third quarter of ₹ 3 lakhs. Out of this loss ₹ 1 lakh relates to previous quarters.

- (vi) Sales of investment in the first quarter resulted in a gain of ₹ 20 lakhs. The company had apportioned this equally to the four quarters.

Prepare the adjusted profit before tax for the third quarter.

SOLUTION

As per para 36 of AS 25 “Interim Financial Reporting”, seasonal or occasional revenue and cost within a financial year should not be deferred as of interim date until it is appropriate to defer at the end of the enterprise’s financial year. Therefore, dividend income, extra-ordinary gain, and gain on sale of investment received during 3rd quarter should be recognised in the 3rd quarter only. Similarly, sales promotion expenses incurred in the 3rd quarter should also be charged in the 3rd quarter only.

Further, as per AS 10, Property, Plant and Equipment, if there is change in the depreciation method, such a change should be accounted for as a change in accounting estimate in accordance with AS 5, Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies, and applied prospectively. Therefore, no adjustment would be required due to change in the method of depreciation.

Accordingly, the adjusted profit before tax for the 3rd quarter will be as follows:

Statement showing Adjusted Profit Before Tax for the third quarter

	(₹ in lakhs)
Profit before tax (as reported)	4
Add:	
Dividend income ₹ (4-1) lakhs	3
Excess depreciation charged in the 3 rd quarter, due to change in the method	-
Extra ordinary gain ₹ (2-1) lakhs	1
Cumulative loss due to change in the method of inventory valuation should be applied retrospectively ₹ (3-2) lakhs	<u>1</u>
	9
Less: Sales promotion expenses (80% of ₹ 15 lakhs)	(12)
Gain on sale of investment (occasional gain should not be deferred)	<u>(5)</u>
Adjusted Profit before tax for the third quarter	<u>(8)</u>

32. ACCOUNTING STANDARD – 27

FINANCIAL REPORTING OF INTERESTS IN JOINT VENTURES

QUESTION 182: (MTP JAN'26)

Hari Ltd., OM Ltd. and Bhakti 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. 18,00,000 to be depreciated @ 5% p.a., Pipeline for Rs. 90,00,000 to be depreciated @ 15% p.a., computers and other electronics for Rs. 4,50,000 to be depreciated @ 40% p.a. and various vehicles of Rs. 13,50,000 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. 9,00,000 each year.

You are required to show the Extract of consolidated balance sheet and the extract of Statement of Profit & Loss and Balance Sheet for each venturer.

SOLUTION

Extract of Consolidated Balance Sheet

	Note	(₹)
Assets		
Non-current Assets		
Property, Plant and Equipment:	1	1,07,10,000
		1,07,10,000

Notes to Accounts

			(₹)
1.	Property, Plant and Equipment		
	Land & Building:		
	Hari Ltd.	5,70,000	
	OM Ltd.	5,70,000	
	Bhakti Ltd.	5,70,000	17,10,000
	Plant & Machinery:		
	Hari Ltd.	25,50,000	
	OM Ltd.	25,50,000	
	Bhakti Ltd.	25,50,000	76,50,000
	Computers:		
	Hari Ltd.	90,000	
	OM Ltd.	90,000	
	Bhakti Ltd.	90,000	2,70,000
	Vehicles:		
	Hari Ltd.	3,60,000	
	OM Ltd.	3,60,000	
	Bhakti Ltd.	3,60,000	10,80,000

In the Books of Hari Ltd.
Extract of statement of Profit & Loss

Particulars	Note No.	₹
Depreciation and amortisation expense	1	6,30,000
Other operating Expenses (Pipeline Expenses)		3,00,000

Extract of Balance Sheet

	Note No.	₹
Assets		
Non-current assets		
Property, Plant and Equipment	2	35,70,000

Notes to Accounts

		₹	₹
1.	Depreciation and amortisation expense		
	Land & Building	30,000	
	Plant & Machinery	4,50,000	
	Computers	60,000	-
	Vehicles	90,000	6,30,000
2.	Land & Building	6,00,000	-
	Less: Depreciation	-	5,70,000
		30,000	
	Plant & Machinery	30,00,000	-
	Less: Depreciation	-	25,50,000
		4,50,000	
	Computers	1,50,000	-
	Less: Depreciation	-	90,000
		60,000	
	Vehicles	4,50,000	-
	Less: Depreciation		3,60,000
		90,000	
		-	35,70,000

In the Books of OM Ltd.
Extract of draft Profit & Loss Account

Particulars	Note No.	₹
Depreciation and amortisation expense	1	6,30,000
Other operating Expenses (Pipeline Expenses)		3,00,000

Extract of Balance Sheet

	Note No.	₹
Assets		
Non-current assets		
Property, Plant and Equipment	2	35,70,000

Notes to Accounts

		₹	₹
1.	Depreciation and amortisation expense		
	Land & Building	30,000	
	Plant & Machinery	4,50,000	

	Computers	60,000	-
	Vehicles	90,000	6,30,000
2.	Land & Building	6,00,000	-
	Less: Depreciation	-30,000	5,70,000
	Plant & Machinery	30,00,000	-
	Less: Depreciation	-4,50,000	25,50,000
	Computers	1,50,000	-
	Less: Depreciation	-60,000	90,000
	Vehicles	4,50,000	-
	Less: Depreciation	-90,000	3,60,000
		-	35,70,000

QUESTION 183: (Q.AS.27.SM.01) (Jointly Controlled Operation)

Mr. A, Mr. B and Mr. C entered into a joint venture to purchase land, construct and sell flats. Mr. A purchased a land for ₹ 60,00,000 on 01.01.20X1 and for the purpose he took loan from a bank for ₹ 50,00,000 @ 8% interest p.a. He also paid registering fees ₹ 60,000 on the same day. Mr. B supplied the materials for ₹ 4,50,000 from his godown and further he purchased the materials for ₹ 5,00,000 for the joint venture. Mr. C met all other expenses of advertising, labour and other incidental expenses which turnout to be ₹ 9,00,000. On 30.06.20X1 each of the venturer agreed to take away one flat each to be valued at ₹ 10,00,000 each flat and rest were sold by them as follow: Mr. A for ₹ 40,00,000; Mr. B for ₹ 20,00,000 and Mr. C for ₹ 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.

SOLUTION

Draft Consolidated Profit & Loss Account

Particulars	₹	₹	Particulars	₹	₹
To Purchase of Land:			By Sale of Flats:		
Mr. A		60,00,000	Mr. A	40,00,000	
To Registration Fees:			Mr. B	20,00,000	
Mr. A		60,000	Mr. C	<u>10,00,000</u>	70,00,000
To Materials:			By Flats taken by Venturers:		
Mr. B		9,50,000	Mr. A	10,00,000	
To Other Expenses:			Mr. B	10,00,000	
Mr. C		9,00,000	Mr. C	<u>10,00,000</u>	30,00,000
To Bank Interest:					
Mr. A		2,00,000			
To Profits:					
Mr. A	6,30,000				
Mr. B	6,30,000				
Mr. C	<u>6,30,000</u>	18,90,000			
		1,00,00,000			1,00,00,000

**In the Books of Mr. A Joint
Venture Account**

Particulars	₹	Particulars	₹
To Bank Loan (Purchase of Land)	50,00,000	By Bank (Sale of Flats)	40,00,000
To Bank:(Purchase of Land)	10,00,000	By Land & Building	10,00,000
To Bank (Registration Fees)	60,000	By Bank (Received from Mr. B)	14,20,000
To Bank (Bank Interest)	2,00,000	By Bank (Received from Mr. C)	4,70,000
To Profit on JV	6,30,000		
	68,90,000		68,90,000

**In the Books of Mr. B Joint
Venture Account**

Particulars	₹	Particulars	₹
To Purchases (Material Supplied)	4,50,000	By Bank (Sale of Flats)	20,00,000
To Bank (Materials)	5,00,000	By Land & Building	10,00,000
To Profit on JV	6,30,000		
To Bank (Paid to Mr. A)	14,20,000		
	30,00,000		30,00,000

**In the Books of Mr. C Joint
Venture Account**

Particulars	₹	Particulars	₹
To Bank (Misc. Expenses)	9,00,000	By Bank (Sale of Flats)	10,00,000
To Profit on JV	6,30,000	By Land & Building	10,00,000
To Bank (Paid to Mr. A)	4,70,000		
	20,00,000		20,00,000

QUESTION 184: (Q.AS27.OM.06) (Master Question)

Standalone Balance sheets on 31/03/24

Particular	H	S	JV	ASS
ESC 10/- face Value	10,00,000	8,00,000	6,00,000	50,000
R&S	9,00,000	75,000	4,50,000	3,00,000
Liability	11,00,000	6,50,000	5,50,000	4,00,000
	30 Laksh	22 Laksh	16 Laksh	12 Laksh
Investments:				
In S 80%	11,00,000	-	-	-
In JV 50%	5,00,000	-	-	-
In Ass. 30%	1,60,000	-	-	-
Other Assets	12,40,000	22,00,000	16,00,000	12,00,000

- 1) Date of Acquisition of all Investments is 01/07/23.
- 2) Opening Balance of R&S on 01/04/23

S Ltd.	4,80,000
JV Ltd.	1,50,000
Associate Ltd.	1,20,000

Prepare Consolidated Balance Sheet for H Ltd.

SOLUTION:**1) Subsidiary Consolidation**

Analysis of Profit (AOP)			
Particulars	Pre	Post	B/S
R&S	4,80,000	2,70,000	7,50,000
(+/-) Time Adjustment	67,500	(2,70,000 × 3/12)	
	5,47,500	2,02,500	
Share of H Ltd.	4,38,000	1,62,000	
Share of M/I	1,09,500	40,500	

Minority Interest		
ESC	20%	1,60,000
(+) Pre-Acquisition	20%	1,09,500
(+) Post Acquisition	20%	40,500
		3,10,000
Cost of Control (COC)		
Investments in S Ltd.		11,00,000
(-) 80% Net Assets		
ESC 80%		(6,40,000)
Share of Pre-Acquisition Profit		(4,38,000)
Goodwill		22,000

2) JV (Proportionate Consolidation Method)

Analysis of Profit (AOP)			
Particulars	Pre	Post	B/S
R&S	1,50,000	3,00,000	4,50,000
(+/-) Time Adjustment	75,000	(3,00,000 × 3/12)	
	2,25,000	2,25,000	
H 50%	1,12,500	1,12,500	

Cost of Control	
Investment	5,00,000
(-) 50% of Net Assets	
ESC 50%	3,00,000
Share of Pre Acquisition	1,12,500
Goodwill	87,500

3) Associate Consolidation (Equity Method):

Analysis of Profit			
	Pre	Post	B/S
R&S	1,20,000	1,80,000	3,00,000
(+/-) Time Adjustment	45,000	(1,80,000 × 3/12)	
	1,65,000	1,35,000	

Equity Method	
Investment Cost	1,60,000
(-) 30% N. Assets as on DOA	1,99,500
Equity Share Capital 5,00,000 Share of Pre-Acquisition 1,65,000 6,65,000 × 30%	
Capital Reserve on DOA (Investment to be Increased by 39,500)	39,500
Revised Carrying Amount of Investment	1,99,500
(+) Share in Post-Acquisition Period Profit 1,35,000 × 30%	40,500
Closing Investment as on Balance Sheet	2,40,000

Consolidated P&L A/c of H Ltd.

Balance of R&S of H Ltd. as per SFS	9,00,000
(+) Share in Post Acquisition profit	
From S Ltd.	1,62,000
From JV Ltd.	1,12,500
From Associate Ltd.	40,500
Consolidation P&L	1,21,500
Capital Reserve from COC	39,500
Consolidation R&S	12,54,500

Consolidated Balance Sheet

Particulars	Amount
Equity Share Capital	10,00,000
Consolidation Reserves and Surplus	12,54,500
Minority Interest	3,10,000
Liability H 11,00,000	20,25,000
S 6,50,000	
JV 2,75,000	
	45,89,500
Investment in Associate as per Equity Method	2,40,000
Other Assets H 12,40,000	
I 22,00,000	
JV 8,00,000	
Goodwill S 22,000	1,09,500
JV 87,500	
	45,89,500

33. ACCOUNTING STANDARD - 29

“PROVISIONS, CONTINGENT LIABILITIES AND CONTINGENT ASSETS”

QUESTION 185: (RTP MAY'26 & EXAM SEP'25) (JAMMU & PUNJAB)

Galaxy Limited is in the process of finalization of its accounts for the year ended 31st March, 2025 and needs your advice on the following issues in line with the provisions of AS 29:

- (i) Galaxy Limited is selling cosmetic products under its brand name "Angel" but is getting these products manufactured from X Limited. It has an understanding (enforceable agreement) with X Limited that if the company becomes liable for any damage claims, due to any injury or harm to the customer of the cosmetic products, 40% shall be reimbursed to it by X Limited. During the year 2024-25, an estimate of the claim of ₹ 25 lakhs may be payable to the customers by Galaxy Limited. How should Galaxy Limited account for the claim that becomes payable?
- (ii) Galaxy Limited has been sued by one of its competitor for alleged infringement of trademark and a notice for levy of penalty of ₹ 50 lakhs has been received by it. The company has appointed a law firm to defend its case for a fee of ₹ 5 lakhs. 60% of the fees has been paid in advance and the rest 40% would be paid after finalization of the case. There are 70% chances that the penalty may not be imposed.

ANSWER:

Since the understanding results in an enforceable agreement, the reimbursement of ₹ 10,00,000 (40% of ₹ 25,00,000) shall be recognized as a reimbursement right and provision will be recognized for the full amount of the liability of ₹ 25,00,000.

The reimbursement right shall be treated as a separate asset and shall not be offset with the provision.

In the Statement of Profit and Loss, the expense may be presented as ₹ 15,00,000 after offsetting the reimbursement right.

As per AS 29, 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. Liability is a present obligation of the enterprise arising from the past events, the settlement of which is expected to result in an outflow from the enterprise of resources embodying economic benefits. In the given case, there are 70% chances that the penalty may not be levied. Accordingly, Galaxy Limited should not make the provision for liability. The matter is disclosed as a contingent liability unless the probability of any outflow is considered as remote.

However, a provision should be made for the remaining 40% fees of the law firm amounting to ₹ 2,00,000 in the financial statements for 2024-25.

QUESTION 186: (Q.AS29.SM.101) (SIMILAR IN Exam Nov'22)

At the end of the financial year ending on 31st March, 2022, a company finds that there are twenty law suits outstanding which have not been settled till the date of approval of accounts by the Board of Directors. The possible outcome as estimated by the Board is as follows:

particulars	probability	Loss (Rs.)
In respect of five cases (Win)	100%	-
Next ten cases (Win)	50%	-
Lose (Low damages)	40%	12,00,000
Lose (High damages)	10%	20,00,000

Remaining five cases		
Win	50%	-
Lose (Low damages)	30%	10,00,000
Lose (High damages)	20%	21,00,000

Outcome of each case is to be taken separate entity. Ascertain the amount of contingent loss and the accounting treatment in respect thereof as per AS – 29.

SOLUTION

According to AS 29 (Revised) 'Provisions, Contingent Liabilities and Contingent Assets', contingent liability should be disclosed in the financial statements if following conditions are satisfied:

- There is a present obligation arising out of past events but not recognized as provision.
- It is not probable that an outflow of resources embodying economic benefits will be required to settle the obligation.
- The possibility of an outflow of resources embodying economic benefits is not remote.
- The amount of the obligation cannot be measured with sufficient reliability to be recognized as provision.

In this case, the probability of winning of first five cases is 100% and hence, question of providing for contingent loss does not arise. The probability of winning of next ten cases is 50% and for remaining five cases is 50%. As per AS 29 (Revised), we make a provision if the loss is probable. As the loss does not appear to be probable and the possibility of an outflow of resources embodying economic benefits is remote, therefore disclosure by way of note should be made. For the purpose of the disclosure of contingent liability by way of note, amount may be calculated as under:

$$\begin{aligned}\text{Expected loss in next ten cases} &= 40\% \text{ of ₹ } 12,00,000 + 10\% \text{ of ₹ } 20,00,000 \\ &= ₹ 4,80,000 + ₹ 2,00,000 \\ &= ₹ 6,80,000\end{aligned}$$

$$\begin{aligned}\text{Expected loss in remaining five cases} &= 30\% \text{ of ₹ } 10,00,000 + 20\% \text{ of ₹ } 21,00,000 \\ &= ₹ 3,00,000 + ₹ 4,20,000 \\ &= ₹ 7,20,000\end{aligned}$$

To disclose contingent liability on the basis of maximum loss will be highly unrealistic. Therefore, the better approach will be to disclose the overall expected loss of ₹ 1,40,00,000 (₹ 6,80,000 x 10 + ₹ 7,20,000 x 5) as contingent liability.

QUESTION 187: (Q.AS29.SM.103) (Similar to Exam Nov'19 & Exam Jan'25)

A Ltd. provides after sales warranty for two years to its customers. Based on past experience, the company has the following policy for making provision for warranties on the invoice amount, on the remaining balance warranty period.

Less than 1 year: 2% provision

More than 1 year: 3% provision

The company has raised invoices as under:

Invoice Date	Amount (Rs)
11 th Feb, 2017	60,000
25 th Dec, 2017	40,000
04 th Oct, 2018	1,35,000

Calculate the provision to be made for warranty under AS-29 as at 31st March, 2018 and 31st March, 2019. Also compute amount to be debited to P & L account for the year ended 31st March, 2019.

ANSWER:

Provision to be made for warranty under AS 29 'Provisions, Contingent Liabilities and Contingent Assets'

As at 31 st March, 2018	= Rs 60,000 x .02 + Rs 40,000 x .03
	= Rs 1,200 + Rs 1,200 = Rs 2,400
As at 31 st March, 2019	= Rs 40,000 x .02 + Rs 1,35,000 x .03
	= Rs 800 + Rs 4,050 = Rs 4,850

Amount debited to Profit and Loss Account for year ended 31st March, 2019

	Rs
Balance of provision required as on 31.03.2019	4,850
Less: Opening Balance as on 1.4.2018	<u>(2,400)</u>
Amount debited to profit and loss account	<u>2,450</u>

Note: No provision will be made on 31st March, 2019 in respect of sales amounting Rs 60,000 made on 11th February, 2017 as the warranty period of 2 years has already expired.

QUESTION 188: (Q.AS29.RMP.201) (RTP May'20 and Exam Nov'20)

With reference to AS 29, how would you deal with the following in the annual accounts of the company at the Balance Sheet dates:

- An organization operates an offshore oilfield where its licensing agreement requires it to remove the oil rig at the end of production and restore the seabed. Ninety percent of the eventual costs relate to the removal of the oil rig and restoration of damage caused by building it, and ten percent arise through the extraction of oil. At the balance sheet date, the rig has been constructed but no oil has been extracted.
- During 2018-19 Ace Ltd. gives a guarantee of certain borrowings of Brew Ltd., whose financial condition at that time is sound. During 2019-20, the financial condition of Brew Ltd. deteriorates and on 31st Dec. 2019, it goes into liquidation. (Balance Sheet date 31-3-19).

ANSWER:

- The construction of the oil rig creates an obligation under the terms of the license to remove the rig and restore the seabed and is thus an obligating event. At the balance sheet date, however, there is no obligation to rectify the damage that will be caused by extraction of the oil. An outflow of resources embodying economic benefits in settlement is probable. Thus, a provision is recognized for the best estimate of ninety per cent of the eventual costs that relate to the removal of the oil rig and restoration of damage caused by building it. These costs are included as part of the cost of the oil rig. However, there is no obligation to rectify the damage that will be caused by extraction of oil, as no oil has been extracted at the balance sheet date. So, no provision is required for the cost of extraction of oil at balance sheet date. Ten per cent of costs that arise through the extraction of oil are recognized as a liability when the oil is extracted.
- As per AS 29, for a liability to qualify for recognition there must be not only a present obligation but also the probability of an outflow of resources embodying economic benefits to settle that obligation.
The obligating event is the giving of the guarantee by Ace Ltd. for certain borrowings of Brew Ltd., which gives rise to an obligation. No outflow of benefits is probable at 31 March

2019. Thus no provision is recognized. The guarantee is disclosed as a contingent liability unless the probability of any outflow is regarded as remote.

During 2019-20, the financial condition of Brew Ltd. deteriorates and finally goes into liquidation. The obligating event is the giving of the guarantee, which gives rise to a legal obligation. At 31 March 2020, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation. Thus, provision is recognized for the best estimate of the obligation.

QUESTION 189: (Q.AS29.RMP.205) (RTP May'22, Nov'22)

Chaos Limited is in the process of finalizing its accounts for the year ended 31st March, 2020. It seeks your advice in the following cases:

- (i) Chaos Limited has filed a court case in 2014-2015 against its competitors. It became evident to its lawyers during the year ended 31st March, 2020 that Chaos Limited may lose the case and would have to pay Rs. 3,00,000 being the cost of litigation. No entries/provisions have been made in the books.
- (ii) A new regulation has been passed in 2019-2020 by the healthcare ministry to upgrade facilities. Deadline set by the government is 31.03.2021. The company estimates an expenditure of Rs. 10,00,000 for the said upgrade.
- (iii) The company gives one year warranty for its healthcare equipment under the contract of sale that it will make good any manufacturing defect by repair or replacement. As per past experience, it is probable that there will be 1% such cases and estimated cost of repair / replacement is estimated at 10% of such sale value. During the year, the company has made a sale of Rs. 5 crores.

Kindly give your answer for each of above with proper reasoning according to the relevant Accounting Standard. Also state the principles for recognition of provision, as per AS 29.

SOLUTION

Principles for recognition of provisions: As per AS 29, "a provision shall be recognised when:

- (i) an entity has a present obligation (legal or constructive) as a result of a past event;
- (ii) it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation; and
- (iii) a reliable estimate can be made of the amount of the obligation. If these conditions are not met, no provision shall be recognised."

Accounting treatment under the given scenarios:

- (i) On 31st March, 2020, since it is evident to the lawyer that Chaos Limited may lose the case and also a reliable estimate of the outflow can be made as Rs. 3,00,000, there is a present obligation. Hence, provision should be recognised for Rs. 3,00,000 for the amount which may be required to settle the obligation.
- (ii) Under new regulation, an entity is required to upgrade its facilities by 31 st March, 2021. However, on 31st March, 2020, i.e. at the end of the reporting period, there is no obligation because there is no obligating event either for the costs of upgrading the facilities or for fines under the regulations. Hence, no provision should be recognized on 31st March, 2020 for upgrading the facilities by 31st March, 2021.
- (iii) The obligating event is the sale of health care equipment with a warranty, which gives rise to a legal obligation. Here, an outflow of resources embodying economic benefits in settlement is probable for the warranties as a whole. Hence, a provision is recognized for the best estimate of the costs of making good under the warranty products sold before the end of the reporting period as follows:

Probability of warranty cases for the entity where repair/replacement may be required as per past experience

$$= 1\% \text{ of Rs. } 5,00,00,000 = \text{Rs. } 5,00,000$$

Estimated cost of repair / replacement

$$= \text{Rs. } 5,00,000 \times 10\% = \text{Rs. } 50,000.$$

QUESTION 190: (Q.AS29.RMP.207) (MTP Nov'21, May'23 & RTP May' 25)

Saharsh Ltd. is engaged in manufacturing of electric home appliances. The company is in the process of finalizing its accounts for the year ended 31.3.2020 and needs your expert advice on the following issues in line with the provisions of AS 29:

A case has been filed against the company in the consumer court and a notice for levy of a penalty of Rs. 20 lakhs has been received. The company has appointed a lawyer to defend the case for a fee of Rs. 2 lakhs. 50% of the fees has been paid and balance 50% will be paid after finalisation of the case. There are 75% chances that the penalty may not be levied.

The company had committed to supply a consignment worth Rs. 1 crore to one of its dealers by the year-end. As per the contract, if delivery is not made on time, a compensation of 15% is to be paid on the value of delayed/lost consignment. While the consignment was in transit, one of the trucks carrying goods worth Rs. 30 lakhs met with an accident. It was however covered by Insurance. According to the surveyor's report, the policy amount is collectable, subject to 10% deduction. Before closing the books of accounts, the company has received the information that the policy amount has been processed and the dealer has also claimed the compensation for the consignment of goods worth Rs. 30 lakhs which was in transit.

SOLUTION

(i) As per AS 29, 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.

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.

In the given case, there are 75% chances that the penalty may not be levied. Accordingly, Saharsh Ltd. should not make the provision for penalty.

However, a provision should be made for remaining 50% fees of the lawyer in the financial statements of financial year 2019-2020.

(ii)

Loss due to accident	Rs. 30,00,000
Insurance claim receivable by company = Rs. 30,00,000 x 90%	Rs. 27,00,000
Loss to be recognised in the books for 2019-2020	Rs. 3,00,000
Insurance claim receivable to be recorded in the books	Rs. 27,00,000
Compensation claim by dealer against company to be provided for in the books = Rs. 30,00,000 x 15%	Rs. 4,50,000

QUESTION 191: (Q.AS29.RMP.213) (RTP Sep'24)

A company incorporated under Section 8 of the Companies Act, 2013, have main objective to promote the trade by organizing trade fairs / exhibitions. When company was organizing the trade fair and exhibitions it decided to charge 5% contingency charges for the participants/outside agencies on the income received from them by the company, while in the case of fairs organized by outside agencies, 5% contingency charges are levied separately in the invoice, the contingency

charges in respect of fairs organized by the company itself are inbuilt in the space rent charged from the participants. Both are credited to Income and Expenditure Account of the company. The intention of levying these charges is to meet any unforeseen liability, which may arise in future. The instances of such unforeseen liabilities could be on account of injury/loss of life to visitors/ exhibitors, etc., due to fire, terrorist attack, stampede, natural calamities and other public and third party liability. The chances of occurrence of these events are high because of large crowds visiting the fair. The decision to levy 5% contingency charges was based on assessment only as actual liability on this account cannot be estimated.

The following accounting treatment and disclosure was made by the company in its financial statements:

1. 5% contingency charges are treated as income and matching provision for the same is also being made in accounts.
2. A suitable disclosure to this effect is also made in the notes forming part of accounts.

Required:

- (i) Whether creation of provision for contingencies under the facts and circumstances of the case is in conformity with AS 29
- (ii) If the answer of (i) is "No" then what should be the treatment of the provision which is already created in the balance sheet.

ANSWER:

- (i) Para 14 of AS 29 "Provisions, Contingent Liabilities and Contingent Assets" states that a provision should be recognised when (a) An enterprise has a present obligation as a result of a past event and (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.
- (ii) "Provision" is the amount retained by the way of providing for any known liability. Since the contingencies stipulated by the company are not known at the balance sheet date, the provision in this regard cannot be created. Therefore, the provision so created by the company shall be treated as a 'Reserve'.

QUESTION 192: (Q.AS29.RMP.214) (RTP Jan'25)

During the year, QA Ltd. delivered manufactured products to customer K. The products were faulty and on 1st October, 2023 customer K commenced legal action against the Company claiming damages in respect of losses due to the supply of faulty product. Upon investigating the matter, QA Ltd. discovered that the products were faulty due to defective raw material procured from supplier F. Therefore, on 1st December, 2023, the Company commenced legal action against F claiming damages in respect of the supply of defective raw materials.

QA Ltd. has estimated that it's probability of success of both legal actions, the action of K against QA Ltd. and action of QA Ltd. against F, is very high.

On 1st October, 2023, QA Ltd. has estimated that the damages it would have to pay K would be ₹ 5 crore. This estimate was revised to ₹ 5.2 crore as on 31st March, 2024 and ₹ 5.25 crore as at 15th May, 2024. This case was eventually settled on 1st June, 2022, when the Company paid damages of ₹ 5.3 crore to K.

On 1st December, 2023, QA Ltd. had estimated that it would receive damages of ₹ 3.5 crore from F. This estimate was revised to ₹ 3.6 crore as at 31st March, 2024 and ₹ 3.7 crore as on 15th May, 2024. This case was eventually settled on 1st June, 2022 when F paid ₹ 3.75 crore to QA Ltd. QA Ltd. had, in its financial statements for the year ended 31st March, 2024, provided ₹ 3.6 crore as the financial statements were approved by the Board of Directors on 26th April, 2024.

- (i) Whether the Company is required to make provision for the claim from customer K as per applicable AS? If yes, please give the rationale for the same.
- (ii) If the answer to (a) above is yes, what is the entry to be passed in the books of account as on 31st March, 2024?
- (iii) What will the accounting treatment of the action of QA Ltd. against supplier F as per applicable AS?

ANSWER:

- (i) Yes, QA Ltd. is required to make provision for the claim from customer K as per AS 29 since the claim is a present obligation as a result of delivery of faulty goods manufactured. Also, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligations. Further, a reliable estimate of ₹ 5.2 crore can be made of the amount of the obligation while preparing the financial statements as on 31st March, 2024.
- (ii) Statement of Profit and Loss A/c Dr. ₹ 5.2 crore
To Current Liability A/c ₹ 5.2 crore
- (iii) As per para 30 of AS 29, QA Ltd. shall not recognise a contingent asset. Here the probability of success of legal action is very high but there is no concrete evidence which makes the inflow virtually certain. Hence, it will be considered as contingent asset only and shall not be recognized.