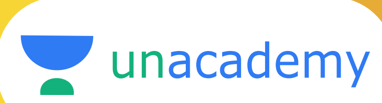

CA- INTER GROUP - II

ADVANCED ACCOUNTS

COMPILER

VERSION 5.0

RAHUL MALKAN

: KEY FEATURES :

- Covers RTP and Past Papers
- Chapter wise
- Along with Solutions
- All Chapters Covered

CA INTERMEDIATE GROUP – 2

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ADVANCED ACCOUNTS – COMPILER – VERSION 5.0

CHAPTER 1

AS 4 CONTINGENCIES AND EVENTS OCCURRING AFTER THE BALANCE SHEET DATE

Question 1 : May – 2020 – RTP

With reference to AS 4 "Contingencies and events occurring after the balance sheet date", state whether the following events will be treated as contingencies, adjusting events or non-adjusting events occurring after balance sheet date in case of a company which follows April to March as its financial year.

(i) A major fire has damaged the assets in a factory on 5th April, 5 days after the year end. However, the assets are fully insured and the books have not been approved by the Directors.

(ii) A suit against the company's advertisement was filed by a party on 10th April, 10 days after the year end claiming damages of Rs.20 lakhs.

Solution :

According to AS 4 on 'Contingencies and Events Occurring after the Balance Sheet Date', 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. However, adjustments to assets and liabilities are not appropriate for events occurring after the balance sheet date, if such events do not relate to conditions existing at the balance sheet date. "Contingencies" used in the Standard is restricted to conditions or situations at the balance sheet date, the financial effect of which is to be determined by future events which may or may not occur.

(i) Fire has occurred after the balance sheet date and also the loss is totally insured. Therefore, the event becomes immaterial and the event is non-adjusting in nature.

(ii) The contingency is restricted to conditions existing at the balance sheet date. However, in the given case, suit was filed against the company's advertisement by a party on 10th April for amount of Rs. 20 lakhs. Therefore, it does not fit into the definition of a contingency and hence is a non-adjusting event.

Question 2 : Nov – 2020 – RTP

A fire, on 2nd April, 2020, completely destroyed a manufacturing plant of Omega Ltd. whose financial year ended on 31st March, 2020, the financial statements were approved by their approving authority on 15th June, 2020. It was expected that the loss of Rs.10 million would be

fully covered by the insurance company. How will you disclose it in the financial statements of Omega Ltd. for the year ended 31st March, 2020.

Solution :

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.

Question 3 : May – 2021 – RTP

A case is going on between ABC Ltd. and Tax department on claiming the exemption for certain items, for the year 2019-2020. The court has issued the order on 15th April and rejected the claim of the company. Accordingly, company is liable to pay the additional tax. The financial statements were approved on 31st May, 2020. Shall company account for such tax in the year 2019-2020 or shall it account for in the year 2020-2021?

Solution :

To decide whether, the event is adjusting or not adjusting two conditions need to be satisfied,

(a) There has to be evidence

(b) The event must have been related to period ending on reporting date.

Here both the conditions are satisfied. Court order is a conclusive evidence which has been received before approval of the financial statements since the liability is related to earlier year. The event will be considered as an adjusting event and accordingly the amount will be adjusted in accounts of 2019-2020.

Question 4 : July – 2021 – Paper

Surya Limited follows the financial year from April to March. It has provided the following information.

(i) A suit against the Company's Advertisement was filed by a party on 5th April, 2021, claiming damages of Rs. 5 lakhs.

(ii) Company sends a proposal to sell an immovable property for Rs. 45 lakhs in March 2021. The book value of the property is Rs. 30 lakhs as on year end date. However, the Deed was registered on 15th April, 2021.

(iii) The terms and conditions for acquisition of business of another company have been decided by the end of March 2021, but the financial resources were arranged in April 2021. The amount invested was Rs. 50 lakhs.

(iv) Theft of cash amounting to Rs. 4 lakhs was done by the Cashier in the month of March 2021 but was detected on the next day after the Financial Statements have been approved by the Directors.

Keeping in view the provisions of AS-4, you are required to state with reasons whether the above events are to be treated as Contingencies, Adjusting Events or Non-Adjusting Events occurring after Balance Sheet date.

Solution :

(i) Suit filed against the company is a contingent liability but it was not existing as on date of balance sheet date as the suit was filed on 5th April after the balance sheet date. As per AS 4, 'Contingencies' is restricted to conditions or situations at the balance sheet date, the financial effect of which is to be determined by future events which may or may not occur. However, it may be disclosed with the nature of contingency, being a contingent liability**.**
This event does not pertain to conditions on the balance sheet date. Hence, it will have no effect on financial statements and will be a non-adjusting event.

(ii) In this case, no adjustment to assets and liabilities is required as the event does not affect the determination and the condition of the amounts stated in the financial statements for the year ended 31st March, 2021. There was just a proposal before 31st March, 2021 and hence sale cannot be shown in the financial statements for the year ended 31st March, 2021.
Sale of immovable property is an event occurring after the balance sheet date and is a non-adjusting event.

(iii) In the given case, terms and conditions for acquisition of business were finalized before the balance sheet date and carried out before the closure of the books of accounts but transaction for payment of financial resources was effected in April, 2021.
Hence, it is an adjusting event and necessary adjustment to assets and liabilities for acquisition of business is necessary in the financial statements for the year ended 31st March 2021.

(iv) Only those events which occur between the balance sheet date and the date on which the financial statements are approved, may indicate the need for adjustments to assets and liabilities as at the balance sheet date or may require disclosure.
In the given case, as the theft of cash was detected after approval of financial statements, no adjustment is required. Hence it is non-adjusting event.

Question 5 : Nov – 2021 – RTP

XYZ Ltd. operates its business into various segments. Its financial year ended on 31st March, 2020 and the financial statements were approved by their approving authority on 15th June, 2020. The following material events took place:

a. A major property was sold (it was included in the balance sheet at Rs. 25,00,000) for which contracts had been exchanged on 15th March, 2020. The sale was completed on 15th May, 2020 at a price of Rs. 26,50,000.

b. On 2nd April, 2020, a fire completely destroyed a manufacturing plant of the entity. It was expected that the loss of Rs. 10 million would be fully covered by the insurance company.

c. A claim for damage amounting to Rs. 8 million for breach of patent had been received by the entity prior to the year-end. It is the director's opinion, backed by legal advice that the claim will ultimately prove to be baseless. But it is still estimated that it would involve a considerable expenditure on legal fees.

You are required to state with reasons, how each of the above items should be dealt with in the financial statements of XYZ Ltd. for the year ended 31st March, 2020.

Solution :

Treatment as per AS 4 'Contingencies and Events Occurring After the Balance Sheet Date'

(a)	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 should be reflected in the financial statements ended on 31.3.2020 and the profit on sale of property Rs. 1,50,000 would be considered.
(b)	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.
(c)	On the basis of evidence provided, the claim against the company will not succeed. Thus, Rs. 8 million should not be provided in the account, but should be disclosed by means of a contingent liability with full details of the facts. Provision should be made for legal fee expected to be incurred to the extent that they are not expected to be recovered.

Question 6 : Dec – 2021 – Paper

As per the provision of AS 4, you are required to state with reason whether the following transactions are adjusting event or non-adjusting event for the year ended 31.03.2021 in the books of New Ltd. (accounts of the company were approved by board of directors on 10.07.2021):

1. Equity Dividend for the year 2020-21 was declared at the rate of 7% on 15.05.2021.
2. On 05.03.2021, Rs.53,000 cash was collected from a customer but not deposited by the cashier. This fraud was detected on 22.06.2021.
3. One building got damaged due to occurrence of fire on 23.05.2021. Loss was estimated to be Rs.81,00,000.

Solution :

(i) If dividends are declared after the balance sheet date but before the financial statements are approved, the dividends are not recognized as a liability at the balance sheet date because no obligation exists at that time unless a statute requires otherwise. Such dividends are disclosed in the notes. Thus, no liability for dividends needs to be recognized in financial statements for financial year ended 31st March, 2021 and declaration of dividend is non-adjusting event.

(ii) As per AS 4 'Contingencies and Events occurring after the Balance Sheet Date' an event occurring after the balance sheet date may require adjustment to the reported values of assets, liabilities, expenses or incomes if such events relate to conditions existing at the balance sheet date. In the given case, fraud of the accounting period is detected after the balance sheet date but before approval of the financial statements, it is necessary to recognize the loss. Thus loss amounting Rs. 53,000 should be adjusted in the accounts of the company for the year ended 31st March, 2021 as it is adjusting event.

(iii) AS 4 states that adjustments to assets and liabilities are not appropriate for events occurring after the balance sheet date, if such events do not relate to conditions existing at the balance sheet date. The damage of one building due to fire did not exist on the balance sheet date i.e. 31.3.2021. Therefore, loss occurred due to fire is not to be recognized in the financial year 2020-2021 as it is non-adjusting event.

However, according to the standard, unusual changes affecting the existence or substratum of the enterprise after the balance sheet date may indicate a need to consider the use of fundamental accounting assumption of going concern in the preparation of the financial statements. As per the information given in the question, the fire has caused major destruction; therefore, fundamental accounting assumption of going concern would have to be evaluated. Considering that the going concern assumption is still valid, the fact of fire together with an estimated loss of Rs. 81 lakhs should be disclosed in the report of the approving authority for financial year 2020-21 to enable users of financial statements to make proper evaluations and decisions.

Question 7 : May – 2022 – RTP

Tee Ltd. closes its books of accounts every year on 31st March. The financial statements for the year ended 31st March 2020 are to be approved by the approving authority on 30th June 2020. During the first quarter of 2020-2021, the following events / transactions has taken place. The accountant of the company seeks your guidance for the following:

(i) Tee Ltd. has an inventory of 50 stitching machines costing at Rs. 5,500 per machine as on 31st March 2020. The company is expecting a heavy decline in the demand in next year. The inventories are valued at cost or net realizable value, whichever is lower. During the month of April 2020, due to fall in demand, the prices have gone down drastically. The company has sold 5 machines during April, 2020 at a price of Rs. 4,000 per machine.

(ii) A fire has broken out in the company's godown on 15th April 2020. The company has estimated a loss of Rs. 25 lakhs of which 75% is recoverable from the Insurance company.

(iii) A suit against the company's advertisement was filed by a party on 10th April, 2020 10 days after the year end claiming damages of Rs. 20 lakhs.

You are required to state with reasons, how the above transactions will be dealt with in the financial statements for the year ended 31 March 2020.

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 30 June 2020. On the basis of above principles, following will be the accounting treatment in the financial statements for the year ended at 31 March 2020:

(i) Since on 31 March 2020, Tee Ltd. was expecting a heavy decline in the demand of the stitching machine. Therefore, decline in the value during April, 2020 will be considered as an adjusting event. Hence, Tee Ltd. needs to adjust the amounts recognized in its financial statements w.r.t. net realizable value at the end of the reporting period. Accordingly, inventory should be written down to Rs. 4,000 per machine. Total value of inventory in the books will be 50 machines x Rs. 4,000 = Rs. 2,00,000.

(ii) A fire took place after the balance sheet date i.e. during 2020-2021 financial year. Hence, the financial statements for the year 2019-2020 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) The contingency is restricted to conditions existing at the balance sheet date. However, in the given case, suit was filed against the company's advertisement by a party on 10th April for amount of Rs. 20 lakhs. Therefore, it does not fit into the definition of a contingency and hence is a non-adjusting event.

Question 8 : Nov – 2022 – RTP

Explain accounting treatment of Contingent Gains as per AS 4 “Contingencies and Events occurring after the Balance Sheet Date”.

Solution :

Contingent gains are not recognised in financial statements since their recognition may result in the recognition of revenue which may never be realised. However, when the realisation of a gain is virtually certain, then such gain is not a contingency and accounting for the gain is appropriate.

Question 9 : Nov – 2022 – Paper

MN Limited operates its business into various segments. Its financial year ended on 31st March, 2022 and financial statements were approved by their approving authority on 15th June, 2022. The following material events took place :

(i) On 7th April, 2022, a fire completely destroyed a manufacturing plant of the entity. It was expected that the loss of Rs.15 crores would be fully covered by the insurance company.

(ii) A claim for damage amounting to Rs.12 crores for breach of patent had been received by the entity prior to the year end. It is the director's opinion, backed by legal advice that the claim will ultimately prove to be baseless. But it is still estimated that it would involve a considerable expenditure on legal fees.

(iii) A major property was sold (it was included in the balance sheet at Rs.37,50,000) for which contracts had been exchanged on 15th March, 2022. The sale was completed on 15th May, 2022 at a price of Rs.39,75,000.

You are required to state with reasons, how each of the above items should be dealt with in the financial statements of MN Limited for the year ended 31st March, 2022 as per AS - 4.

Thanks ....

CHAPTER 2

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

Question 1 : May – 2020 – RTP

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

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

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

Solution :

As per AS 5 'Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies', 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.

(i) Accordingly, introduction of a formal retirement gratuity scheme by an employer in place of ad hoc ex-gratia payments to employees on retirement is not a change in an accounting policy.

(ii) Similarly, the adoption of a new accounting policy for events or transactions which did not occur previously or that were immaterial will not be treated as a change in an accounting policy

Question 2 : Nov – 2020 – RTP

The Accountant of Virush Limited has sought your opinion, whether the following transactions will be treated as change in Accounting Policy or not for the year ended 31st March, 2020. Please advise him in the following situations in accordance with the provisions of relevant Accounting Standard;

(i) Till the previous year the machinery 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.

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

Solution :

(i) Change in useful life of machinery from 5 years to 3 years is a change in estimate and is not a change in accounting policy.

(ii) Introduction of a formal retirement gratuity scheme by an employer in place of ad hoc ex-gratia payments to employees on retirement is not a change in an accounting policy.

Question 3 : Jan – 2021 – Paper

State whether the following items are an example of change in Accounting policy / Change in accounting Estimates / Extraordinary items / Prior period items / Ordinary Activity.

(i) Actual from 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 the 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 assets.

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	Extra -ordinary Items
(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

Question 4 : May – 2021 – RTP

XYZ Ltd. is in the process of finalizing its account for the year ended 31st March, 2020. The company seeks your advice on the following:
The company's tax assessment for assessment year 2017-18 has been completed on 14th February, 2020 with a demand of Rs.5.40 crore. The company paid the entire due under protest without prejudice to its right of appeal. The company files its appeal before the appellate authority wherein the grounds of appeal cover tax on additions made in the assessment order for a sum of Rs.3.70 crore.

Solution :

Since the company is not appealing against the addition of Rs. 1.70 crore (Rs. 5.40 crore less Rs. 3.70 crore), therefore, the same should be provided/ expensed off in its accounts for the year ended on 31st March, 2020. However, the amount paid under protest can be kept under the heading 'Long-term Loans & Advances / Short-term Loans and Advances' as the case may be alongwith disclosure as contingent liability of Rs. 3.70 crore.

Question 5 : Nov – 2021 – RTP

There was a major theft of stores valued at Rs. 10 lakhs in the preceding year which was detected only during current financial year (2020-2021). How will you deal with this information in preparing the financial statements of R Ltd. for the year ended 31st March, 2021.

Solution :

Due to major theft of stores in the preceding year (2019-2020) which was detected only during the current financial year (2020–2021), there was overstatement of closing inventory of stores in the preceding year. This must have also resulted in the overstatement of profits of previous year, brought forward to the current year. The adjustments are required to be made in the current year as 'Prior Period Items' as per AS 5 (Revised) on Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies. Accordingly, the adjustments relating to both opening inventory of the current year and profit brought forward from the previous year should be separately disclosed in the statement of profit and loss together with their nature and amount in a manner that their impact on the current profit or loss can be perceived. Alternatively, it may be assumed that in the preceding year, the value of inventory of stores as found out by physical verification of inventories was considered in the preparation of financial statements of the preceding year. In such a case, only the disclosure as to the theft and the resulting loss is required in the notes to the accounts for the current year i.e, year ended 31st March, 2021.

Question 6 : Nov – 2021 – RTP

Management decided to pay pension to those employees who have retired after completing 5 years of service in the organisation. Such employees will get pension of Rs. 20,000 per month.

Earlier there was no such scheme of pension in the organization. Explain whether this will constitute a change in accounting policy or not as per AS 5.

Solution :

As per AS 5 'Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies', 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. Accordingly, the adoption of a new accounting policy of paying pension to retired employees is a policy for events or transactions which did not occur previously. Hence, it will not be treated as a change in an accounting policy.

Question 7 : May – 2022 – RTP

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, 2021. Please advise him in the following situations in accordance with the provisions of relevant Accounting Standard;

(i) Provision for doubtful debts was created @ 2% till 31st March, 2020. From the Financial year 2020-2021, the rate of provision has been changed to 3%.

(ii) During the year ended 31st March, 2021, 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, 2021, 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, 2020. Subsequently in 2020-21, 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 accounting estimate and is not a 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 accounting policy.

(iii) Change in useful life of furniture from 5 years to 3 years is a change in accounting 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 8 : May – 2022 – Paper

TQ Cycles Ltd. is in the manufacturing of bicycles, a labour 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 31stMarch, 2023.

Question 9 : Nov – 2022 – RTP

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. Do you agree with the treatment and disclosure? If not, state your views.

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 10 : Nov – 2022 – Paper

The Accountant of Shiva Limited has sought your opinion with relevant reasons, whether the following transactions will be treated as change in Accounting Policies or change in Accounting Estimates for the year ended 31st March, 2021. Please advise him in the following situations in accordance with the provisions of AS - 5 :

(i) Provision for doubtful debts was created @ 3% till 31st March, 2020. From the Financial year 2020-2021, the rate of provision has been changed to 4%.

(ii) During the year ended 31st March, 2021, the management has introduced a formal gratuity scheme in place of ad-hoc ex-gratia payments to employees on retirement.

(iii) Till 31st March, 2020 the furniture was depreciated on straight line basis over a period of 5 years. From the Financial year 2020- 2021, 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, 2021, there was change in cost formula in measuring the cost of inventories.

Thanks ....

CHAPTER 3

AS 7 CONSTRUCTION CONTRACTS

Question 1 : May – 2018 – Paper

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:

(i) Profit/Loss for the year ended 31st March, 2018.

(ii) Contract work in progress as at end of financial year 2017-18.

(iii) Revenue to be recognized out of the total contract value.

(iv) 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 × 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 2 : May – 2019 – RTP

GTI Ltd. negotiates with Bharat Oil Corporation Ltd. (BOCL), for construction of "Retail Petrol & Diesel Outlet Stations". Based on proposals submitted to different Regional Offices of BOCL, the final approval for one outlet each in Region X, Region Y, Region Z is awarded to GTI Ltd. A single agreement is entered into between two. The agreement lays down values for each of the three outlets i.e. Rs. 102 lacs, Rs. 150 lacs, Rs. 130 lacs for Region X, Region Y, Region Z respectively. Agreement also lays down completion time for each Region.
Comment whether GTI Ltd. will treat it as single contract or three separate contracts with reference to AS-7?

Solution :

As per AS 7 'Construction Contracts', when a contract covers number of assets, the construction of each asset should be treated as a separate construction contract when:
(a) separate proposals have been submitted for each asset;
(b) each asset has been subject to separate negotiation and the contractor and customer have been able to accept or reject that part of the contract relating to each asset; and
(c) the costs and revenues of each asset can be identified.
In the given case, each outlet is submitted as a separate proposal to different Zonal Offices, which can be separately negotiated, and costs and revenues thereof can be separately identified. Hence, each asset will be treated as a "single contract" even if there is one single agreement for contracts.
Therefore, three separate contract accounts must be recorded and maintained in the books of GTI Ltd. For each contract, principles of revenue and cost recognition must be applied separately and net income will be determined for each asset as per AS 7.

Question 3 : May – 2019 – Paper / May – 2021 – RTP

(i) AP Ltd., a construction contractor, undertakes the construction of commercial complex for Kay Ltd. AP Ltd. submitted separate proposals for each of 3 units of commercial complex. A single agreement is entered into between the two parties. The agreement lays down

the value of each of the 3 units, i.e. Rs.50 Lakh Rs.60 Lakh and Rs.75 Lakh respectively. Agreement also lays down the completion time for each unit.
Comment, with reference to AS - 7, whether AP Ltd., should treat it as a single contract or three separate contracts.

(ii) On 1st December, 2017, GR Construction Co. Ltd. undertook a contract to construct a building for Rs.45 lakhs. On 31st March, 2018, the company found that it had already spent Rs.32.50 lakhs on the construction. Additional cost of completion is estimated at Rs.15.10 lakhs. What amount should be charged to revenue in the final accounts for the year ended 31st March, 2018 as per provisions of AS - 7 ?

Solution :

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

(a) separate proposals have been submitted for each asset;
(b) each asset has been subject to separate negotiation and the contractor and customer have been able to accept or reject that part of the contract relating to each asset; and
(c) the costs and revenues of each asset can be identified.

Therefore, Mr. AP Ltd. is required to treat construction of each unit as a separate construction contract as the above-mentioned conditions of AS 7 are fulfilled in the given case.

(ii)

	Rs. in lakhs
Cost of construction incurred till date	32.50
Add: Estimated future cost	15.10
Total estimated cost of construction	47.60

Percentage of completion till date to total estimated cost of construction
= (32.50/47.60) × 100 = 68.28%
Proportion of total contract value recognised as revenue for the year ended 31st March, 2018 per AS 7 (Revised)
= Contract price x percentage of completion
= Rs.45 lakh x 68.28% = Rs.30.73 lakhs.

	Rs. in lakhs
Total cost of construction	47.60
Less: Total contract price	(45.00)
Total foreseeable loss to be recognized as expense	2.60

According to of AS 7, when it is probable that total contract costs will exceed total contract revenue, the expected loss should be recognized as an expense immediately.

Question 4 : Nov – 2019 – RTP

On 1st December, 2018, "Sampath" Construction Company Limited undertook a contract to construct a building for Rs. 108 lakhs. On 31st March, 2019 the company found that it had already spent Rs. 83.99 lakhs on the construction. A prudent estimate of additional cost for completion was Rs. 36.01 lakhs.

You are required to compute the amount of provision for foreseeable loss, which must be made in the Final Accounts for the year ended 31st March, 2019 based on AS 7 "Accounting for Construction Contracts.

Solution :

Calculation of foreseeable loss for the year ended 31st March, 2019
(as per AS 7 "Construction Contracts")

	(Rs. In lakhs)
Cost incurred till 31st March, 2019	83.99
Prudent estimate of additional cost for completion	36.01
Total cost of construction	120.00
Less: Contract price	(108.00)
Foreseeable loss	12.00

According to para 35 of AS 7 (Revised 2002) "Construction Contracts", when it is probable that total contract costs will exceed total contract revenue; the expected loss should be recognized as an expense immediately. Therefore, amount of Rs.12 lakhs is required to be provided for in the books of Sampath Construction Company for the year ended 31st March, 2019.

Question 5 : May – 2020 – RTP

A construction contractor has a fixed price contract for Rs.9,000 lacs to build a bridge in 3 years time frame. A summary of some of the financial data is as under:

	(Amount Rs.in lacs)		
	Year 1	**Year 2**	**Year 3**
Initial Amount for revenue agreed in contract	9,000	9,000	9,000
Variation in Revenue (+)	-	200	200
Contracts costs incurred up to the reporting date	2,093	6,168*	8,100**
Estimated profit for whole contract	950	1,000	1,000

*Includes Rs. 100 lacs for standard materials stored at the site to be used in year 3 to complete the work.

**Excludes Rs. 100 lacs for standard material brought forward from year 2.

The variation in cost and revenue in year 2 has been approved by customer.

Compute year wise amount of revenue, expenses, contract cost to complete and profit or loss to be recognized in the Statement of Profit and Loss as per AS-7 (revised).

Solution :

The amounts of revenue, expenses and profit recognized in the statement of profit and loss in three years are computed below:

(Amount in Rs. lakhs)

	Up to the reporting date	Recognized in previous years	Recognized in current year
Year 1			
Revenue (9,000 x 26%)	2,340	-	2,340
Expenses (8,050 x 26%)	2,093	-	2,093
Profit	247	-	247
Year 2			
Revenue (9,200 x 74%)	6,808	2,340	4,468
Expenses (8,200 x 74%)	6,068	2,093	3,975
Profit	740	247	493
Year 3			
Revenue (9,200 x 100%)	9,200	6,808	2,392
Expenses (8,200 x 100%)	8,200	6,068	2,132
Profit	1,000	740	260

Working Note :

	Year 1	Year 2	Year 3
Revenue after considering variations	9,000	9,200	9,200
Less: Estimated profit for whole contract	950	1,000	1,000
Estimated total cost of the contract (A)	8,050	8,200	8,200
Actual cost incurred upto the reporting date (B)	2,093	6068 (6,168-100)	8200 (8,100+100)
Degree of completion (B/A)	26%	74%	100%

Question 6 : Nov – 2020 – RTP

Uday Constructions undertake to construct a·bridge for the Government of Uttar Pradesh. The construction commenced during the financial year ending 31.03.2019 and is likely to be completed by the next financial year. The contract is for a fixed price of Rs.12 crore with an escalation clause. You are given the following information for the year ended 31.03.2019:

Cost incurred upto 31.03.2019	Rs.4 crore
Further cost estimated to complete the contract	Rs.6 crore

Escalation in cost was by 5%. Hence, the contract price is also increased by 5%.

You are required to ascertain the stage of completion and compute the amount of revenue and profit to be recognized for the year as per AS 7.

Solution :

	Rs. in crore
Cost of construction of bridge incurred upto 31.3.2019	4.00
Add: Estimated future cost	6.00
Total estimated cost of construction	10.00
Contract Price (12 crore x 1.05)	12.60 crore

Stage of completion

Percentage of completion till date to total estimated cost of construction

= $(4/10) \times 100 = 40\%$

Revenue and Profit to be recognized for the year ended 31st March, 2019 as per AS 7:

Proportion of total contract value recognized as revenue

= Contract price x percentage of completion

= Rs. 12.60 crore x 40% = Rs. 5.04 crore

Profit for the year ended 31st March, 2019 = Rs. 5.04 crore – Rs. 4 crore = 1.04 crore.

Question 7 : Nov – 2020 – Paper

Rajendra undertook a contract for Rs. 20,00,000 on an arrangement that 80% of value of work done as certified by the architect of the contractee should be paid immediately and that remaining 20% be retained until the contract was completed.

In year 1 the amount expended were Rs.8,60,000 the work was certified for 8,00,000 and 80% of this was paid as agreed. It was estimated that future expenditure to complete the contract would be Rs. 10,00,000

In Year 2, the amounts were Rs. 4,75,000. Three-fourth of the contract was certified as done by December 31st and 80% of this was received accordingly it was estimated that future expenditure to complete the contract would be Rs. 4,00,000

In year 3 amount expended were Rs. 3,10,000 and on June 30th the whole contract was completed

Show how contract revenue would be recognized in the P & L account of Mr Rajendra every year

Solution :

Year 1	**Rs.**
Actual expenditure	8,60,000
Future estimated expenditure	10,00,000
Total Expenditure	18,60,000

% of work completed = $\frac{8,60,000}{18,60,000} \times 100$ = 46.24% (rounded off)

Revenue to be recognized = 20,00,000 x 46.24%

= Rs. 9,24,800

Year 2	
Actual expenditure	4,75,000
Future Expenditure	4,00,000
Expenditure incurred in Year 1	8,60,000
	17,35,000

% of work completed = $\frac{4,75,000 + 8,60,000}{17,35,000}$ = 76.95% (rounded off)

Revenue to be recognized (cumulative)	= 20,00,000 x 76.95%
	= 15,39,000
Less: revenue recognized in Year 1	= (9,24,800)
Revenue to be recognized in Year 2	Rs. 6,14,200

Year 3

Whole contract got completed therefore total contract value less revenue recognized up to year 2 will be amount of revenue to be recognized in year 3 i.e. 20,00,000 – 15,39,000 (9,24,800 + 6,14,200) = Rs. 4,61,000.

Note: Calendar year has been considered as accounting year.

Question 8 : May – 2021 – RTP

Sky Limited belongs to Heavy Engineering Contractors specializing in construction of Flyovers. The company just entered into a contract with a local municipal corporation for building a flyover. No activity has started on this contract.

As per the terms of the contract, Sky Limited will receive an additional Rs. 50 lakhs if the construction of the flyover were to be finished within a period of two years from the commencement of the contract. The Accountant of the entity wants to recognize this revenue since in the past the company has been able to meet similar targets very easily. Give your opinion on this treatment.

Solution :

According to AS 7 'Construction Contracts', incentive payments are additional amounts payable to the contractor if specified performance standards are met or exceeded. For example, a contract may allow for an incentive payment to the contractor for early completion of the contract. Incentive payments are included in contract revenue when both the conditions are met:

(i) the contract is sufficiently advanced that it is probable that the specified performance standards will be met or exceeded; and

(ii) the amount of the incentive payment can be measured reliably.

In the given problem, the contract has not even begun and hence the contractor (Sky Limited) should not recognize any revenue of this contract. Therefore, the accountant's contention for recognizing Rs.50 lakhs as revenue is not correct.

Question 9 : July – 2021 – Paper

The following data is provided for M/s. Raj Construction Co.

(i) Contract Price - Rs. 85 lakhs

(ii) Materials issued - Rs. 21 Lakhs out of which Materials costing Rs. 4 Lakhs is still lying unused at the end of the period.

(iii) Labour Expenses for workers engaged at site - Rs. 16 Lakhs (out of which Rs. 1 Lakh is still unpaid)

(iv) Specific Contract Costs - Rs. 5 Lakhs

(v) Sub-Contract Costs for work executed - Rs. 7 Lakhs, Advances paid to sub-contractors - Rs. 4 Lakhs

(vi) Further Cost estimated to be incurred to complete the contract - Rs. 35 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

	Rs. Lakh	Rs. 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
= Rs. 45,00,000/Rs. 80,00,000
= 56.25%

Contract revenue and costs to be recognized
Contract revenue (Rs. 85,00,000x56.25%) = Rs. 47,81,250
Contract costs = Rs. 45,00,000

Question 10 : Nov – 2021 – RTP

In the case of a fixed price contract, the outcome of a construction contract can be estimated reliably only when certain conditions prescribed under AS 7 are satisfied. You are required to describe these conditions mentioned in the standard.

Solution :

In the case of a fixed price contract, the outcome of a construction contract can be estimated reliably when all the following conditions are satisfied:

(i) total contract revenue can be measured reliably;

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

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

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

Question 11 : Nov – 2021 – RTP

Mr. 'X' as a contractor has just entered into a contract with a local municipal body for building a flyover. As per the contract terms, 'X' will receive an additional Rs. 2 crore if the construction of the flyover were to be finished within a period of two years of the commencement of the contract. Mr. X wants to recognize this revenue since in the past he has been able to meet similar targets very easily. Is X correct in his proposal? Discuss.

Solution :

According to AS 7 (Revised) 'Construction Contracts', incentive payments are additional amounts payable to the contractor if specified performance standards are met or exceeded. For example, a contract may allow for an incentive payment to the contractor for early completion of the contract. Incentive payments are included in contract revenue when: (i) the contract is sufficiently advanced that it is probable that the specified performance standards will be met or exceeded; and (ii) the amount of the incentive payment can be measured reliably. In the given problem, the contract has not even begun and hence the contractor (Mr. X) should not recognize any revenue of this contract.

Question 12 : May – 2022 – RTP

B Ltd. undertook a construction contract for Rs. 50 crores in April, 2020. The cost of construction was initially estimated at Rs. 35 crores. The contract is to be completed in 3 years. While executing the contract, the company estimated that the cost of completion of the contract would be Rs. 53 crores.

Can the company provide for the expected loss in the financial Statements for the year ended 31st March, 2021? Explain.

Solution :

As per para 35 of AS 7 "Construction Contracts", when it is probable that total contract costs will exceed total contract revenue, the expected loss should be recognized as an expense immediately. Therefore, the foreseeable loss of Rs. 3 crores (Rs. 53 crores less Rs. 50 crores) should be recognized as an expense immediately in the year ended 31st March, 2021. The amount of loss is determined irrespective of

(i) Whether or not work has commenced on the contract;

(ii) Stage of completion of contract activity; or

(iii) The amount of profits expected to arise on other contracts which are not treated as a single construction contract in accordance provisions of AS 7.

Question 13 : May – 2022 – Paper

Grace Ltd., a firm of contractors provided the following information in respect of a contract for the year ended on 31st March, 2022 :

Particulars	(Rs. in '000)
Fixed Contract Price with an escalation clause	35,000
Work Certified	17,500
Work not Certified (includes Rs.26,25,000 for materials issued, out of which material lying unused at the end of the period is Rs.1,40,000)	3,815
Estimated further cost to completion	17,325
Progress Payment Received	14,000
Payment to be Received	4,900
Escalation in cost is by 8% and accordingly the contract price is increased by 8%	-

From the above information, you are required to :

(i) Compute the contract revenue to be recognised,

(ii) Calculate Profit / Loss for the year ended 31st March, 2022 and additional provision for loss to be made, if any, for the year ended 31st March, 2022.

Solution :

		Rs. in thousand
Cost of Contract incurred till date		
Work certified	17,500	
Work not certified (3,815 thousand – 140 thousand)	3,675	21,175
Add: Estimated future cost		17,325
Total estimated cost of construction		38,500
Contract Price (35,000 thousand x 1.08)		37,800

Stage of completion

Percentage of completion till date to total estimated cost of construction = [Cost of work completed till date / total estimated cost of the contract] x 100

= [Rs. 21,175 thousand / Rs. 38,500 thousand] x 100= 55%

Revenue to be recognized for the year ended 31stMarch, 2022

Proportion of total contract value recognized as revenue = Contract price x percentage of completion = Rs. 37,800 thousand x 55% = Rs. 20,790 thousand

Loss to be recognized for the year ended 31stMarch, 2022

Loss for the year ended 31stMarch, 2022 = Cost incurred till date – Revenue to be recognized for the year ended 31st March, 2022

= Rs. 21,175 thousand – Rs. 20,790 thousand = Rs. 385 thousand

Provision for loss to be made at the end of 31stMarch, 2022

		Rs. in thousand
Total estimated loss on the contract		
Total estimated cost of the contract	38,500	
Less: Total revised contract price	(37,800)	700
Less: Loss recognized for the year ended 31st March, 2022		(385)
Provision for loss to be made at the end of 31stMarch, 2022		315

Question 14 : Nov – 2022 – RTP

On 1st December, 2020, "Sampath" Construction Limited undertook a contract to construct a building for Rs. 108 lakhs. On 31st March, 2021 the company found that it had already spent Rs. 83.99 lakhs on the construction. A prudent estimate of additional cost for completion was Rs. 36.01 lakhs.

You are required to compute the amount of provision for foreseeable loss, which must be made in the Final Accounts for the year ended 31st March, 2021 based on AS 7 "Accounting for Construction Contracts."

Solution :

Calculation of foreseeable loss for the year ended 31st March, 2021
(as per AS 7 "Construction Contracts")

	(Rs. in lakhs)
Cost incurred till 31st March, 2021	83.99
Prudent estimate of additional cost for completion	36.01
Total cost of construction	120.00
Less: Contract price	(108.00)
Foreseeable loss	12.00

According to AS 7 (Revised 2002) "Construction Contracts", when it is probable that total contract costs will exceed total contract revenue; the expected loss should be recognized as an expense immediately. Therefore, amount of Rs.12 lakhs is required to be provided for in the books of Sampath Construction Ltd. for the year ended 31st March, 2021.

Thanks ....

CHAPTER 4

AS 9 REVENUE RECOGNITION

Question 1 : May – 2019 – RTP

Raj Ltd. entered into an agreement with Heena Ltd. to dispatch goods valuing Rs. 5,00,000 every month for next 6 months on receipt of entire payment. Heena Ltd. accordingly made the entire payment of Rs. 30,00,000 and Raj Ltd. started dispatching the goods. In fourth month, due to fire in premise of Heena Ltd., Heena Ltd. requested to Raj Ltd. not to dispatch goods worth Rs. 15,00,000 ready for dispatch. Raj Ltd. accounted Rs. 15,00,000 as sales and transferred the balance to Advance received against Sales account.

Comment upon the above treatment by Raj Ltd. with reference to the provision of AS-9.

Solution :

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

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

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

In the given case, transfer of property in goods results in or coincides with the transfer of significant risks and rewards of ownership to the buyer. Also, the sale price has been recovered by the seller. Hence, the sale is complete but delivery has been postponed at buyer's request. Raj Ltd. should recognize the entire sale of Rs. 30,00,000 (Rs. 5,00,000 x 6) and no part of the same is to be treated as Advance Received against Sales.

Question 2 : May – 2019 – Paper

Given below are the following informations of B.S. Ltd.

(i) Goods of Rs.50,000 were sold on 18-03-2018 but at the request of the buyer these were delivered on 15-04-2018.

(ii) On 13-01-2018 goods of Rs.1,25,000 are sent on consignment basis of which 20% of the goods unsold are lying with the consignee as on 31-03-2018.

(iii) Rs.1,00,000 worth of goods were sold on approval basis on 01-12-2017. The period of approval was 3 months after which they were considered sold. Buyer sent approval for 75% goods up to 31-01-2018 and no approval or disapproval received for the remaining goods till 31-03-2018.

You are required to advise the accountant of B.S. Ltd., with valid reasons, the amount to be recognized as revenue for the year ended 31st March, 2018 in above cases in the context of AS - 9.

Solution :

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

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

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

Case (i)

The sale is complete but delivery has been postponed at buyer's request. B.S. Ltd. should recognize the entire sale of Rs.50,000 for the year ended 31st March, 2018.

Case (ii)

In case of consignment sale revenue should not be recognized until the goods are sold to a third party. 20% goods lying unsold with consignee should be treated as closing inventory and sales should be recognized for Rs.1,00,000 (80% of Rs.1,25,000).

Case (iii)

In case of goods sold on approval basis, revenue should not be recognized until the goods have been formally accepted by the buyer or the buyer has done an act adopting the transaction or the time period for rejection has elapsed or where no time has been fixed, a reasonable time has elapsed. Therefore, revenue should be recognized for the total sales amounting Rs.1,00,000 as the time period for rejecting the goods had expired.

Thus total revenue amounting Rs.2,50,000 (50,000 + 1,00,000+ 1,00,000) will be recognized for the year ended 31st March, 2018 in the books of B.S. Ltd.

Question 3 : Nov – 2019 – RTP

The Board of Directors decided on 31.3.2019 to increase the sale price of certain items retrospectively from 1st January, 2019. In view of this price revision with effect from 1st January 2019, the company has to receive Rs.15 lakhs from its customers in respect of sales made from 1st January, 2019 to 31st March, 2019. Accountant cannot make up his mind whether to include Rs.15 lakhs in the sales for 2018-2019. Advise.

Solution :

Price revision was effected during the current accounting period 2018-2019. As a result, the company stands to receive Rs. 15 lakhs from its customers in respect of sales made from 1st January, 2019 to 31st March, 2019. If the company is able to assess the ultimate collection with reasonable certainty, then additional revenue arising out of the said price revision may be recognised in 2018-2019 vide para 10 of AS 9.

Question 4 : Nov – 2019 – Paper

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 5 : May – 2020 – RTP

The following information of Meghna Ltd. is provided:

(i) Goods of Rs. 60,000 were sold on 20-3-2019 but at the request of the buyer these were delivered on 10-4-2019.
(ii) On 15-1-2019 goods of Rs. 1,50,000 were sent on consignment basis of which 20% of the goods unsold are lying with the consignee as on 31-3-2019.
(iii) Rs. 1,20,000 worth of goods were sold on approval basis on 1-12-2018. The period of approval was 3 months after which they were considered sold. Buyer sent approval for 75% goods up to 31-1-2019 and no approval or disapproval received for the remaining goods till 31-3-2019.
(iv) Apart from the above, the company has made cash sales of Rs. 7,80,000 (gross). Trade discount of 5% was allowed on the cash sales.

You are required to advise the accountant of Meghna Ltd., with valid reasons, the amount to be recognized as revenue in above cases in the context of AS-9.

Solution :

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

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

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

Case (i)

The sale is complete but delivery has been postponed at buyer's request. M/s Paper Products Ltd. should recognize the entire sale of Rs. 60,000 for the year ended 31st March, 2019.

Case (ii)

20% goods lying unsold with consignee should be treated as closing inventory and sales should be recognized for Rs. 1,20,000 (80% of Rs. 1,50,000). 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 Rs. 1,20,000 as the time period for rejecting the goods had expired.

Case (iv)

Trade discounts given should be deducted in determining revenue. Thus Rs. 39,000 should be deducted from the amount of turnover of Rs. 7,80,000 for the purpose of recognition of revenue. Thus, revenue should be Rs. 7,41,000.

Question 6 : Nov – 2020 – RTP

Fashion Limited is engaged in manufacturing of readymade garments. They provide you the following information on 31st March, 2019:

(i) On 15th January, 2019 garments worth Rs. 4,00,000 were sent to Anand on consignment basis of which 25% garments unsold were lying with Anand as on 31st March, 2019.

(ii) Garments worth Rs. 1,95,000 were sold to Shine boutique on 25th March, 2019 but at the request of Shine Boutique, these were delivered on 15th April, 2019.

You are required to advise the accountant of Fashion Limited, the amount to be recognised as revenue in above cases in the context of AS 9.

Solution :

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

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

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

Case (i) :

25% goods lying unsold with consignee should be treated as closing inventory and sales should be recognized for Rs. 3,00,000 (75% of Rs. 4,00,000) for the year ended on 31.3.19. In case of consignment sale revenue should not be recognized until the goods are sold to a third party.

Case (ii) :

The sale is complete but delivery has been postponed at buyer's request. Fashion Ltd. should recognize the entire sale of Rs.1,95,000 for the year ended 31st March, 2019.

Question 7 : May – 2021 – RTP

Tonk Tanners is engaged in manufacturing of leather shoes. They provide you the following information for the year ended 31st March,2020:

(i) On 31st December, 2019 shoes worth Rs. 3,20,000 were sent to Mohan Shoes for sale on consignment basis of which 25% shoes were unsold and lying with Mohan Shoes as on 31st March, 2020.

(ii) On 10th January, 2020, Tonk Tanner supplied shoes worth Rs. 4,50,000 to Shani Shoes and concurrently agrees to re-purchase the same goods on 11th April. 2020.

(iii) On 21st March, 2020 shoes worth Rs. 1,60,000 were sold to Shoe Shine but due to refurbishing of their showroom being underway, on their request, shoes were delivered on 12th April, 2020.

You are required to advise the accountant of Tonk Tanners, when amount is to be recognised as revenue in 2019 -20 in above cases in the context of AS 9.

Solution :

(i) Shoes sent to Mohan Shoes (consignee) for consignment sale

In case goods are sent for consignment sale, revenue is recognized when significant risks of ownership have passed from seller to the buyer.

In the given case, Mohan Shoes is the consignee i.e. an agent of Tonk Tanners and not the buyer. Therefore, the risk and reward is considered to vest with Tonk Tanners only till the time the sale is made to the third party by Mohan Shoes; although the goods are held by Mohan Shoes. Hence, in the year 2019-2020, the sale will be recognized for the amount of goods sold by Mohan Shoes to the third party i.e. for Rs. 3,20,000 x 75% = Rs. 2,40,000.

(ii) Sale/repurchase agreements i.e. where seller concurrently agrees to repurchase the same goods at a later date

For such transactions that are in substance a financing agreement, the resulting cash inflow is not revenue and should not be recognised as revenue in the year 2019-2020. Hence, sale of Rs. 4,50,000 to Shani Shoes should not be recognized as revenue.

(iii) Delivery is delayed at buyer's request

On 21st March, 2020, if Shoe Shine takes title and accepts billing for the goods then it is implied that the sale is complete and all the risk and rewards of ownership has been transferred to the buyer. In case no significant uncertainty exists regarding the amount of consideration for sale, revenue shall be recognized in the year 2019-2020 irrespective of the fact that the delivery is delayed on the request of Shoe Shine.

Question 8 : July – 2021 – Paper

A Limited sells goods with unlimited right of return from its customers.
The following pattern has been observed in the Return of Sales:

Time frame of Return from date of purchase	% of Cumulative Sales
Between 0-1 month	6%
Between 1-2 months	7%
Between 2-3 months	8%

The Company has made Sales of Rs. 36 Lakhs in the month of January, Rs. 48 Lakhs in the month of February and of Rs. 60 Lakhs in the month of March. The Total Sales for the Financial Year have been Rs. 400 Lakhs and the Cost of Sales was Rs. 320 Lakhs. You are required to determine the amount of Provision to be made and Revenue to be recognized for the year ended 31st March.

Solution :

Amount of provision

The goods are sold with a right to return. The existence of such right gives rise to a present obligation on the company as per AS 29, 'Provisions, Contingent Liabilities and Contingent Assets'. According to the standard, a provision should be created on the Balance sheet date, for sales returns after the Balance Sheet date, at the best estimate of the loss expected, along with any estimated incremental cost that would be necessary to resell the goods expected to be returned.

Sales during	Sales value (Rs. in lacs)	Sales value (cumulative) Rs. (in lacs)	Likely returns (%)	Likely returns Rs. (in lacs)	Provision @ 20% (Rs. in lacs) (Refer W.N.)
March	60	60	6%	3.60	0.720
February	48	108	7%	7.56	1.512
January	36	144	8%	11.52	2.304
Total				22.68	4.536

Revenue to be recognized

Revenue in respect of sale of goods is recognized fully at the time of sale itself assuming that the company has complied with the conditions stated in AS 9 relating to recognition of revenue in the case of sale of goods. As per AS 9, in a transaction involving the sale of goods, performance should be regarded as being achieved when the following conditions have been fulfilled:

(i) 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. AS 9 also provides that in case of retail sales offering a guarantee of 'money back, if not completely satisfied, it may be appropriate to recognize the sale but to make a suitable provision for returns based on previous experiences.

Therefore, sale of Rs. 36 lakhs, Rs. 48 lakhs and Rs. 60 lakhs made in the months of January, February and March will be recognized at full value. Thus, total revenue to be recognized for Rs. 400 lacs for the year.

Working Note:

Calculation of Profit % on sales

	(Rs. in lacs)
Sales for the year	400
Less: Cost of sales	(320)
Profit	80
Profit mark up on sales (80/400) x 100 = 20%	

Question 9 : Nov – 2021 – RTP

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 10 : Nov – 2021 – RTP

Shipra Ltd., has been successful jewellers for the past 100 years and sales are against cash only (returns are negligible). The company also diversified into apparels. A young senior executive was put in charge of Apparels business and sales increased 5 times. One of the conditions for sales is that dealers can return the unsold stocks within one month of the end of season. Sales return for the year was 25% of sales. Suggest a suitable Revenue Recognition Policy, with reference to AS 9.

Solution :

As per AS 9 "Revenue recognition", revenue recognition is mainly concerned with the timing of recognition of revenue in statement of profit and loss of an enterprise. The amount of revenue arising on a transaction is usually determined by the agreement between the parties involved in the transaction. When uncertainties exist regarding the determination of the amount, or its associated costs, these uncertainties may influence the timing of revenue recognition.

Effect of Uncertainty- In the case of the jewellery business the company is selling for cash and returns are negligible. Hence, revenue can be recognized on sales. On the other hand, in Apparels Industry, the dealers have a right to return the unsold goods within one month of the end of the season. In this case, the company is bearing the risk of sales return and therefore, the company should not recognize the revenue to the extent of 25% of its sales. The company may disclose suitable revenue recognition policy in its financial statements separately for both Jewellery and Apparels business.

Question 11 : Dec – 2021 – Paper

Given the following information of Rainbow Ltd. :

(i) On 15th November, goods worth Rs.5,00,000 were sold on approval basis. The period of approval was 4 months after which they were considered sold. Buyer sent approval for 75% goods sold upto 31st January and no approval or disapproval received for the remaining goods till 31st March.

(ii) On 31st March, goods worth Rs.2,40,000 were sold to Bright Ltd. but due to refurnishing of their show-room being underway, on their request, goods were delivered on 10th April.

(iii) Rainbow Ltd. supplied goods worth Rs.6,00,000 to Shyam Ltd. and concurrently agrees to re-purchase the same goods on 14th April.

(iv) Dew Ltd. used certain assets of Rainbow Ltd. Rainbow Ltd. received Rs.7.5 lakhs and Rs.12 lakhs as interest and royalties respectively from Dew Ltd. during the year 2020-21.

(v) On 25th December goods of Rs.4,00,000 were sent on consignment basis of which 40% of the goods unsold are lying with the consignee at the year end on 31st March.

In each of the above cases, you are required to advise, with valid reasons, the amount to be recognized as revenue under the provisions of AS-9.

Solution :

(i) As per AS 9 "Revenue Recognition", in case of goods sold on approval basis, revenue should not be recognized until the goods have been formally accepted by the buyer or the buyer has done an act adopting the transaction or the time period for rejection has elapsed or where no time has been fixed, a reasonable time has elapsed. Therefore, revenue should be recognized for the total sales amounting Rs. 5,00,000 as the time period for rejecting the goods had expired.

(ii) The sale is complete but delivery has been postponed at buyer's request. The entity should recognize the entire sale of Rs. 2,40,000 for the year ended 31st March.

(iii) Sale/repurchase agreements i.e. where seller concurrently agrees to repurchase the same goods at a later date, such transactions that are in substance a financing agreement, the

resulting cash inflow is not revenue as defined and should not be recognized as revenue. Hence no revenue to be recognized in the given case.

(iv) Revenue arising from the use by others of enterprise resources yielding interest and royalty should be recognized when no significant uncertainty as to measurability or collectability exists. The interest should be recognized on time proportion basis taking into account the amount outstanding and rate applicable. The royalty should be recognized on accrual basis in accordance with the terms of relevant agreement.

(v) 40% goods lying unsold with consignee should be treated as closing inventory and sales should be recognized for Rs. 2,40,000 (60% of Rs. 4,00,000). In case of consignment sale revenue should not be recognized until the goods are sold to a third party.

Question 12 : May – 2022 – RTP

An infrastructure company has constructed a mall and entered into agreement with tenants towards license fee (monthly rental) and variable license fee, a percentage on the turnover of the tenant (on an annual basis). Chief Financial Officer of the company wants to account/recognize license fee as income for 12 months during current year and variable license fee as income during next year, since invoice is raised in the subsequent year. Comment whether the treatment desired by the CFO is correct or not.

Solution :

AS 9 on Revenue Recognition, is mainly concerned with the timing of recognition of revenue in the Statement of Profit and Loss of an enterprise. The amount of revenue arising on a transaction is usually determined by agreement between the parties involved in the transaction. However, when uncertainties exist regarding the determination of the amount, or its associated costs, these uncertainties may influence the timing of revenue recognition. Further, as per accrual concept, revenue should be recognized as and when it is accrued i.e. recorded in the financial statements of the periods to which they relate. In the present case, monthly rental towards license fee and variable license fee as a percentage on the turnover of the tenant (though on annual basis) is the income related to common financial year.

Therefore, recognizing the fee as revenue cannot be deferred simply because the invoice is raised in subsequent period. Hence it should be recognized in the financial year of accrual. Therefore, the contention of the Chief Financial Officer is not in accordance with AS 9.

Question 13 : May – 2022 – RTP

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.

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 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.

Question 14 : Nov – 2022 – RTP

When revenue will be recognized in the following situation:

(i) Where the purchaser makes a series of installment payments to the seller and the seller deliver the goods only when the final payment is received.

(ii) Where seller concurrently agrees to repurchase the same goods at a later date.

(iii) Where goods are sold to distributors, dealers or others for resale.

(iv) Commissions on service rendered as agent on insurance business.

Solution :

(i) Revenue from sales where the purchaser makes a series of instalment payments to the seller, and the seller delivers the goods only when the final payment is received, should not be recognised until goods are delivered. However, when experience indicates that most such sales have been consummated, revenue may be recognised when a significant deposit is received.

(ii) For sale where seller concurrently agrees to repurchase the same goods at a later date, such transactions are in substance a financing agreement. In such a situation, the resulting cash inflow should not be recognised as revenue.

(iii) Revenue from sales of goods to distributors, dealers or others for resale can generally be recognised 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.

(iv) Commissions on service rendered as agent on insurance business should be recognised as revenue when the service is completed. Insurance agency commissions should be recognised on the effective commencement or renewal dates of the related policies.

Question 15 : Nov – 2022 – Paper

Indicate in each case whether revenue can be recognized and when it will be recognized as per AS - 9.

(i) Delivery is delayed at buyer's request but buyer takes title and accepts billing.

(ii) Instalment Sales.

(iii) Trade discounts and volume rebates.

(iv) Insurance agency commission for rendering services.

(v) Advertising commission.

Thanks ….

Rahul Malkan

CHAPTER 5

AS 17 SEGMENT REPORTING

Question 1 : May – 2020 – RTP / Jan – 2021 – Paper

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 2 : Nov – 2020 – RTP / May – 2021 – RTP

A Company has an inter-segment transfer pricing policy of charging at cost less 5%. The market prices are generally 20% above cost. You are required to examine whether the policy adopted by the company for pricing inter-segment transfers at reduced prices is correct or not in line with the provisions of AS 17?

Solution :

AS 17 'Segment Reporting' requires that inter-segment transfers should be measured on the basis that the enterprise actually used to price these transfers. The basis of pricing inter-segment transfers and any change therein should be disclosed in the financial statements. Hence, the enterprise can have its own policy for pricing inter-segment transfers and hence, inter-segment transfers may be based on cost, below cost or market price. However, whichever policy is followed, the same should be disclosed and applied consistently. Therefore, in the given case inter-segment transfer pricing policy adopted by the company is correct if followed consistently.

Question 3 : Nov – 2020 – Paper

The accountant of Parag Ltd has furnished you with the following data related to its Business Division

(Rs. In lacs)

Division	A	B	C	D	Total
Segment Revenue	100	300	200	400	1000
Segment Result	45	-70	80	-10	45
Segment Assets	39	51	48	12	150

You requested to identify the reportable segments in accordance with the criteria laid down in AS 17.

Solution :

As per AS 17 'Segment Reporting', a business segment or geographical segment should be identified as a reportable segment if:

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 Its segment result whether profit or loss is 10% or more of:

- The combined result of all segments in profit; or
- The combined result of all segments in loss,

whichever is greater in absolute amount; or

Its segment assets are 10% or more of the total assets of all segments.

On the basis of revenue criteria, segments A, B, C and D - all are reportable segments.

On the basis of the result criteria, segments A, B and C are reportable segments (since their results in absolute amount is 10% or more of 125 Lakhs).

On the basis of asset criteria, all segments except D are reportable segments.

Since all the segments are covered in at least one of the above criteria, all segments have to be reported upon in accordance with Accounting Standard (AS) 17.

Question 4 : Nov – 2021 – RTP

Company A is engaged in the manufacture of chemicals. The company manufactures five types of chemicals that have different applications. Can this company include more than one type of chemical in a single business segment? Comment.

Solution :

As per AS 17, "A business segment is a distinguishable component of an enterprise that is engaged in providing an individual product or service or a group of related products of services and that is subject to risks and returns that are different from those of other business segments. Factors that should be considered in determining whether products or services are related include:

(a) the nature of the products of services;
(b) the nature of the productions processes;
(c) the type of class of customers for the products or services;
(d) the methods use to distribute the products or provide the services; and
(e) if applicable, the nature of the regulatory environment, for example, banking, insurance, or public utilities."

As per provisions of the standard, a single business segment does not include products and services with significantly differing risks and returns. Products and services included in a single business segment may be dissimilar with respect to one or several factors listed above but are expected to be similar with respect to majority of the factors.

In the present case, the Company should consider whether the chemicals with different applications, have similar risks end returns. For this purpose, the Company should ascertain whether one or more types of chemicals are related keeping in view the relevant factors including those given in the definition of business segment. Chemicals having different applications can be included in a single business segment if majority of the relevant factors including those listed above are similar. This would ensure that the chemicals having significantly different risks and returns are not included in a single business segment.

Question 5 : Nov – 2021 – RTP

Is an enterprise required to disclose changes in the basis of allocation of revenue and expenses to segments? Explain.

Solution :

As per AS 17, "Changes in accounting policies adopted for segment reporting that have a material effect on segment information should be disclosed. Such disclosure should include a description of the nature of the change, and the financial effect of the change if it is reasonably determinable." It also states that "some changes in accounting policies relate specifically to segment reporting. Examples include changes in identification of segments and changes in the basis for allocating revenues and expenses to segments. Such changes can have a significant impact on the segment information reported but will not change aggregate financial information reported for the enterprise. To enable users to understand and impact of such changes, this Statement requires the disclosure of the nature of change and the financial effect of the change, if reasonably determinable".

In view of the above, a change in the basis of allocation of revenue and expenses to segments is a change in the accounting policy adopted for segment reporting. Accordingly, if the change has a material financial effect on the segment information, a description of the nature of the change, and the financial effect of the change, if it is reasonably determinable, should be disclosed.

Question 6 : May – 2022 – RTP

Company A is engaged in the manufacture and sale of products, which constitute two distinct business segments. The products of the Company are sold in the domestic market only. The management information system of the Company is organized to reflect operating information by two broad market segments, rural and urban. Besides the two business segments, how should Company A identify geographical segments? Do geographical segments exist within the same country? Explain in line with the provisions of AS 17.

Solution :

AS 17 explains that, "a single geographical segment does not include operations in economic environments with significantly differing risks and returns. A geographical segment may be a single country, a group of two or more countries, or a region within a country". Accordingly, to identity geographical segments, Company A needs to evaluate whether the segments reflected in the management information system function in environments that are subject to significantly differing risks and returns irrespective of the fact whether they are within the same country.

The Standard recognizes that, "Determining the composition of a business or geographical segment involves a certain amount of judgement…". Accordingly, while the management information system of the Company provides segment information for rural and urban geographical segments for the purpose of internal reporting, judgement is required to determine whether these segments are subject to significantly differing risks and returns based on the definition of geographical segment. In making such a judgement, aspect like different pricing and other policies, e.g., credit policies, deployment of resources between different regions etc., may be considered for the purpose identifying 'urban and 'rural' as separate geographical segment.

Company A, in making judgment for identifying geographical segments, should also consider the relevance, reliability and comparability over time of segment information that will be reported. The Standard, explains that, "In making that judgement, enterprise management takes into account the objective of reporting financial information by segment as set forth in the standard and the qualitative characteristics of financial statements. The qualitative characteristics include the relevance, reliability and comparability over time of financial information that is reported about the different groups of products and services of an enterprise and about its operations in particular geographical areas, and the usefulness of that information for assessing the risks and returns of the enterprise."

Question 7 : May – 2022 – RTP

A Company has an inter-segment transfer pricing policy of charging at cost less 10%. The market prices are generally 20% above cost. You are required to examine whether the policy adopted by the company is correct or not?

Solution :

AS 17 'Segment Reporting' requires that inter-segment transfers should be measured on the basis that the enterprise actually used to price these transfers. The basis of pricing inter-segment transfers and any change therein should be disclosed in the financial statements. Hence, the enterprise can have its own policy for pricing inter-segment transfers and hence, inter-segment transfers may be based on cost, below cost or market price. However, whichever policy is followed, the same should be disclosed and applied consistently. Therefore, in the given case inter-segment transfer pricing policy adopted by the company is correct if followed consistently.

Question 8 : May – 2022 – Paper

XYZ Ltd. has 5 business segments. Profit / Loss of each of the segments for the year ended 31st March, 2022 has been provided below. You are required to identify from the following whether reportable segments or not reportable segments, on the basis of "profitability test" as per AS-17.

Segment	Profit (Loss) Rs. in lakhs
A	225
B	25
C	(175)
D	(20)
E	(105)

Solution :

As per AS 17 'Segment Reporting', a business segment or geographical segment should be identified as a reportable segment if:

Its segment results whether profit or loss is 10% or more of:

- The combined result of all segments in profit; i.e. Rs. 250 Lakhs or
- The combined result of all segments in loss; i.e. Rs. 300 Lakhs

Whichever is greater in absolute amount i.e. Rs. 300 Lakhs.

Operating Segment	Absolute amount of Profit or Loss (Rs. In lakhs)	Reportable Segment Yes or No
A	225	Yes
B	25	No
C	175	Yes
D	20	No
E	105	Yes

On the basis of the profitability test (result criteria), segments A, C and E are reportable segments (since their results in absolute amount is 10% or more of Rs. 300 lakhs i.e. 30 lakhs).

Question 9 : Nov – 2022 – RTP

A Company has an inter-segment transfer pricing policy of charging at cost less 10%. The market prices are generally 25% above cost. Is the policy adopted by the company correct?

Solution :

AS 17 'Segment Reporting' requires that inter-segment transfers should be measured on the basis that the enterprise actually used to price these transfers. The basis of pricing inter-segment transfers and any change therein should be disclosed in the financial statements. Hence, the enterprise can have its own policy for pricing inter-segment transfers and hence, inter-segment transfers may be based on cost, below cost or market price. However, whichever policy is followed, the same should be disclosed and applied consistently. Therefore, in the given case inter-segment transfer pricing policy adopted by the company is correct if, followed consistently.

Thanks ....

CHAPTER 6

AS 18 RELATED PARTY TRANSACTIONS

Question 1 : Nov – 2018 – Paper

Following transactions are disclosed as on 31st March, 2018:

(i) Mr. Sumit, a relative of Managing Director, received remuneration of Rs. 2,10,000 for his services in the company for the period from 1st April, 2017 to 30th June, 2017. He left the service on 1st July, 2017.

Should the relative be identified as a related party as on closing date i.e. on 31-3-2018 for the purpose of AS-18.

(ii) Goods sold amounting to Rs. 50 lakhs to associate company during the 1st quarter ended on 30th June, 2017. After that related party relationship ceased to exist. However, goods were supplied as was supplied to any other ordinary customer.

Decide whether transactions of the entire year have to be disclosed as related party transactions.

Solution :

(i) According to AS 18 'Related Party Disclosures', parties are considered to be related if at any time during the reporting period, one party has the ability to control the other party or exercise significant influence over the other party in making financial and/or operating decisions.

Hence, Mr. Sumit a relative of key management personnel should be identified as related party as at the closing date i.e. on 31.3.2018 as he received remuneration forhis services in the company from1st April, 2017 to 30th June, 2017and this period comes under the reporting period.

(ii) As per provision of AS 18, the transactions only for the period in which related party relationships exist need to be reported.

Hence, transactions of the entity with its associate company for the first quarter ending 30.06.2017 only are required to be disclosed as related party transactions. Transactions of the entire year need not be disclosed as related party transactions and transactions for the period (after 1st July) in which related party relationship did not exist need not be reported.

Hence transaction of sale of goods with the associate company for first quarter ending 30th June, 2017 for Rs. 50 Lakhs only are required to be disclosed as related party transaction on 31.3.18

Question 2 : May – 2019 – RTP / Nov – 2019 - RTP

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 example, 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 3 : May – 2019 – Paper

Identify the related parties in the following cases as per AS - 18

(i) Maya Ltd. holds 61 % shares of Sheetal Ltd.
Sheetal Ltd. holds 51 % shares of Fair Ltd.
Care Ltd. holds 49% shares of Fair Ltd.
(Give your answer - Reporting Entity wise for Maya Ltd., Sheetal Ltd., Care Ltd. and Fair Ltd.)

(ii) Mr. Subhash Kumar is Managing Director of A Ltd. and also holds 72% capital of B Ltd.

Solution :

(i) (a) Reporting entity - Maya Ltd.
- Sheetal Ltd. (subsidiary) is a related party
- Fair Ltd.(subsidiary) is a related party

(b) Reporting entity - Sheetal Ltd.
- Maya Ltd. (holding company) is a related party
- Fair Ltd. (subsidiary) is a related party

(c) Reporting entity - Fair Ltd.
- Maya Ltd. (holding company) is a related party
- Sheetal Ltd. (holding company) is a related party
- Care Ltd. (investor/ investing party) is a related party

(d) Reporting entity - Care Ltd.
- Fair Ltd. (associate) is a related party

(ii) Mr. Subhash Kumar is Key management personnel as he has the authority for planning, directing and controlling the activities of A Ltd. He also holds substantial interest in B Ltd. as he holds 72% capital of B Ltd. Thus, Mr. Subhash is related party for both A Ltd. and B

Ltd. Moreover, as per the definition of related party relationship described in para 3 of AS 18, enterprises over which Subhash is able to exercise significant influence are also related parties. Thus, a Ltd. and B Ltd. will also be construed as related to each other.

Question 4 : May – 2020 – RTP

Arohi Ltd. sold goods for Rs.90 lakhs to Anya Ltd. during financial year ended31-3-2019. The Managing Director of Arohi Ltd. own 100% of Anya Ltd. The sales were made to Anya Ltd. at normal selling prices followed by Arohi Ltd. The Chief accountant of Arohi Ltd contends that these sales need not require a different treatment from the other sales made by the company and hence no disclosure is necessary as per the accounting standard. Is the Chief Accountant correct? Comment in accordance with AS 18.

Solution :

As per AS 18 'Related Party Disclosures', Enterprises over which the key management personnel is able to exercise significant influence are related parties. This includes enterprises owned by directors or major shareholders of the reporting enterprise that have a member of key management in common with the reporting enterprise. In the given case, Arohi Ltd. and Anya Ltd. are related parties and hence disclosure of transaction between them is required irrespective of whether the transaction was done at normal selling price. Hence the contention of Chief Accountant of Arohi Ltd. is wrong.

Question 5 : Nov – 2020 – RTP

On the basis of provisions of AS 18 'Related Party Disclosures':

(i) Identify the related parties in the following cases:
X Limited holds 60% shares of Y Limited
Y Limited holds 55% shares of W Limited
Z Limited holds 35% shares of W Limited

(ii) Himalaya Limited sold goods for Rs.40 Lakhs to Aravalli Limited during financial year ended on March 31, 2019. The Managing Director of Himalaya Limited owns 80% shares of Aravalli Limited. The sales were made to Aravalli Limited at normal selling prices followed by Himalaya Limited. The chief accountant of Himalaya Limited contends that these sales need not require a different treatment from the other sales made by the company and hence no disclosure is necessary as per AS 18. You are required to comment on this.

Solution :

(i) X Ltd., Y Ltd. & W Ltd. are related to each other. Z Ltd. & W Ltd. are related to each other by virtue of associate relationship. However, neither X Ltd. nor Y Ltd. is related to Z Ltd. and vice versa since neither control nor significant influence exists between them.

(ii) Himalaya Ltd. and Aravalli Ltd are related parties since key management personnel of Himalaya Ltd. i.e. its managing director holds 80% in Aravalli Ltd. and hence disclosure of transaction between them is required irrespective of whether the transaction was done at normal selling price. Hence the contention of Chief Accountant of Himalaya Ltd that these sales require no disclosure under related party transactions, is wrong.

Question 6 : May – 2021 – RTP

R Ltd. has 60% voting right in S Ltd. S Ltd. has 15% voting right in T Ltd. R Ltd. directly enjoys voting right of 10% in T Ltd. T Ltd. is a listed company and regularly supplies goods to R Ltd. The management of T Ltd. has not disclosed its relationship with R Ltd. You are required to assess the situation from the view point of AS 18 on Related Party Disclosures.

Solution :

AS 18 'Related Party Disclosures', defines related party as one that has at any time during the reporting period, the ability to control the other party or exercise significant influence over the other party in making financial and/or operating decisions.

Definition for Control

Here, control is defined as ownership directly or indirectly of more than one-half of the voting power of an enterprise; and Significant Influence is defined as participation in the financial and/or operating policy decisions of an enterprise but not control of those policies.

Nature of Relationship

R Ltd. has direct economic interest in T Ltd. to the extent of 10%, and through S Ltd. in which it is the majority shareholders, it has further control of 9% in T Ltd. (60% of S Ltd.'s 15%). These two taken together (10% + 9%) make the total control of 19%.

Conclusion

In the present case, control of R Ltd. in T Ltd. directly and through S Ltd., is only 19%. Significant influence may also not be exercised as an investing party (R Ltd.) holds, directly or indirectly through intermediaries only 19% of the voting power of the T Ltd. Accordingly, R Ltd. and T Ltd. are not related parties. Hence related party disclosure, as per AS 18, is not required.

Question 7 : July – 2021 – Paper

(i) Khushi Limited enter into an agreement with Mr. Happy for running a business for a fixed amount payable to the later every year. The contract states that the day-to-day management of the business will be handled by Mr. Happy, while all financial and operating policy decisions are taken by the Board of Directors of the Company. Mr. Happy does not own any voting power in Khushi Limited.

(ii) Shri Bhanu a relative of key management personnel received remuneration of ` 3,50,000 for his services in the company for the period from 1st April, 2020 to 30th June, 2020. On 1st July, 2020, he left the service.

You are required to suggest how the above transactions will be treated as at the closing date i.e. on 31st March, 2021 for the purposes of AS 18- Related Party Disclosures.

Solution :

(i) Mr. Happy will not be considered as a related party of Khushi Limited in view of provisions of AS 18 "Related Party Disclosures" 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 are related parties".

In the given case, in the absence of share ownership, Mr. Happy would not be considered to exercise significant influence on Khushi Limited, even though there is an agreement giving him the power to manage the company. Further, the fact that Mr. Happy does not have the ability to direct or instruct the board of directors does not qualify him as a key management personnel.

(ii) According to AS 18 on 'Related Party Disclosures', parties are considered to be related if at any time during the reporting period one party has the ability to control the other party or exercise significant influence over the other party in making financial and/or operating decisions.

Hence, Shri Bhanu, a relative of key management personnel should be identified as related party for disclosure in the financial statements for the year ended 31.3.2021 as he received remuneration for his services in the company for the period from 1st April,2020 to 30th June,2020.

Question 8 : Nov – 2021 – RTP

Omega Bank Limited holds 25 per cent of the voting power of B Limited. Omega Bank Limited also provides finance by way of a loan to B Limited at market rates of interest, on account of which, Omega Bank Limited would have the power to nominate one person to the board of directors of B Limited. Any major transactions proposed to be entered into by B Limited would need the consent of Omega Bank Limited. Would Omega Bank Limited be considered as related party for B Ltd. (reporting enterprise)?

Solution :

Omega Bank Limited would be a related party of B Limited. As per AS 18 "associates and joint ventures of the reporting enterprise and the investing party of venture in respect of which the reporting enterprise is an associate or a joint venturer" are related party relationship. Further, an associate has been defined as "an enterprise in which an investing reporting party has significant influence and which is neither a subsidiary nor a joint venture of the party". Significant influence has been defined to be "participation in the financial and /or operating policy decisions of an enterprise, but not control of those policies". Further, it is given in the standard that significant influence may be gained by share ownership, agreement or statute. As regards share ownership, there is a presumption that ownership of 20 per cent or more of the voting power enables the enterprise to exercise significant influence, unless it could be clearly demonstrated otherwise. In the given example, Omega Bank Limited exercises significant influence over B Limited by virtue of ownership of 25 per cent of the voting power.

Omega Bank Limited is also a provider of finance for B Limited (as it has provided a loan to B Limited), and as per the standard, a provider of finance is deemed not to be a related party during its normal dealings with the enterprise by virtue only of those dealing. However, in this case, the exemption would not be available to Omega Bank Limited as the exercise of significant influence of Omega Bank Limited over B Limited has been demonstrated on account of ownership of more than 20 per cent of voting power. Accordingly, Omega Bank Limited would be construed to be a related party in the financial statements of B Limited and consequently, the latter would be required to disclose the transactions with Omega Bank Limited in its financial statements.

Question 9 : Nov – 2021 – RTP

A Limited has two Associates, B Limited and C Limited, and owns 25 per cent of the voting power of B Limited and 30 per cent of the voting power of C Limited. Would B Limited be considered a related party for the purpose of financial statements of C Limited?

Solution :

Both B Limited and C Limited are 'associates' of A Limited. Follow-associates cannot be regarded as a related parties only by virtue of the relationship. AS 18 states that "enterprise that directly, or indirectly through one or more intermediaries, control, or are controlled by, or are under common control with, the reporting enterprise" are related parties. Further, it is given that "associates and joint ventures of the reporting enterprise and the investing party or venture in respect of which the reporting enterprise is an associate or a joint venturer" are also related parties. As B Limited is not an associate of C Limited, nor is it being controlled, directly or indirectly, by C Limited or is not so controlling C Limited, it is not a related party of C Limited.

Question 10 : May – 2022 – RTP

In respect of a key supplier who is dependent on the company for its existence and the company enjoys influence over the prices of this supplier (which may not be formally demonstrable), can the supplier and the company be considered as related parties?

Solution :

The supplier and the company cannot be considered to be related parties merely because the latter is able to influence the transaction price between the parties. Paragraph 3 of AS 18 states that "enterprises that directly, or indirectly through one or more intermediaries, control, or are controlled by, or are under common control with, the reporting enterprise" are considered to be related party relationships. However, the conditions which define the existence of control, as follows, are not satisfied in the given example.

- 'ownership, directly or indirectly, of more than one-half of the voting power of an enterprise, or
- Control of the composition of the board of directors in the case of a company or of the composition of the corresponding governing body in case of any other enterprise, or
- a substantial interest in voting power and the power to direct, by statue or agreement, the financial and/or operating policies of the enterprise".

Paragraph 10 of the standard defines significant influence as "participation in the financial and/or operating policy decisions of an enterprise, but not control of those policies". In the given example, although the supplier and the company have entered into a commercial transaction, the terms of which are influenced by the latter because of its better bargaining power in the specific market for such goods, it cannot be concluded that there is participation in the financial and/or operating policy decisions. Therefore, as the conditions specified by the Standard for being classified as a related party are not satisfied in the given example, the company cannot be said to be related to the supplier. This view is supported by paragraph 4 (b) of the Standard which states that "a single customer, supplier, franchiser, distributor, or general agent with whom an

enterprise transacts a significant volume of business merely by virtue of the resulting economic dependence" would not be deemed to be related parties.

Question 11 : May – 2022 – RTP

Define "Key management personnel" in the context of AS 18.

Solution :

In context of AS 18, "Key management personnel" are those persons who have the authority and responsibility for planning, directing and controlling the activities of the reporting enterprise. For example, in the case of a company, the managing director(s), whole time director(s), manager and any person in accordance with whose directions or instructions the board of directors of the company is accustomed to act, are usually considered key management personnel.

Question 12 : Nov – 2022 – RTP

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 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 given 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.

Thanks ….

CHAPTER 7

AS 19 LEASES

Question 1 : May – 2018 – Paper / Jan – 2021 – Paper

A Ltd. sold JCB having WDV of Rs. 20 lakhs to B Ltd. for Rs. 24 lakhs and the same JCB was leased back by B Ltd. to A Ltd. The lease is operating lease. In context of Accounting Standard 19 "Leases" explain the accounting treatment of profit or loss in the books of A Ltd. if

(i) Sale price of Rs. 24 lakhs is equal to fair value.
(ii) Fair value is Rs. 20 lakhs and sale price is Rs. 24 lakhs.
(iii) Fair value is Rs. 22 lakhs and sale price is Rs. 25 lakhs.
(iv) Fair value is Rs. 25 lakhs and sale price is Rs. 18 lakhs.
(v) Fair value is Rs. 18 lakhs and sale price is Rs. 19 lakhs

Solution :

Following will be the treatment in the given cases:

(i) When sale price of Rs. 24 lakhs is equal to fair value, A Ltd. should immediately recognise the profit of Rs.4 lakhs (i.e. 24 – 20) in its books.
(ii) When fair value is Rs. 20 lakhs & sale price is Rs. 24 lakhs then profit of Rs. 4 lakhs is to be deferred and amortised over the lease period.
(iii) When fair value is Rs. 22 lakhs & sale price is Rs. 25 lakhs, profit of Rs. 2 lakhs (22 - 20) to be immediately recognised in its books and balance profit of Rs.3 lakhs (25-22) is to be amortised/deferred over lease period.
(iv) When fair value of leased machinery is Rs. 25 lakhs & sale price is Rs. 18 lakhs, then loss of Rs. 2 lakhs (20 – 18) to be immediately recognised by A Ltd. in its books provided loss is not compensated by future lease payment.
(v) When fair value is Rs. 18 lakhs & sale price is Rs. 19 lakhs, then the loss of Rs. 2 lakhs (20-18) to be immediately recognised by A Ltd. in its books and profit of Rs. 1 lakhs (19-18) should be amortised/deferred over lease period.

Question 2 : May – 2019 – RTP

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
= Rs. 50,000 x 0.7513
= Rs. 37,565

Present value of lease payments = Rs. 5,00,000 – Rs. 37,565
= Rs. 4,62,435

The percentage of present value of lease payments to fair value of the equipment is
(Rs. 4,62,435/ Rs. 5,00,000) x 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
= (Rs. 1,85,956 × 3) + Rs. 50,000
= Rs. 5,57,868 + Rs. 50,000 = 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 3 : May – 2019 – Paper

Jaya Ltd. took a machine on lease from Deluxe Ltd., the fair value being Rs.11,50,000. Economic life of the machine as well as lease term is 4 years. At the end of each year, lessee pays Rs.3,50,000 to lessor. Jaya Ltd. has guaranteed a residual value of Rs.70,000 on expiry of the lease to Deluxe Ltd., however Deluxe Ltd. estimates that residual value will be only Rs.25,000. The implicit rate of return is 10% p.a. and present value factors at 10% are : 0.909, 0.826, 0.751 and 0.683 at the end of 1st, 2nd, 3rd and 4th year respectively.

Calculate the value of machinery to be considered by Jaya Ltd. and 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 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 @10%)	Present value Rs.
1	3,50,000	0.909	3,18,150
2	3,50,000	0.826	2,89,100
3	3,50,000	0.751	2,62,850
4	4,20,000*	0.683	2,86,860
Total	**14,70,000**		**11,56,960**

Present value of minimum lease payments Rs. 11,56,960 is more than fair value at the inception of lease i.e. Rs. 11,50,000, therefore, the lease liability and machinery should be recognized in the books at Rs. 11,50,000 as per AS 19.

Question 4 : Nov – 2019 – RTP / May – 2021 – RTP

Sun Limited wishes to obtain a machine costing Rs.30 lakhs by way of lease. The effective life of the machine is 14 years, but the company requires it only for the first 3 years. It enters into an agreement with Star Ltd., for a lease rental for Rs.3 lakhs p.a. payable in arrears and the implicit rate of interest is 15%. The chief accountant of Suraj Limited is not sure about the treatment of these lease rentals and seeks your advice. (use annuity factor at @ 15% for 3 years as 3.36)

Solution :

Sun Limited wishes to obtain a machine costing Rs. 30 lakhs by way of lease. The effective life of the machine is 14 years, but the company requires it only for the first 3 years. It enters into an agreement with Star Ltd., for a lease rental for Rs. 3 lakhs p.a. payable in arrears and the implicit rate of interest is 15%. The chief accountant of Suraj Limited is not sure about the treatment of these lease rentals and seeks your advice. (use annuity factor at @ 15% for 3 years as 3.36)

Question 5 : Nov – 2019 – Paper

Classify the following into either operating lease or finance lease with reason:

(1) Economic life of asset is 10 years, lease term is 9 years, but asset is not acquired at the end of lease term.

(2) Lessee has option to purchase the asset at lower than fair value at the end of lease term.

(3) Lease payments should be recognized as an expense in the statement of Profit & Loss of a lessee.

(4) Present Value (PV) of Minimum Lease Payment (MLP) = "X".
Fair value of the asset is "Y". And X = Y.

(5) Economic life of the asset is 5 years, lease term is 2 years, but the asset is of special nature and has been procured only for use of the lessee.

Solution :

(i) The lease will be classified as a finance lease, since a substantial portion of the life of the asset is covered by the lease term.

(ii) If it becomes certain at the inception of lease itself that the option will be exercised by the lessee, it is a Finance Lease.

(iii) It is an operating lease under which lease payments are recognized as expense in the profit and loss account of lessee to have better matching between cost and revenue.
(iv) The lease is a finance lease if X = Y, or where X substantially equals Y.
(v) Since the asset is of special nature and has been procured only for the use of lessee, it is a finance lease.

Question 6 : May – 2020 – RTP

ABC Ltd. took a machine on lease from XYZ Ltd., the fair value being Rs.10,00,000. The economic life of the machine as well as the lease term is 4 years. At the end of each year, ABC Ltd. pays Rs.3,50,000. The lessee has guaranteed a residual value of Rs.50,000 on expiry of the lease to the lessor. However, XYZ Ltd. estimates that the salvage value of the machine will be only Rs.35,000 only. It was not practicable for the lessee to determine the interest rate implicit in the lease, However the incremental borrowing rate of ABC Ltd. is determined at 16.4%. PV factors at 16.4% for year 1, year 2, year 3 and year 4 are 0.8591, 0.7381, 0.6341 and 0.5447 respectively. You are required to calculate the value of machinery to be considered by ABC Ltd. and the finance charges for each year.

Solution :

As per AS 19 "Leases", the lessee should recognize the lease as an asset and a liability at the inception of a finance lease at an amount equal to the fair value of the leased asset at the inception of lease. However, if the fair value of the leased asset exceeds the present value of minimum lease payment from the standpoint of the lessee, the amount recorded as an asset and liability should be the present value of minimum lease payments from the standpoint of the lessee.

Value of machinery

In the given case, fair value of the machinery is Rs. 10, 00,000 which is more than net present value of minimum lease payments of Rs. 9,98,835 (Refer working Note). Hence, the machine and the corresponding liability will be recorded at value of Rs. 9,98,835 in the books of ABC Ltd.

Calculation of finance charges for each year

Year	Finance charge	Payment	Reduction in outstanding liability	Outstanding liability
1st year beginning	-	-	-	9,98,835
End of 1st year	1,63,809	3,50,000	1,86,191	8,12,644
End of 2nd year	1,33,274	3,50,000	2,16,726	5,95,918
End of 3rd year	97,731	3,50,000	2,52,269	3,43,649
End of 4th year	56,358	4,00,000*	3,43,642	7**

Working Note:

Present value of minimum lease payments

Annual lease rental x PV factor 3,50,000 x (0.8591+ 0.7381+ 0.6341+ 0.5447)	Rs. 9,71,600
Present value of guaranteed residual value 50,000 x (0.5447)	Rs. 27,235
	Rs. 9,98,835

Question 7 : Nov – 2020 – RTP

Classify the following into either operating or finance lease:

(i) If Present value (PV) of Minimum lease payment (MLP) = "X" ; Fair value of the asset is "Y" and X=Y.

(ii) Economic life of the asset is 7 years, lease term is 6.5 years, but asset is not acquired at the end of the lease term;

(iii) Economic life of the asset is 6 years, lease term is 2 years, but the asset is of special nature and has been procured only for use of the lessee.

Solution :

(i) The lease is a finance lease if X = Y, or if X substantially equals Y.

(ii) The lease will be classified as a finance lease, since a substantial portion of the life of the asset is covered by the lease term.

(iii) Since the asset is procured only for the use of lessee, it is a finance lease.

Question 8 : Nov – 2020 – RTP

Viral Ltd. sold machinery having WDV of Rs.40 lakhs to Saral Ltd. for Rs.50 lakhs and the same machinery was leased back by Saral Ltd. to Viral Ltd. The lease back is in nature of operating lease. You are required to explain the treatment in the given cases –

(i) Fair value is Rs.45 lakhs and sale price is Rs.38 lakhs.

(ii) Fair value is Rs.40 lakhs and sale price is Rs.50 lakhs.

(iii) Fair value is Rs.46 lakhs and sale price is Rs.50 lakhs.

Solution :

As per AS 19, where sale and leaseback results in operating lease, then the accounting treatment in different situations is as follows:

Situation 1: Sale price = Fair Value

Profit or loss should be recognized immediately.

Situation 2: Sale Price < Fair Value

Profit should be recognized immediately. The loss should also be recognized immediately except that, if the loss is compensated by future lease payments at below market price, it should be deferred and amortized in proportion to the lease payments over the period for which the asset is expected to be used.

Situation 3: Sale Price > Fair Value

The excess over fair value should be deferred and amortized over the period for which the asset is expected to be used.

Following will be the treatment in the situations given in the question:

(i) When fair value of leased machinery is Rs. 45 lakhs & sales price is Rs. 38 lakhs, then loss of Rs. 2 lakhs (40 – 38) to be immediately recognized by Viral Ltd. in its books provided loss is not compensated by future lease payment.

(ii) When fair value is Rs. 40 lakhs & sales price is Rs. 50 lakhs then, profit of Rs. 10 lakhs is to be deferred and amortized over the lease period.

(iii) When fair value is Rs. 46 lakhs & sales price is Rs. 50 lakhs, profit of Rs. 6 lakhs (46 less 40) to be immediately recognized in its books and balance profit of Rs.4 lakhs (50-46) is to be amortized/deferred over lease period.

Question 9 : Dec – 2021 – Paper

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 of Rs.2,25,000. Economic life of the machine is 5 years and output from the machine is estimated as 60,000 units, 75,000 units 90,000 units, 1,20,000 units and 1,05,000 units consecutively for 5 years. Straight line depreciation in proportion of output is considered appropriate. You are required to compute the following as per AS-19.

(i) Annual Lease Rent

(ii) Lease Rent income to be recognised in each operating year and

(iii) Depreciation for 3 years of lease

Solution :

(i) Annual lease rent

Total lease rent

= 130% of Rs. 2,25,000 ▯ Output during lease period/ Total output

= 130% of Rs. 2,25,000 x (60,000 +75,000+ 90,000)/(60,000 + 75,000 + 90,000 + 1,20,000 + 1,05,000)

= 2,92,500 x 2,25,000 units/4,50,000 units = Rs. 1,46,250

Annual lease rent = Rs. 1,46,250 / 3 = Rs. 48,750

(ii) Lease rent Income to be recognized in each operating year

Total lease rent should be recognized as income in proportion of output during lease period, i.e. in the proportion of 60,000 : 75,000 : 90,000 or 4:5:6

Hence income recognized in years 1, 2 and 3 will be as:

Year 1 Rs. 39,000,

Year 2 Rs. 48,750 and

Year 3 Rs. 58,500.

(iii) Depreciation for three years of lease

Since depreciation in proportion of output is considered appropriate, the depreciable amount Rs. 2,25,000 should be allocated over useful life 5 years in proportion of output, i.e. in proportion of 60 :75: 90 : 120 : 105 .

Depreciation for year 1 is Rs. 30,000, year 2 = 37,500 and year 3 = 45,000.

Question 10 : May – 2022 – RTP

Classify the following into either operating or finance lease:

(i) If Present value (PV) of Minimum lease payment (MLP) = "X"; Fair value of the asset is "Y" and X=Y.

(ii) Economic life of the asset is 7 years, lease term is 6.5 years, but asset is not acquired at the end of the lease term;

(iii) Economic life of the asset is 6 years, lease term is 2 years, but the asset is of special nature and has been procured only for use of the lessee.

Solution :

(i) The lease is a finance lease if X = Y, or if X substantially equals Y.

(ii) The lease will be classified as a finance lease, since a substantial portion of the life of the asset is covered by the lease term.

(iii) Since the asset is procured only for the use of lessee, it is a finance lease.

Question 11 : May – 2022 – RTP

Viral Ltd. sold machinery having WDV of Rs. 40 lakhs to Saral Ltd. for Rs. 50 lakhs and the same machinery was leased back by Saral Ltd. to Viral Ltd. The lease back is in nature of operating lease. You are required to explain the treatment in the given cases –

(i) Fair value is Rs. 45 lakhs and sale price is Rs. 39 lakhs.

(ii) Fair value is Rs. 40 lakhs and sale price is Rs. 49 lakhs.

(iii) Fair value is Rs. 46 lakhs and sale price is Rs. 50 lakhs

Solution :

As per AS 19, where sale and leaseback results in operating lease, then the accounting treatment in different situations is as follows:

Situation 1: Sale price = Fair Value

Profit or loss should be recognized immediately.

Situation 2: Sale Price < Fair Value

Profit should be recognized immediately. The loss should also be recognized immediately except that, if the loss is compensated by future lease payments at below market price, it should be deferred and amortized in proportion to the lease payments over the period for which the asset is expected to be used.

Situation 3: Sale Price > Fair Value

The excess over fair value should be deferred and amortized over the period for which the asset is expected to be used.

Following will be the treatment in the situations given in the question:

(i) When fair value of leased machinery is Rs. 45 lakhs & sale price is Rs. 39 lakhs, then loss of Rs. 1 lakh (40 – 39) to be immediately recognized by Viral Ltd. in its books provided loss is not compensated by future lease payment.

(ii) When fair value is Rs. 40 lakhs & sale price is Rs. 49 lakhs then, profit of Rs. 9 lakhs is to be deferred and amortized over the lease period.

(iii) When fair value is Rs. 46 lakhs & sale price is Rs. 50 lakhs, profit of Rs. 6 lakhs (46 less 40) to be immediately recognized in its books and balance profit of Rs.4 lakhs (50-46) is to be amortized/deferred over lease period.

Question 12 : May – 2022 – Paper

What are the disclosures requirements for operating leases by the lessee as per AS-19 ?

Solution :

As per AS 19, lessees are required to make following disclosures for operating leases:

(a) the total of future minimum lease payments under non-cancelable operating leases for each of the following periods:
   (i) not later than one year;
   (ii) later than one year and not later than five years;
   (iii) later than five years;

(b) the total of future minimum sublease payments expected to be received under non-cancelable subleases at the balance sheet date;

(c) lease payments recognised in the statement of profit and loss for the period, with separate amounts for minimum lease payments and contingent rents;

(d) sub-lease payments received (or receivable) recognised in the statement of profit and loss for the period;

(e) a general description of the lessee's significant leasing arrangements including, but not limited to, the following:
   (i) the basis on which contingent rent payments are determined;
   (ii) the existence and terms of renewal or purchase options and escalation clauses; and
   (iii) restrictions imposed by lease arrangements, such as those concerning dividends, additional debt, and further leasing.

   Note: The Level II and Level III non-corporate entities (and SMCs) need not make disclosures required by (a), (b) and (e) above.

Question 13 : Nov – 2022 – RTP

WIN Ltd. has entered into a three year lease arrangement with Tanya sports club in respect of Fitness Equipment’s costing Rs. 16,99,999.50. The annual lease payments to be made at the end of each year are structured in such a way that the sum of the Present Values of the lease payments and that of the residual value together equal the cost of the equipments leased out. The

unguaranteed residual value of the equipment at the expiry of the lease is estimated to be Rs. 1,33,500. The assets would revert to the lessor at the end of the lease. Given that the implicit rate of interest is 10%. You are required to compute the amount of the annual lease payment and the unearned finance income. Discounting Factor at 10% for years 1, 2 and 3 are 0.909, 0.826 and 0.751 respectively.

Solution :

(i) Computation of annual lease payment to the lessor

	Rs.
Cost of equipment	16,99,999.50
Unguaranteed residual value	1,33,500.00
Present value of residual value after third year @ 10% (Rs. 1,33,500 × 0.751)	1,00,258.50
Fair value to be recovered from lease payments (Rs. 16,99,999.5– Rs. 1,00,258.5)	15,99,741.00
Present value of annuity for three years is 2.486	
Annual lease payment = Rs. 15,99,741/ 2.486	6,43,500.00

(ii) Computation of Unearned Finance Income

	Rs.
Total lease payments (Rs. 6,43,500 x 3)	19,30,500
Add: Unguaranteed residual value	1,33,500
Gross investment in the lease	20,64,000.00
Less: Present value of investment (lease payments and residual value) (Rs. 1,00,258.5+ Rs. 15,99,741)	(16,99,999.50)
Unearned finance income	3,64,000.50

Thanks ....

CHAPTER 8

AS 20 EARNINGS PER SHARE

Question 1 : May – 2018 – Paper

As at 1st April, 2016 a company had 6,00,000 equity shares of Rs. 10 each (Rs. 5 paid up by all shareholders). On 1st September, 2016 the remaining Rs. 5 was called up and paid by all shareholders except one shareholder having 60,000 equity shares. The net profit for the year ended 31st March, 2017 was Rs. 21,96,000 after considering dividend on preference shares and dividend distribution tax on such dividend totalling to Rs. 3,40,000.

Compute Basic EPS for the year ended 31st March, 2017 as per Accounting Standard 20 "Earnings Per Share".

Solution :

Basic Earnings per share (EPS) =

$$\frac{\text{Net profit attributable to equity shareholders}}{\text{Weighted average number of equity shares outstanding during the year}}$$

$$= \frac{21,96,000}{4,57,500 \text{ Shares (as per working note)}} = \text{Rs.4.80 per share}$$

Working Note:

Calculation of weighted average number of equity shares

As per AS 20 'Earnings Per Share', partly paid equity shares are treated as a fraction of equity share to the extent that they were entitled to participate in dividend relative to a fully paid equity share during the reporting period. Assuming that the partly paid shares are entitled to participate in the dividend to the extent of amount paid, weighted average number of shares will be calculated as follows:

Date	No. of equity shares	Amount paid per share	Weighted average no. of equity shares
	Rs.	Rs.	Rs.
1.4.2016	6,00,000	5	6,00,000 x 5/10 x 5/12 = 1,25,000
1.9.2016	5,40,000	10	5,40,000 x 7/12 = 3,15,000
1.9.2016	60,000	5	60,000 x 5/10 x 7/12 = 17,500
Total weighted average equity shares			4,57,500

Question 2 : Nov – 2018 – Paper

From the following information given by Sampark Ltd., Calculate Basis EPS and Diluted EPS as per AS 20 :

	Rs.
Net Profit for the current year	2,50,00,000
No. of Equity Shares Outstanding	50,00,000
No. of 12% convertible debentures of Rs.100 each	50,000
Each debenture is convertible into 8 Equity Shares	
Interest expense for the current year	6,00,000
Tax saving relating to interest expense (30%)	1,80,000

Solution :

Calculation of Basic Earning Per Share

Basic EPS $= \dfrac{\text{Net Profit for the current year}}{\text{No. of Equity Shares}}$

$= \dfrac{2{,}50{,}000}{50{,}00{,}00}$

Basic EPS per share = Rs.5

Calculation of Diluted Earning Per Share

Diluted EPS = $\dfrac{\text{Adjusted net profit for the current year}}{\text{Weighted average no. of Equity Shares}}$

Adjusted net profit for the current year	Rs.
Net profit for the current year	2,50,00,000
Add: Interest expenses for the current year	6,00,000
Less: Tax saving relating to Tax Expenses	(1,80,000)
	2,54,20,000

No. of equity shares resulting from conversion of debentures: 4,00,000 Shares

Weighted average no. of equity shares used to compute diluted EPS: (50,00,000 + 4,00,000) = 54,00,000 Equity Shares

Diluted earnings per share: (2,54,20,000/54,00,000) = Rs. 4.71 (Approx.)

Question 3 : May – 2019 – RTP

"While calculating diluted EPS, effect is given to all dilutive potential equity shares that were outstanding during the period." Explain this statement in the light of relevant AS.

Also calculate the diluted EPS from the following information:

Net Profit for the current year (After Tax)	Rs.1,00,00,000
No. of Equity shares outstanding	10,00,000
No. of 10% Fully Convertible Debentures of Rs.100 each	1,00,000
(Each Debenture is compulsorily & fully convertible into 10 equity shares issued at the mid of the year)	
Debenture interest expense for the current year	Rs.5,00,000
Assume applicable Income Tax rate @ 30%	

Solution :

As per AS 20 'Earnings per Share', the net profit or loss for the period attributable to equity shareholders and the weighted average number of shares outstanding during the period should be adjusted for the effects of all dilutive potential equity shares for calculation of diluted earnings per share. Hence, "in calculating diluted earnings per share, effect is given to all dilutive potential equity shares that were outstanding during the period."

Computation of diluted earnings per share = $\frac{\text{Adjusted net profit for the current year}}{\text{Weighted average no. of Equity Shares}}$

Adjusted net profit for the current year

	Rs.
Net profit for the current year (after tax)	1,00,00,000
Add: Interest expense for the current year	5,00,000
Less: Tax relating to interest expense (30% of Rs.5,00,000)	(1,50,000)
Adjusted net profit for the current year	1,03,50,000

Weighted average number of equity shares

Number of equity shares resulting from conversion of debentures

= $\frac{1,00,000 \times 100}{10}$ = 10,00,000 Equity shares

Weighted average number of equity shares used to compute diluted earnings per share

= [(10,00,000 x 12) + (10,00,000 x 6)]/12 = 15,00,000 equity shares

Diluted earnings per share = Rs.1,03,50,000 / 15,00,000 shares = Rs.6.90 per share

Question 4 : Nov – 2019 – RTP

The following information relates to M/s. XYZ Limited for the year ended 31st March, 2019:

Net Profit for the year after tax: Rs.37,50,000

Number of Equity Shares of Rs. 10 each outstanding: Rs.5,00,000

Convertible Debentures Issued by the Company (at the beginning of the year)

Particulars	Nos.
8% Convertible Debentures of Rs.100 each	50,000
Equity Shares to be issued on conversion	55,000

The Rate of Income Tax: 30%.

You are required to calculate Basic and Diluted Earnings Per Share (EPS).

Solution :

Computation of basic earnings per share

Net profit for the current year / Weighted average number of equity shares outstanding during the year

Rs. 37,50,000 / 5,00,000 = Rs. 7.50 per share

Computation of diluted earnings per share $\frac{\text{Adjusted net profit for the current year}}{\text{Weighted average no. of Equity Shares}}$

Adjusted net profit for the current year

	Rs.
Net profit for the current year	37,50,000
Add: Interest expense for the current year	4,00,000
Less: Tax relating to interest expense (30% of Rs. 4,00,000)	(1,20,000)
Adjusted net profit for the current year	40,30,000

Number of equity shares resulting from conversion of debentures

= 55,000 Equity shares (given in the question)

Weighted average number of equity shares used to compute diluted earnings per share

= 5,55,000 shares (5,00,000 + 55,000)

Diluted earnings per share

= 40,30,000/ 5,55,000 = Rs. 7.26 per share

Note: Conversion of convertible debentures into Equity Share will be dilutive potential equity shares. Hence, to compute the adjusted profit the interest paid on such debentures will be added back as the same would not be payable in case these are converted into equity shares.

Question 5 : Nov – 2019 – Paper

Following information is supplied by K Ltd.:

Number of shares outstanding prior to right issue - 2,50,000 shares.

Right issue - two new share for each 5 outstanding shares (i.e. 1,00,000 new shares)

Right issue price – Rs.98

Last date of exercising rights - 30-06-2018.

Fair value of one equity share immediately prior to exercise of right on 30-06-2018 is Rs.102.

Net Profit to equity shareholders:

2017-2018 - Rs.50,00,000

2018-2019 - Rs.75,00,000

You are required to calculate the basic earnings per share as per AS-20 Earnings per Share.

Solution :

$$\frac{\text{Fair Value of shares immediately prior to exercise of rights} + \text{Total amount received from exercise}}{\text{Number of shares outstanding prior to exercise} + \text{Number of shares issued in the exercise}}$$

$$\frac{102 \times 2{,}50{,}000 + \text{Rs.}98 \times 1{,}00{,}000 \text{ shares}}{3{,}50{,}000 \text{ shares}}$$

Computation of adjustment factor :

$$\frac{\text{Fair Value per share prior to exercise of rights}}{\text{Theoretical ex - rights value per share}} = 102/100.86 = 1.01$$

Computation of earnings per share:

EPS for the year 2017-18 as originally reported: Rs. 50,00,000/2,50,000 shares = Rs. 20

EPS for the year 2017-18 restated for rights issue: =Rs. 50,00,000/ (2,50,000 shares x 1.01) = Rs. 19.80

EPS for the year 2018-19 including effects of rights issue:
EPS = 75,00,000/3,25,625* = Rs.23.03
* [(2,50,000 x 1.01 x 3/12) + (3,50,000 x 9/12)] =63,125 + 2,62,500 = 3,25,625 shares
Note : Financial year (ended 31st March) is considered as accounting year while giving the above answer.

Question 6 : May – 2020 – RTP

From the following information, you are required to compute Basic and Diluted Earnings Per Share (EPS) of M/s. XYZ Limited for the year ended 31st March, 2019:

Net Profit for the year after tax : Rs.75,00,000
Number of Equity Shares of Rs.10 each outstanding: 10,00,000

1,00,000, 8% Convertible Debentures of Rs. 100 each were issued by the Company at the beginning of the year. 1,10,000 Equity Shares were supposed to be issued on conversion. Consider rate of Income Tax as 30%.

Solution :

Computation of basic earnings per share
Net profit for the current year / Weighted average number of equity shares outstanding during the year
Rs. 75,00,000 / 10,00,000 = Rs. 7.50 per share

Computation of diluted earnings per share Adjusted $\frac{\text{Adjusted net profit for the current year}}{\text{Weighted average no. of Equity Shares}}$

Adjusted net profit for the current year

	Rs.
Net profit for the current year	75,00,000
Add: Interest expense for the current year	8,00,000
Less: Tax relating to interest expense (30% of Rs.8,00,000)	(2,40,000)
Adjusted net profit for the current year	80,60,000

Number of equity shares resulting from conversion of debentures
= 1,10,000 Equity shares (given in the question)
Weighted average number of equity shares used to compute diluted earnings per share
= 11,10,000 shares (10,00,000 + 1,10,000)
Diluted earnings per share
= Rs. 80,60,000/ 11,10,000
= Rs. 7.26 per share

Note: Conversion of convertible debentures into Equity Share will be dilutive potential equity shares. Hence, to compute the adjusted profit the interest paid on such debentures will be added back as the same would not be payable in case these are converted into equity shares.

Question 7 : Nov – 2020 – RTP

A-One Limited supplied the following information. You are required to compute the earnings per share as per AS 20:

Net profit attributable to equity shareholders Year 2017-18: Rs.1,00,00,000
Year 2018-19 : Rs.1,50,00,000

Number of shares outstanding prior to Right Issue 50,00,000 shares

Right Issue: One new share for each four outstanding shares i.e., 12,50,000 shares
Right Issue Price – Rs.96
Last date of exercising rights - 30-06-2018

Fair value of one equity share immediately prior to exercise of rights on 30-06-2018 was Rs. 101.

Solution :

Computation of earnings per share :

	2017-18 Rs.	2018-19 Rs.
EPS for the year 2017-18 as originally reported : (Rs. 1,00,00,000 / 50,00,000 shares)	2.00	
EPS for the year 2017-18 restated for rights issue : Rs.1,00,00,000 / (50,00,000 shares x 1.01) *	1.98	
EPS for the year 2018-19 including effects of rights issue : $\frac{Rs.1,50,00,000}{(50,00,000 \times 1.01 \times 3/12) + (62,50,000 \times 9/12)}$		2.52

*Computation of earnings per share in case of Rights Issue requires computation of adjustment factor which is given as working note.

Working Notes :

1. Computation of theoretical ex-rights fair value per share

$$\frac{\text{Fair value of all outstanding shares immediately prior to exercise of rights + total amount received from exercise}}{\text{Number of shares outstanding prior to exercise + Number of shares issued in the exercise}}$$

$$\frac{(\text{Rs.}101 \times 50,00,000 \text{ shares}) + (\text{Rs.}96 \times 12,50,000 \text{ shares})}{50,00,000 \text{ shares} + 12,50,000 \text{ shares}}$$

= Rs.62,50,00,000 / 62,50,000 = Rs.100

2. Computation of adjustment factor

$$\frac{\text{Fair value per share prior to exercise of rights}}{\text{Theoretical ex - rights value per share}} = \frac{Rs.(101)}{Rs.(100)} = 1.01$$

Question 8 : May – 2021 – RTP

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 an other financial instrument,

(vi) Equity Shares issued as consideration for the acquisition of an asset other than in cash.

Solution :

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 on which the acquisition is recognised.

Question 9 : Nov – 2021 – RTP

AB Limited is a company engaged in manufacturing industrial packaging equipment. As per the terms of an agreement entered 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 as per provisions of AS 20?

Solution :

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. AS 20 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 10 : Dec – 2021 – Paper

"At the time of calculating diluted earnings per share, effect is given to all dilutive potential equity shares that are outstanding during the period."

Comment and also calculate the basic and diluted earnings per share for the tear 2020-21 from the following information :

(i)	Net profit after tax for the year	Rs.64,12500
(ii)	No. of equity shares outstanding	15,00,000
(iii)	No. of 9% convertible debentures of Rs.100 issued on 1st July, 2020	75,000
(iv)	Each debenture is convertible into 8 Equity Shares.	
(v)	Tax relating to interest expenses	35%

Solution :

In calculating diluted earnings per share, effect is given to all dilutive potential equity shares that were outstanding during the period.” As per AS 20 ‘Earnings per Share’, the net profit or loss for the period attributable to equity shareholders and the weighted average number of shares outstanding during the period should be adjusted for the effects of all dilutive potential equity shares for the purpose of calculation of diluted earnings per share.

Basic EPS for the year 2020-21= 64,12,500/15,00,000 = Rs. 4.275 or Rs. 4.28

Computation of diluted earnings per share for year 2020-21

$$\frac{\text{Adjusted net profit for the current year}}{\text{Weighted average number of equity shares}}$$

Adjusted net profit for the current year will be (64,12,500 + 5,06,250 – 1,77,188) = Rs. 67,41,562

No. of equity shares resulting from conversion of debentures:

6,00,000 Shares (75,000 × 8)

Weighted average no. of equity shares used to compute diluted EPS:

(15,00,000 X12/12+ 6,00,000X9/12) = 19,50,000 Shares

Diluted earnings per share: (67,41,562/19,50,000) = Rs. 3.46

Working Note:

Interest expense for 9 months = 75,00,000×9%×9/12 =Rs. 5,06,250

Tax expense 35 % on interest is Rs.1,77,188 (5,06,250 x 35%)

Question 11 : May – 2022 – RTP

Stock options have been granted by AB Limited to its employees and they vest equally over 5 years, i.e., 20 per cent at the end of each year from the date of grant. The options will vest only if the employee is still employed with the company at the end of the year. If the employee leaves the company during the vesting period, the options that have vested can be exercised, while the others would lapse. Currently, AB Limited includes only the vested options for calculating Diluted EPS. Should only completely vested options be included for computation of Diluted EPS? Is this in accordance with the provisions of AS 20? Explain.

Solution :

The current method of calculating Diluted EPS adopted by AB limited is not in accordance with AS 20. The calculation of Diluted EPS should include all potential equity shares, i.e., all the stock options granted at the balance sheet date, which are dilutive in nature, irrespective of the vesting pattern. The options that have lapsed during the year should be included for the portion of the period the same were outstanding, pursuant to the requirement of the standard.

AS 20 states that “A potential equity share is a financial instrument or other contract that entitles, or may entitle, its holder to equity shares”. Options including employee stock option plans under which employees of an enterprise are entitled to receive equity shares as part of their remuneration and other similar plans are examples of potential equity shares. Further, for the purpose of calculating diluted earnings per share, the net profit or loss for the period attributable to equity shareholders and the weighted average number of shares outstanding during the period should be adjusted for the effects of all dilutive potential equity shares.

Question 12 : May – 2022 – RTP

X Limited, as at March 31, 2021, has income from continuing ordinary operations of Rs. 2,40,000, a loss from discontinuing operations of Rs. 3,60,000 and accordingly a net loss of Rs. 1,20,000. The Company has 1,000 equity shares and 200 potential equity shares outstanding as at March 31, 2021. You are required to compute Basic and Diluted EPS?

Solution :

As per 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". As income from continuing ordinary operations, Rs. 2,40,000 would be considered and not Rs. (1,20,000), for ascertaining whether 200 potential equity shares are dilutive or anti-dilutive. Accordingly, 200 potential equity shares would be dilutive potential equity shares since their inclusion would decrease the net profit per share from continuing ordinary operations from Rs. 240 to Rs. 200. Thus the basic E.P.S would be Rs. (120) and diluted E.P.S. would be Rs. (100).

Question 13 : May – 2022 – Paper

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 :

(i) 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.

(ii) 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 :

(i) Calculation of Basic Earnings per share for the year ended 31stMarch, 2022 including the comparative figure:

(a) Earnings for the year ended 31st March, 2021 = EPS x Number of shares outstanding during 2020-2021

= Rs. 62.30 x 10,00,000 equity shares

= Rs. 6,23,00,000

(b) Adjusted Earnings per share after taking into consideration bonus issue

Adjusted Basic EPS = Earnings for the year 2020-2021 / Total outstanding shares +Bonus issue

= Rs. 6,23,00,000 / (10,00,000+ 5,00,000)

= Rs. 6,23,00,000 / 15,00,000

= Rs. 41.53 per share

(c) 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)

= (Rs. 90,00,000 – Rs. (1,00,00,000 x 8%) / (10,00,000 + 5,00,000 + (2,00,000 x 3/12))

= Rs. 82,00,000 / 15,50,000 shares

= Rs. 5.29 per share

(ii) 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 14 : Nov – 2022 – RTP

The following information relates to XYZ Limited for the year ended 31st March, 2022:

Net Profit for the year after tax: Rs. 37,50,000

Number of Equity Shares of Rs. 10 each outstanding: Rs. 5,00,000

Convertible Debentures Issued by the Company (at the beginning of the year)

Particulars	**Nos.**
8% Convertible Debentures of Rs. 100 each Equity Shares to be issued on conversion	50,000 55,000

The Rate of Income Tax: 30%.

You are required to calculate Basic and Diluted Earnings Per Share (EPS).

Solution :

Computation of basic earnings per share

Net profit for the current year / Weighted average number of equity shares outstanding during the year

Rs. 37,50,000 / 5,00,000 = Rs. 7.50 per share

Computation of diluted earnings per share $\frac{\text{Adjusted net profit for the current year}}{\text{Weighted average number of equity shares}}$

Adjusted net profit for the current year

	Rs.
Net profit for the current year Add: Interest expense for the current year Less: Tax relating to interest expense (30% of Rs. 4,00,000) Adjusted net profit for the current year	37,50,000 4,00,000 (1,20,000) 40,30,000

Number of equity shares resulting from conversion of debentures

= 55,000 Equity shares (given in the question)

Weighted average number of equity shares used to compute diluted earnings per share

= 5,55,000 shares (5,00,000 + 55,000)

Diluted earnings per share

= 40,30,000/ 5,55,000 = Rs. 7.26 per share

Note: Conversion of convertible debentures into Equity Share will be dilutive potential equity shares. Hence, to compute the adjusted profit the interest paid on such debentures will be added back as the same would not be payable in case these are converted into equity shares.

Question 15 : Nov – 2022 – Paper

The following information is provided to you :

Net profit for the year 2022 :	Rs.72,00,000
Weighted average number of equity shares outstanding during the year 2022 :	30,00,000 shares
Average Fair value of one equity share during the year 2022 :	Rs.25.00
Weighted average number of shares under option during the year 2022 :	6,00,000 shares
Exercise price for shares under option during the year 2022 :	Rs.20.00

You are required to compute Basic and Diluted Earnings Per Share as per AS-20.

Thanks ....

CHAPTER 9

AS 22 ACCOUNTING FOR TAXES ON INCOME

Question 1 : May – 2020 – RTP / Jan – 2021 – Paper

The following particulars are stated in the Balance Sheet of PQR Ltd. as on31.03.2018:

	(Rs. in Lakhs)
Deferred Tax Liability (Cr.) Deferred Tax Assets (Dr.)	30.00 15.00

The following transactions were reported during the year 2018-2019:

(i)	Tax Rate	30%
		(Rs.in lakh)
(ii)	Depreciation as per books	80.00
	Depreciation for tax purposes	70.00
(iii)	Items disallowed in 2017-2018 and allowed for tax purposes in 2018-2019.	10.00
(iv)	Donations to Private Trust made in 2018-2019.	10.00

There were no additions to Fixed Assets during the year.

You are required to show the impact of various items on Deferred Tax Assets and Deferred Tax Liability as on 31.03.2019.

Solution :

Impact of various items in terms of AS 22 deferred tax liability/deferred tax asset

Transactions	Analysis	Nature of difference	Effect	Amount
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	Rs.(80-70) lakh × 30% = Rs.3 lakh
Disallowances, as per IT Act, of earlier years	Tax payable for the earlier year was	Responding timing difference	Reversal of DTA	Rs.10 lakh × 30% = Rs.3 lakh

	higher on this account.			
Donation to private trusts	Not an allowable expenditure under IT Act.	Permanent difference	Not applicable	Not applicable

Question 2 : Nov – 2020 – RTP

Write short note on Timing differences and Permanent differences as per AS 22.

Solution :

Accounting income and taxable income for a period are seldom the same. Permanent differences are those which arise in one period and do not reverse subsequently. For e.g., an income exempt from tax or an expense that is not allowable as a deduction for tax purposes. Timing differences are those which arise in one period and are capable of reversal in one or more subsequent periods. For e.g., Depreciation, Bonus, etc.

Question 3 : Nov – 2020 – RTP

Rama Ltd., has provided the following information:

	Rs.
Depreciation as per accounting records	6,00,000
Depreciation as per income tax records	10,00,000
Unamortized preliminary expenses as per tax record	60,000

There is adequate evidence of future profit sufficiency. You are required to calculate the amount of deferred tax asset/liability to be recognized as transition adjustment assuming Tax rate as 30%.

Solution :

Table showing calculation of deferred tax asset / liability

Particulars	**Amount Rs.**	**Timing differences**	**Deferred tax**	**Amount @ 30% Rs.**
Excess depreciation as per tax records (Rs.10,00,000 – Rs.6,00,000)	4,00,000	Timing	Deferred tax liability	1,20,000
Unamortized preliminary expenses as per tax records	60,000	Timing	Deferred tax asset	(18,000)
Net deferred tax liability				1,02,000

Question 4 : Nov – 2020 – Paper

From the following details of Aditya Ltd for accounting year ended on 31st March 2020

Particulars	**Rs.**
Accounting Profit	15,00,000
Book Profit as per MAT	7,50,000
Profit as per Income Tax	2,50,000

Tax Rate	20%
MAT Rate	7.5%

Calculate the deferred tax assets/liability as per AS 22and amount tax to be debited to the profit and loss accounts for the year.

Solution :

Tax as per accounting profit 15,00,000 × 20%= Rs. 3,00,000
Tax as per Income-tax Profit 2,50,000 × 20% =Rs. 50,000
Tax as per MAT 7,50,000 × 7.50%= Rs. 56,250
Tax expense= Current Tax +Deferred Tax
Rs. 3,00,000 = Rs. 50,000 + Deferred tax
Therefore, Deferred Tax liability as on 31-03-2020
= Rs. 3,00,000 – Rs. 50,000 = Rs. 2,50,000
Amount of tax to be debited in Profit and Loss account for the year 31-03-2020
Current Tax + Deferred Tax liability + Excess of MAT over current tax
= Rs. 50,000 + Rs. 2,50,000 + Rs. 6,250 (56,250 – 50,000) = Rs. 3,06,250

Question 5 : May – 2021 – RTP

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.

Solution :

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)
(ii)	Depreciation on new machinery	Due to allowance of full amount as expenditure under IT Act, tax payable in the earlier years is less.	Timing difference	Creation of DTL	(1,20,000 – 30,000) x 40% = 36,000
	Net impact				NIL

Question 6 : May – 2021 – RTP

What are the disclosure requirements for deferred tax assets and deferred tax liabilities in the balance sheet as per AS 22?

Solution :

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 7 : July – 2021 – Paper

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) Depreci0ation as per books was Rs.70 Lakhs whereas Depreciation for Tax purpose was Rs.42 Lakhs. There were no additions to Fixed Assets during the year.

(ii) Expense disallowed in 2019-20 and allowed for tax purpose in 2020-21 were Rs.14 Lakhs.

(iii) Share issue expenses allowed under section 35(D) of the Income Tax Act, 1963 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.14.00 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 purpose 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 Asset 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	Responding timing difference	Reversal of DTA	7 lakhs × 40% = Rs. 2.8 lakhs

	earlier years was higher.			
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 8 : Nov – 2021 – RTP

Can an enterprise offset deferred tax assets and deferred tax liabilities? If yes, prescribe the conditions required for such offset as per provisions of AS 22.

Solution :

Yes. It can offset deferred tax assets and deferred tax liabilities.

As per AS 22, an enterprise should offset deferred tax assets and deferred tax liabilities if:

(i) the enterprise has a legally enforceable right to set off assets against liabilities representing current tax; and

(ii) the deferred tax assets and the deferred tax liabilities relate to taxes on income levied by the same governing taxation laws.

Question 9 : May – 2022 – RTP

The following transactions were reported by PQR Ltd. during the year 2020-2021:

i	Tax Rate	30% (Rs. in lakh)
ii	Items disallowed in 2019-2020 and allowed for tax purposes in 2020-2021.	20
iii	Interest to Financial Institutions accounted in the books accrual basis, but actual payment was made before the date of filing return and allowed for tax purpose also.	20
iv	Donations to Private Trust made in 2020-2021 (not allowed under Income Tax Laws).	10

You are required to show impact of the above items in terms of Deferred Tax Assets/Deferred Tax Liability for the year ended 31.03.2021.

Solution :

Impact of various items in terms of deferred tax liability/deferred tax asset as per AS 22

Transactions	**Analysis**	**Nature of difference**	**Effect**	**Amount**

Disallowances, as per IT Act, of earlier years	Tax payable for the earlier year was higher on this account.	Timing difference	Reversal of DTA	Rs. 20 lakh × 30% = Rs. 6 lakh
Interest to financial institutions	It is allowed as deduction under IT Act, if the payment is made before the due date of filing the return of income	No timing difference	Not applicable	Not applicable
Donation to private trusts	Not an allowable expenditure under IT Act.	Permanent difference	Not applicable	Not applicable

Question 10 : Nov – 2022 – RTP

Define followings as per AS 22:

(i) Accounting income (loss)

(ii) Taxable income (tax loss)

(iii) Tax expense (tax saving)

Solution :

Accounting income (loss) is the net profit or loss for a period, as reported in the statement of profit and loss, before deducting income-tax expense or adding income tax saving.

Taxable income (tax loss) is the amount of the income (loss) for a period, determined in accordance with the tax laws, based upon which income-tax payable (recoverable) is determined.

Taxable expenses is the aggregate of current tax and deferred tax charged or credited to the statement of profit and loss for the period.

Question 11 : Nov – 2022 – Paper

The following information is furnished in respect of Mohit Limited for the year ending 31st March, 2022.

(i) Depreciation as per accounting records Rs.56,000

Depreciation for income tax records Rs.38,000

The above depreciation does not include depreciation on new addition.

(ii) A new machinery purchased on 1st April, 2021 costing Rs.24,000 on which 100% depreciation is allowed in the 1st Year for income tax purpose, whereas straight line

method of depreciation is considered appropriate for accounting purpose with a life estimation of 4 years.

(iii) The company has made a profit of Rs.1,28,000 before depreciation and taxes.

(iv) Donation to private trust during the year is Rs.15,000 (not allowed under Income tax laws.)

(v) Corporate tax is 40%.

Prepare relevant extract of statement of Profit & Loss for the year ending 31st March, 2022. Also show the effect of the above items on Deferred Tax Liability / Assets as per AS - 22.

Thanks ....

CHAPTER 10

AS 24 DISCONTINUING OPERATIONS

Question 1 : May – 2020 – RTP

(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 the following information relating to a discontinuing operation in its financial statements beginning with the financial statements for the period in which the initial disclosure event (as defined in paragraph 15) occurs:

(a) a description of the discontinuing operation(s);

(b) the business or geographical segment(s) in which it is reported as per AS 17, Segment Reporting;

(c) the date and nature of the initial disclosure event;

(d) the date or period in which the discontinuance is expected to be completed if known or determinable;

(e) the carrying amounts, as of the balance sheet date, of the total assets to be disposed of and the total liabilities to be settled;

(f) the amounts of revenue and expenses in respect of the ordinary activities attributable to the discontinuing operation during the current financial reporting period;

(g) the amount of pre-tax profit or loss from ordinary activities attributable to the discontinuing operation during the current financial reporting period, and the income tax expense related thereto; and

(h) the amounts of net cash flows attributable to the operating, investing, and financing activities of the discontinuing operation during the current financial reporting period.

(ii) Para 3 of AS 24 "Discontinuing Operations" explains the criteria for determination of discontinuing operations. According to Paragraph 9 of AS 24, examples of activities that do not necessarily satisfy criterion (a) of paragraph 3, 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.

An example in relation to consolidated financial statements is selling a subsidiary whose activities are similar to those of the parent or other subsidiaries.

Question 2 : Nov – 2020 – RTP

What do you understand by Discontinuing Operations? What are the disclosure and presentation requirements of AS 24 for discontinuing operations? Explain in brief.

Solution :

As per AS 24 "Discontinuing Operations", a discontinuing operation is a component of an enterprise:

a. That the enterprise, pursuant to a single plan, is:
   (i) Disposing of substantially in its entirety, such as by selling the component in a single transaction or by demerger or spin-off of ownership of the component to the enterprise's shareholders or
   (ii) Disposing of piecemeal, such as by selling off the component's assets and settling its liabilities individually or
   (iii) Terminating through abandonment and

b. That represents a separate major line of business or geographical area of operations.

c. That can be distinguished operationally and for financial reporting purposes.

An enterprise should include the following information relating to a discontinuing operation in its financial statements beginning with the financial statements for the period in which the initial disclosure event occurs:

- A description of the discontinuing operation(s);
- The business or geographical segment(s) in which it is reported as per AS 17;
- The date and nature of the initial disclosure event.
- The date or period in which the discontinuance is expected to be completed if known or determinable,
- The carrying amounts, as of the balance sheet date, of the total assets to be disposed of and the total liabilities to be settled;
- The amounts of revenue and expenses in respect of the ordinary activities attributable to the discontinuing operation during the current financial reporting period;
- The amount of pre-tax profit or loss from ordinary activities attributable to the discontinuing operation during the current financial reporting period, and the income tax expense related thereto;
- The amounts of net cash flows attributable to the operating, investing, and financing activities of the discontinuing operation during the current financial reporting period.

Question 3 : May – 2021 – RTP

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 to the commercial vehicles 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 has planned that 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. These plans have not approved from the Board of Directors and the new factory for manufacture of commercial vehicles has not yet started. 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.

Solution :

Mere gradual phasing out is not considered as discontinuing operation as defined under 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.

In view of the above, mere gradual phasing out in itself cannot be considered as discontinuing operation. The companies' strategic plan also has no final approval from the board through a resolution and there is no specific time bound activities like shifting of assets and employees. Moreover, the new segment i.e. commercial vehicle production line in a new factory has not started.

Question 4 : July – 2021 – Paper

Rohini Limited is in the business of manufacture of passenger cars and commercial vehicles. The Company is working on a strategic plan to close the production of passenger cars and to produce only commercial vehicles over the coming 5 years. However no specific plans have been drawn up for sale of neither the division not its assets. As part of its prospective plan it will reduce the production of passenger cars by 20% annually. It also plans to establish another new factory for the manufacturer of commercial vehicles and transfer surplus employees in a phased manner. You are required to comment :

(i) If mere gradual phasing out in itself can be considered as a 'discounting 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?

Solution :

(i) As per AS 24, a discontinuing operation is a component of an enterprise:

(a) that the enterprise, pursuant to a single plan, is:

(i) disposing of substantially in its entirety, such as by selling the component in a single transaction or by demerger or spin-off of ownership of the component to the enterprise's shareholders; or

(ii) disposing of piecemeal, such as by selling off the component's assets and settling its liabilities individually; or

(iii) terminating through abandonment; and

(b) that represents a separate major line of business or geographical area of operations; and

(c) that can be distinguished operationally and for financial reporting purposes.

Mere gradual phasing out is not considered as discontinuing operation as defined under 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:

(a) Gradual or evolutionary phasing out of a product line or class of service;

(b) Shifting of some production or marketing activities for a particular line of business from one location to another; and

(c) Closing of a facility to achieve productivity improvements or other cost savings.

In this case, it cannot be considered as Discontinuing Operation as per AS-24 as the company's 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. Moreover, the new segment i.e. commercial vehicle production line in a new factory has not started.

(ii) No, the resolution is silent 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, but the closure road map and new segment starting roadmap are missing.

Hence, AS 24 will not be applicable and it cannot be considered as discontinuing operation.

(iii) Yes, phased and time bound program 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 and it will be considered as Discontinuing Operation as per AS-24.

Question 5 : Nov – 2021 – RTP

What are discontinuing operations as per AS 24? Should an enterprise include prescribed information relating to a discontinuing operation in its financial statements?

Solution :

A discontinuing operation is a component of an enterprise:

a. That the enterprise, pursuant to a single plan, is:

(i) Disposing of substantially in its entirety, such as by selling the component in a single transaction or by demerger or spin-off of ownership of the component to the enterprise's shareholders or

(ii) Disposing of piecemeal, such as by selling off the component's assets and settling its liabilities individually or

(iii) Terminating through abandonment and

b. That represents a separate major line of business or geographical area of operations.

c. That can be distinguished operationally and for financial reporting purposes.

An enterprise should include prescribed information relating to a discontinuing operation in its financial statements, as per requirements of AS 24, beginning with the financial statements for the period in which the initial disclosure event occurs.

Question 6 : May – 2022 – RTP

(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 the following information relating to a discontinuing operation in its financial statements beginning with the financial statements for the period in which the initial disclosure event occurs:

(a) a description of the discontinuing operation(s);

(b) the business or geographical segment(s) in which it is reported as per AS 17 'Segment Reporting';

(c) the date and nature of the initial disclosure event;

(d) the date or period in which the discontinuance is expected to be completed if known or determinable;

(e) the carrying amounts, as of the balance sheet date, of the total assets to be disposed of and the total liabilities to be settled;

(f) the amounts of revenue and expenses in respect of the ordinary activities attributable to the discontinuing operation during the current financial reporting period;

(g) the amount of pre-tax profit or loss from ordinary activities attributable to the discontinuing operation during the current financial reporting period, and the income tax expense related thereto; and

(h) the amounts of net cash flows attributable to the operating, investing, and financing activities of the discontinuing operation during the current financial reporting period.

(ii) Para 3 of AS 24 "Discontinuing Operations" explains the criteria for determination of discontinuing operations. According to AS 24, examples of activities that do not necessarily satisfy criterion (a) of paragraph 3, but that might do so in combination with other circumstances, include:

(i) Gradual or evolutionary phasing out of a product line or class of service;
(ii) Discontinuing, even if relatively abruptly, several products within an ongoing line of business;
(iii) Shifting of some production or marketing activities for a particular line of business from one location to another; and
(iv) Closing of a facility to achieve productivity improvements or other cost savings.

An example in relation to consolidated financial statements is selling a subsidiary whose activities are similar to those of the parent or other subsidiaries.

Question 7 : Nov – 2022 – RTP

What are the disclosure requirement in interim financial reports as per AS 24 for discontinuing operations?

Solution :

Disclosure in interim financial reports

Disclosures in an interim financial report in respect of a discontinuing operation should be made in accordance with AS 25, 'Interim Financial Reporting', including:

(a) Any significant activities or events since the end of the most recent annual reporting period relating to a discontinuing operation and
(b) Any significant changes in the amount or timing of cash flows relating to the assets to be disposed or liabilities to be settled.

Thanks ....

Rahul Malkan

CHAPTER 11

AS 26 INTANGIBLE ASSETS

Question 1 : May – 2018 – Paper

A company acquired a patent at a cost of Rs. 160 lakhs for a period of 5 years and the product life cycle is also 5 years. The company capitalized the cost and started amortising the asset at Rs. 16 lakhs per year based on the economic benefits derived from the product manufactured under the patent. After 2 years it was found that the product life cycle may continue for another 5 years from then (the patent is renewable and the company can get it renewed after 5 years). The net cash flows from the product during these 5 years were expected to be Rs. 50 lakhs, Rs. 30 lakhs, Rs. 60 lakhs, Rs. 70 lakhs and Rs. 40 lakhs. Find out the amortization cost of the patent for each of the years.

Solution :

Company amortized Rs. 16,00,000 per annum for the first two years. Hence, Amortization for the first two years (Rs. 16,00,000 X 2) = Rs. 32,00,000.

Remaining carrying cost after two years =Rs. 1,60,00,000 – Rs. 32,00,000

= Rs. 1,28,00,000

Since after two years it was found that the product life cycle may continue for another 5 years, hence the remaining carrying cost Rs.128 lakhs will be amortized during next 5 years in the ratio of net cash arising from the sale of the products of Fast Limited.

The amortization cost of the patents may be computed as follows :

Year	Net cash flows Rs.	Amortization Ratio	Amortization Amount Rs.
I	-	0.1	16,00,000
II	-	0.1	16,00,000
III	50,00,000	0.2	25,60,000
IV	30,00,000	0.12	15,36,000
V	60,00,000	0.24	30,72,000
VI	70,00,000	0.28	35,84,000
VII	40,00,000	0.16	20,48,000
Total	250,00,000	1.000	160,00,000

Question 2 : May – 2019 – RTP

A Company with a turnover of Rs. 375 crores and an annual advertising budget of Rs. 3 crores had taken up the marketing of a new product. It was estimated that the company would have a turnover of Rs. 37.5 croes from the new product. The company had debited to its
Profit and Loss account the total expenditure of Rs. 3 crores incurred on extensive special initial advertisement campaign for the new product.
Is the procedure adopted by the Company correct?

Solution :

According to AS 26 'Intangible Assets', "expenditure on an intangible item should be recognized as an expense when it is incurred unless it forms part of the cost of an intangible asset".
In the given case, advertisement expenditure of Rs. 3 crores had been taken up for the marketing of a new product which may provide future economic benefits to an enterprise by having a turnover of Rs.37.5 crores. Here, no intangible asset or another asset is acquired or created that can be recognized.
Therefore, the accounting treatment by the company of debiting the entire advertising expenditure of Rs.3 crores to the Profit and Loss account of the year is correct.

Question 3 : Nov – 2019 – RTP

K Ltd. launched a project for producing product X in October, 2018. The Company incurred Rs.40 lakhs towards Research and Development expenses upto 31st March, 2019. Due to prevailing market conditions, the Management came to conclusion that the product cannot be manufactured and sold in the market for the next 10 years. The Management hence wants to defer the expenditure write off to future years.
Advise the Company as per the applicable Accounting Standard.

Solution :

As per para 41 of AS 26 "Intangible Assets", expenditure on research should be recognized as an expense when it is incurred. An intangible asset arising from development (or from the development phase of an internal project) should be recognized if, and only if, an enterprise can demonstrate all of the conditions specified in para 44 of the standard. An intangible asset (arising from development) should be derecognised when no future economic benefits are expected from its use according to para 87 of the standard. Thus, the manager cannot defer the expenditure write off to future years in the given case.
Hence, the expenses amounting Rs. 40 lakhs incurred on the research and development project has to be written off in the current year ending 31st March, 2019.

Question 4 : Nov – 2019 – Paper

As per provisions of AS-26, how would you deal to the following situations:

(1) Rs.23,00,000 paid by a manufacturing company to the legal advisor for defending the patent of a product is treated as a capital expenditure.

(2) During the year 2018-19, a company spent Rs. 7,00,000 for publicity and research expenses on one of its new consumer product which was marketed in the same accounting year but proved to be a failure.

(3) A company spent Rs.25,00,000 in the past three years to develop a product, these expenses were charged to profit and loss account since they did not meet AS-26 criteria for capitalization. In the current year approval of the concerned authority has been received. The company wishes to capitalize Rs.25,00,000 by disclosing it as a prior period item.

(4) A company with a turnover of Rs.200 crores and an annual advertising budget of Rs.50,00,000 had taken up for the marketing of a new product by a company. It was estimated that the company would have a turnover of Rs.20 crore from the new product.

The company had debited to its Profit & Loss Account the total expenditure of Rs.50,00,000 incurred on extensive special initial advertisement campaign for the new product.

Solution :

As per AS 26 "Intangible Assets", subsequent expenditure on an intangible asset after its purchase or its completion should be recognized as an expense when it is incurred unless (a) it is probable that the expenditure will enable the asset to generate future economic benefits in excess of its originally assessed standard of performance; and (b) expenditure can be measured and attributed to the asset reliably. If these conditions are met, the subsequent expenditure should be added to the cost of the intangible asset.

(i) In the given case, the legal expenses to defend the patent of a product amounting Rs. 23,00,000 should not be capitalized and be charged to Profit and Loss Statement.

(ii) The company is required to expense the entire amount of Rs. 7,00,000 in the Profit and Loss account for the year ended 31st March, 2019 because no benefit will arise in the future.

(iii) As per AS 26, expenditure on an intangible item that was initially recognized as an expense by a reporting enterprise in previous annual financial statements should not be recognized as part of the cost of an intangible asset at a later date. Thus the company cannot capitalize the amount of Rs. 25,00,000 and it should be recognized as expense

(iv) Expenditure of Rs. 50,00,000 on advertising and promotional activities should always be charged to Profit and Loss Statement. Hence, the company has done the correct treatment by debiting the sum of 50 lakhs to Profit and Loss Account.

Question 5 : May – 2020 – RTP

A company acquired patent right for Rs.1200 lakhs. The product life cycle has been estimated to be 5 years and the amortization was decided in the ratio of estimated future cash flows which are as under:

Year	1	2	3	4	5
Estimated future cash flows (Rs. in lakhs)	600	600	600	300	300

After 3rd year, it was ascertained that the patent would have an estimated balance future life of 3 years and the estimated cash flow after 5th year is expected to be Rs.150 lakhs. You are required to determine the amortization pattern under Accounting Standard 26.

Solution :

Amortization of cost of patent as per AS 26

Year	Estimated future cash flow (Rs.in lakhs)	Amortization Ratio	Amortized Amount (Rs.in lakhs)
1	600	.25	300
2	600	.25	300
3	600	.25	300
4	300	.40 (Revised)	120
5	300	.40 (Revised)	120
6	150	.20 (Revised)	60
			1,200

In the first three years, the patent cost will be amortized in the ratio of estimated future cash flows i.e. (600: 600: 600: 300: 300).

The unamortized amount of the patent after third year will be Rs. 300 lakh (1,200-900) which will be amortized in the ratio of revised estimated future cash flows (300:300:150) in the fourth, fifth and sixth year.

Question 6 : Nov – 2020 – RTP

X Ltd. carried on business of manufacturing of Bakery products. The company has two trademarks "Sun" and "Surya''. One month before, the company comes to know through one of the marketing managers that both trademarks have allegedly been infringed by other competitors engaged in the same field. After investigation, legal department of the company informed that it had weak case on trademark “Sun” and strong case in regard to trademark “Surya”'. X Ltd. incurred additional legal fees to stop infringement on both trademarks. Both trademarks have a remaining legal life of 10 years. How should X Ltd. account for these legal costs incurred relating to the two trademarks?

Solution :

As per AS 26, subsequent expenditure on an intangible asset after its purchase or its completion should be recognized as an expense. However, if the subsequent expenditure enables the asset to generate future economic benefits in excess of its originally assessed standard of performance or can be measured and attributed to the asset reliably, then such subsequent expenditure should be added to the cost of the intangible asset.

The legal costs incurred for both the trademarks do not enable them to generate future economic benefits in excess of its originally assessed standard of performance. They only ensure to maintain them if the case is decided in favour of the company. Therefore, such legal costs incurred for both trademarks must be recognized as an expense.

Question 7 : Nov – 2020 – Paper

Swift Limited acquired patent rights to manufacture Solar Roof Top Panels at a cost of Rs. 600 lacs. The product life cycle has been estimated to be 5 years and the amortization was decided in the ratio of future cash flows which are estimated as under

Year	1	2	3	4	5
Cash Flows (Rs. In lacs)	300	300	300	150	150

After 3rd year, it was estimated that the patents would have an estimated balance future life of 3 years and Swift Ltd. Expected the estimated cash flow after 5th Year to be 75 lacs. Determine the amortization cost of the patent for each of the above years as per Accounting standards 26.

Solution :

Amortization of cost of patent as per AS 26

Year	Estimated future cash flow (Rs. in lakhs)	Amortization Ratio	Amortized Amount (Rs. in lakhs)
1	300	.25	150
2	300	.25	150
3	300	.25	150
4	150	.10	60
5	150	.10	60
6	75	.05	30
		1.00	600

In the first three years, the patent cost will be amortized in the ratio of estimated future cash flows i.e. (300: 300: 300: 150: 150).The unamortized amount of the patent after third year will be Rs. 150 lakh (600-450) which will be amortized in the ratio of revised estimated future cash flows (150:150:75 or 2:2:1) in the fourth, fifth and sixth year.

Question 8 : Nov – 2020 – Paper

M/s. Pasa Ltd is developing a new production process. During the financial year ended 31st March 2019, the total expenditure incurred on the process was Rs. 80 lakhs. The production process met the criteria for recognition as on intangible asset on 01st November 2018. Expenditure incurred till this date was Rs. 42 lakhs.

Further expenditure incurred on the process for the financial year ending 31st March 2020 was Rs. 90 Lakhs. As on 31.03.2020, the recoverable amount of know how to embodied in the process is estimated to be Rs. 82 lakhs. This includes estimates of future cash outflows and inflows

You are required to work out:

1. What is the expenditure to be charged to Profit and Loss Account for the year ended 31st March 2019?
2. What is the carrying amount of the intangible asset as on 31st March 2019?
3. What is the expenditure to be charged to Profit & Loss Account for the year ended 31st March 2020?
4. What is the carrying amount of the intangible asset as on 31st March 2020?

Solution :

As per AS 26 'Intangible Assets'

(i) Expenditure to be charged to Profit and Loss account for the year ending 31.03.2019

Rs. 42 lakhs is recognized as an expense because the recognition criteria were not met until 1st November, 2018. This expenditure will not form part of the cost of the production process recognized as an intangible asset in the balance sheet.

(ii) Carrying value of intangible asset as on 31.03.2019

At the end of financial year, on 31st March 2019, the production process will be recognized (i.e. carrying amount) as an intangible asset at a cost of Rs. 38 (80-42) lakhs (expenditure incurred since the date the recognition criteria were met, i.e., from 1st November 2018)

(iii) Expenditure to be charged to Profit and Loss account for the year ended 31.03.2020

	(Rs. in lacs)
Carrying Amount as on 31.03.2019	38
Expenditure during 2019 – 2020	90
Book Value	128
Recoverable Amount	(82)
Impairment loss to be charged to Profit and loss account	46

(iv) Carrying value of intangible asset as on 31.03.2020

	(Rs. in lacs)
Book Value	128
Less: Impairment loss	(46)
Carrying amount as on 31.03.2020	82

Question 9 : Jan – 2021 – Paper

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 expenditure were :

(i) Import Duty 10%

(ii) Additional Import Duty 5%

(iii) Entry Tax 2% (Recoverable later from tax department).

(iv) Installation expense Rs.1,50,000.

(v) Professional fees for clearance from customs Rs.50,000.

Computer the cost of software to be Capitalised 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)	1,46,25,000
Add: Import duty on cost @ 10% (Rs.)	14,62,500
	1,60,87,500
Add: Additional import duty @ 5% (Rs.)	8,04,375
	1,68,91,875
Add: Installation expenses (Rs.)	1,50,000
Add: Professional fee for clearance from customs (Rs.)	50,000
Cost of the software to be capitalized (Rs.)	1,70,91,875

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 10 : May – 2021 – RTP

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) Non-current assets		
Intangible assets	1	8,11,200

Notes to Accounts (Extract)

		Rs.	Rs.
1	Intangible assets		
	Goodwill (Refer to note 1)	4,51,200	
	Franchise (Refer to Note 2)	1,50,000	
	Patents (Refer to Note 3)	2,10,000	8,11,200

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

Question 11 : Nov – 2021 – RTP

A company is showing an intangible asset at Rs. 88 lakhs as on 01.04.2021. This asset was acquired for Rs. 120 lakhs on 01.04.2017 and the same was available for use from that date. The company has been following the policy of amortization of the intangible assets over a period of 15 years on straight line basis. Comment on the accounting treatment of the above with reference to the relevant Accounting Standard.

Solution :

As per AS 26 'Intangible Assets', the depreciable amount of an intangible asset should be allocated on systematic basis over the best estimate of its useful life. There is a rebuttable presumption that the useful life of an intangible asset will not exceed ten years from the date when the asset is available for use. Company has been following the policy of amortization of the intangible asset over a period of 15 years on straight line basis. The period of 15 years is more than the maximum period of 10 years specified as per AS 26. Accordingly, the company would be required to restate the carrying amount of intangible asset as on 01.04.2021 at Rs. 72 lakhs i.e. Rs. 120 lakhs less Rs. 48 lakhs $\left(\frac{\text{Rs.120 Lakhs}}{10\text{ years}} \times 4\text{ years} = 48\text{ lakhs}\right)$

The difference of Rs. 16 Lakhs (Rs. 88 lakhs – Rs. 72 lakhs) will be adjusted against the opening balance of revenue reserve. The carrying amount of Rs. 72 lakhs will be amortized over remaining 6 years by amortizing Rs. 12 lakhs per year.

Question 12 : Dec – 2021 – Paper

Surgical Ltd. is developing a new production process of surgical equipment. During the financial year ended 31st March, 2020 the total expenditure incurrent on the process was Rs.67 lakhs. The production process met the criteria for recognition as an intangible assets on 1st January, 2020. Expenditure incurred till this date was Rs.35 lakhs.

Further expenditure incurrent on the process for the financial year ending 31st March, 2021 was Rs.105 lakhs. As on 31st March, 2021, the recoverable amount of technique embodied in the process is estimated to be Rs.89 lakhs. This includes estimates of further cash outflows and inflows.

Under the provisions of AS 26, you are required to ascertain :

(i) The expenditure to be charged to Profit and Loss account for the year ended 31st March, 2020;

(ii) Carrying amount of the intangible asset as on 31st March, 020;

(iii) Expenditure to be charged to Profit and Loss Account for the year ended 31st March, 2021;

(iv) Carrying amount of the intangible asset as on 31st March, 2021.

Solution :

As per AS 26 'Intangible Assets'

(i) **Exhpenditure to be charged to Profit and Loss account for the year ended 31.03.2020**

Rs. 35 lakhs is recognized as an expense because the recognition criteria were not met until 1stJanuary 2020. This expenditure will not form part of the cost of the production process recognized as an intangible asset in the balance sheet.

(ii) **Carrying value of intangible asset as on 31.03.2020**

At the end of financial year, on 31st March 2020, the production process will be recognized (i.e. carrying amount) as an intangible asset at a cost of Rs. 32 (67-35) lacs (expenditure incurred since the date the recognition criteria were met, i.e., from 1stJanuary 2020).

(iii) **Expenditure to be charged to Profit and Loss account for the year ended 31.03.2021**

	(Rs. in lacs)
Carrying Amount as on 31.03.2020	32
Expenditure during 2020 – 2021	105
Book Value	137
Recoverable Amount	(89)
Impairment loss	48

Rs. 48 lakhs to be charged to Profit and loss account for the year ending 31.03.2021.

(iv) **Carrying value of intangible asset as on 31.03.2021**

	(Rs. in lacs)
Book Value	137
Less: Impairment loss	(48)
Carrying amount as on 31.03.2021	89

Question 13 : May – 2022 – RTP

PQR Ltd. has acquired a Brand from another company for Rs. 100 lakhs. PQR Ltd. contends that since the said brand is a very popular and famous brand, no amortization needs to be provided. Comment on this in line with the Accounting Standards.

Solution :

AS 26 'Intangible Assets" provides that an intangible asset should be measured initially at cost. After initial recognition, an intangible asset should be carried at cost less any accumulated amortization and any accumulated impairment losses. The amount of an intangible asset should be allocated on a systematic basis over the best estimate of its useful life for computing amortization. There is a rebuttable presumption that the useful life of an intangible asset will not exceed 10 years from the date when the asset is available for use. It must be ensured that the value of brand is amortized in accordance with AS 26, as brand is considered to be intangible asset. The contention of PQR Ltd. that Brand is very popular and famous, hence no amortization needs to be provided is not correct as there is no persuasive evidence that the useful life of the intangible asset will exceed 10 years.

Question 14 : May – 2022 – RTP

X Ltd. is engaged in the business of newspaper and radio broadcasting. It operates through different brand names. During the year ended 31st March, 2021, it incurred substantial amount on business communication and branding expenses by participation in various corporate social responsibility initiatives. The company expects to benefit by this expenditure by attracting new customers over a period of time and accordingly it has capitalized the same under brand development expenses and intends to amortize the same over the period in which it expects the benefits to flow. As the accountant of the company do you concur with these views? You are required to explain in line with provisions of Accounting Standards.

Solution :

As per AS 26 on Intangible Assets, expenditure on an intangible item should be recognized as on expense when it is incurred unless it forms part of the cost of an intangible asset that meets the recognition criteria. An intangible asset should be recognized if, and only if: (i) it is probable that the future economic benefits that are attributable to the asset will flow to the enterprise; and (ii) the cost of the asset can be measured reliably. In the given case, no intangible assets or other asset is acquired or created that can be recognized, the accounting treatment by the company to amortize the entire expenditure over the period in which it expects the benefits to flow is not correct and the same should be debited to the profit and loss statement during the year ended 31st March, 2021.

Question 15 : Nov – 2022 – RTP

K Ltd. launched a project for producing product X in October, 2021. The Company incurred Rs. 40 lakhs towards Research and Development expenses upto 31st March, 2022. Due to prevailing market conditions, the Management came to conclusion that the product cannot be manufactured and sold in the market for the next 10 years. The Management hence wants to defer the expenditure write off to future years.

Advise the Company as per the applicable Accounting Standard.

Solution :

As per AS 26 "Intangible Assets", expenditure on research should be recognized as an expense when it is incurred. An intangible asset arising from development (or from the development phase of an internal project) should be recognized if, and only if, an enterprise can demonstrate all of the conditions specified in the standard. An intangible asset (arising from development) should be derecognised when no future economic benefits are expected from its use according to the standard. Thus, the manager cannot defer the expenditure write off to future years in the given case.

Hence, the expenses amounting Rs. 40 lakhs incurred on the research and development project has to be written off in the current year ending 31st March, 2022.

Thanks ....

Rahul Malkan

CHAPTER 12

AS 29 PROVISIONS, CONTINGENT LIABILITIES & CONTINGENT ASSETS

Question 1 : May – 2019 – RTP

M/s. XYZ Ltd. is in a dispute with a competitor company. The dispute is regarding alleged infringement of Copyrights. The competitor has filed a suit in the court of law seeking damages of Rs.200 lacs.

The Directors are of the view that the claim can be successfully resisted by the Company.

How would the matter be dealt in the annual accounts of the Company in the light of AS 29? Explain in brief giving reasons for your answer.

Solution :

As per AS 29, 'Provisions, Contingent Liabilities and Contingent Assets', a provision should be recognized when

(a) an enterprise has a present obligation as a result of a past event;

(b) it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation; and

(c) a reliable estimate can be made of the amount of the obligation.

If these conditions are not met, no provision should be recognized.

In the given situation, since, the directors of the company are of the opinion that the claim can be successfully resisted by the company, therefore there will be no outflow of the resources. Hence, no provision is required. The company will disclose the same as contingent liability by way of the following note:

"Litigation is in process against the company relating to a dispute with a competitor who alleges that the company has infringed copyrights and is seeking damages of Rs. 200 lakhs. However, the directors are of the opinion that the claim can be successfully resisted by the company."

Question 2 : Nov – 2019 – RTP

XYZ Ltd. has not made provision for warrantee in respect of certain goods due to the fact that the company can claim the warranty cost from the original supplier. Hence the accountant of the company says that the company is not having any liability for warrantees on a particular date as the amount gets reimbursed. You are required to comment on the accounting treatment done by the XYZ Ltd. in line with the provisions of AS 29.

Solution :

As per para 46 of AS 29 "Provisions, Contingent Liabilities and Contingent Assets", where some or all of the expenditure required to settle a provision is expected to be reimbursed by another

party, the reimbursement should be recognised when, and only when, it is virtually certain that reimbursement will be received if the enterprise settles the obligation. The reimbursement should be treated as a separate asset. The amount recognised for the reimbursement should not exceed the amount of the provision.

It is apparent from the question that the company had not made provision for warranty in respect of certain goods considering that the company can claim the warranty cost from the original supplier. However, the provision for warranty should have been made as per AS 29 and the amount claimable as reimbursement should be treated as a separate asset in the financial statements of the company rather than omitting the disclosure of such liability. Accordingly, it is viewed that the accounting treatment adopted by the company with respect to warranty is not correct.

Question 3 : Nov – 2019 – Paper

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.)**
11th Feb, 2017	60,000
25th Dec, 2017	40,000
04th 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.

Solution :

Provision to be made for warranty under AS 29 ‘Provisions, Contingent Liabilities and Contingent Assets’

As at 31st March, 2018 = Rs. 60,000 x .02 + Rs. 40,000 x .03

= Rs. 1,200 + Rs. 1,200 = Rs. 2,400

As at 31st 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	(2,400)
Amount debited to profit and loss account	2,450

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 4 : May – 2020 – RTP

With reference to AS 29, how would you deal with the following in the annual accounts of the company at the Balance Sheet dates:

(i) 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.

(ii) 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).

Solution :

(i) 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.

(ii) 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 5 : Nov – 2020 – RTP

How will you distinguish contingent assets with Contingent Liabilities. Explain in brief.

Solution :

A Contingent liability is a possible obligation that arises from past events and the existence of which will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly within the control of the enterprise; or

A present obligation that arises from past events but is not recognized because:

(i) It is not probable that an outflow of resources embodying economic benefits will be required to settle the obligation; or

(ii) A reliable estimate of the amount of the obligation cannot be made.

An enterprise should not recognize a contingent liability but should be disclosed. A contingent liability is disclosed, unless the possibility of an outflow of resources embodying economic benefits is remote.

Contingent assets usually arise from unplanned or other unexpected events that give rise to the possibility of an inflow of economic benefits to the enterprise. An example is a claim that an enterprise is pursuing through legal processes, where the outcome is uncertain. An enterprise should not recognize a contingent asset, since this may result in the recognition of income that may never be realized. However, when the realization of income is virtually certain, then the related asset is not a contingent asset and its recognition is appropriate. A contingent asset is not disclosed in the financial statements. It is usually disclosed in the report of the approving authority (Board of Directors in the case of a company, and, the corresponding approving authority in the case of any other enterprise), where an inflow of economic benefits is probable. Contingent assets are assessed continually and if it has become virtually certain that an inflow of economic benefits will arise, the asset and the related income are recognised in the financial statements of the period in which the change occurs.

Question 6 : Nov – 2020 – RTP

Alpha Ltd. has entered into a sale contract of Rs. 7 crores with Gamma Ltd. during 2018-19 financial year. The profit on this transaction is Rs. 1 crore. The delivery of goods to take place during the first month of 2019-20 financial year. In case of failure of Alpha Ltd. to deliver within the schedule, a compensation of Rs.2 crores is to be paid to Gamma Ltd. Alpha Ltd. planned to manufacture the goods during the last month of 2018-19 financial year. As on balance sheet date (31.3.2019), the goods were not manufactured and it was unlikely that Alpha Ltd. will be in a position to meet the contractual obligation. You are required to advise Alpha Ltd. on requirement of provision for contingency in the financial statements for the year ended 31st March, 2019, in line with provisions of AS 29?

Solution :

AS 29 "Provisions, Contingent Liabilities and Contingent Assets" provides that when an enterprise has a present obligation, as a result of past events, that probably requires an outflow of resources and a reliable estimate can be made of the amount of obligation, a provision should be recognized. Alpha Ltd. has the obligation to deliver the goods within the scheduled time as per

the contract. It is probable that Alpha Ltd. will fail to deliver the goods within the schedule and it is also possible to estimate the amount of compensation. Therefore, Alpha Ltd. should provide for the contingency amounting Rs. 2 crores as per AS 29.

Question 7 : Nov – 2020 – Paper

With Reference to AS 29, how would you deal with the following in the Annual Accounts of the company at the Balance Sheet date:

1. The company operates an offshore oilfield where its licensing agreement requires it to remove the oil rig at the end of the production and restore the seabed. Eighty five percent of the eventual costs relate to the removal of the oil rig and restoration of damage caused by building it, and fifteen percent arise through the extraction of oil. At the balance sheet date, rig has been constructed but no oil has been extracted.
2. The Government introduces a number of changes to the taxation laws. As a result of these changes, the company will need to train a large proportion of its accounting and legal workforce in order to ensure continued compliances with tax law regulations. At the balance sheet date, no retraining of staff has taken place.

Solution :

(i) 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 85% 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. 15% of costs that arise through the extraction of oil are recognized as a liability when the oil is extracted.

(ii) As per AS 29, a provision for restructuring costs is recognized only when the recognition criteria for provisions are met. A restructuring provision does not include costs as of retraining or relocating continuing staff.

The expenditures of training the staff related to the future conduct of the business and are not liabilities for restructuring at the balance sheet date. Such expenditures are recognized on the same basis as if they arose independently of a restructuring. At the balance sheet date, no such expenditure has been incurred hence no provision is required.

Question 8 : May – 2021 – RTP

The company has not made provision for warranty in respect of certain goods considering that the company can claim the warranty cost from the original supplier.

You are required to **examine** in line with the provisions of AS 29.

Solution :

As per provisions of AS 29 "Provisions, Contingent Liabilities and Contingent Assets", where some or all of the expenditure required to settle a provision is expected to be reimbursed by another party, the reimbursement should be recognized when, and only when, it is virtually certain that reimbursement will be received if the enterprise settles the obligation. The reimbursement should be treated as a separate asset. The amount recognized for the reimbursement should not exceed the amount of the provision.

It is apparent from the question that the company had not made provision for warranty in respect of certain goods considering that the company can claim the warranty cost from the original supplier. However, the provision for warranty should have been made as per AS 29 and the amount claimable as reimbursement should be treated as a separate asset in the financial statements of the company rather than omitting the disclosure of such liability. Accordingly, it can be said that the accounting treatment adopted by the company with respect to warranty is not correct.

Question 9 : May – 2021 – RTP

Explain whether provision is required in the following situations in line with AS 29:

(i) There is a present obligation that probably requires an outflow of resources and a reliable estimate can be made of the amount of obligation;

(ii) There is a possible obligation or a present obligation that may, but probably will not, require an outflow of resources.

(iii) There is a possible obligation or a present obligation where the likelihood of an outflow of resources is remote.

Solution :

(i) There is a present obligation that probably requires an outflow of resources and a reliable estimate can be made of the amount of obligation – Provision is recognised. Disclosures are required for the provision.

(ii) There is a possible obligation or a present obligation that may, but probably will not, require an outflow of resources – No provision is recognised. Disclosures are required for the contingent liability.

(iii) There is a possible obligation or a present obligation where the likelihood of an outflow of resources is remote – No provision is recognised. No disclosure is required.

Question 10 : Nov – 2021 – RTP

A company, incorporated as NPO under the Companies Act, is having main objective to promote the trade by organizing trade fairs / exhibitions. While 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 accounting treatment and disclosure was made by the company in its financial statements as: (i) 5% contingency charges are treated as income and matching provision for the same is also being made in accounts and (ii) suitable disclosure to this effect is also made in the notes forming part of accounts.
You are required to comment whether creation of provision for contingencies considering the facts and circumstances of the case is required in line with AS 29.

Solution :

As per AS 29 "Provisions, Contingent Liabilities and Contingent Assets", a provision should be recognized 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 recognized.
From the above, it is clear that for the contingencies considered by the company, neither a present obligation exists because of past event, nor a reliable estimate can be made of the amount of the obligation. Accordingly, a provision cannot be recognized for such contingencies under the facts and circumstances of the case.

Question 11 : Nov – 2021 – RTP

An oil company has been contaminating land for several years. It does not clean up because there is no legislation requiring cleaning up. On 31st March 2021, it is virtually certain that a law requiring a clean-up of land already contaminated will be enacted shortly after the year end. Is provisioning presently necessary considering the circumstances in line with provisions of AS 29?

Solution :

As per AS 29 ‘Provisions, Contingent Liabilities and Contingent Assets’, a past event will lead to present obligation when the enterprise has no realistic alternative to settle the obligation created by the past event. However, when environmental damage is caused there may be no obligation to remedy the consequences. The causing of the damage will become an obligating event when a new law requires the existing damage to be rectified. Where details of a proposed new law have yet to be finalised, an obligation arises only when the legislation is virtually certain to be enacted. In the given case it is virtually certain that law will be enacted requiring clean-up of a land already contaminated. Therefore, an oil company has to provide for such clean-up cost in the year in which the law is virtually certain to be enacted.

Question 12 : May – 2022 – RTP

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

(ii) 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 31st 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% of Rs. 5,00,00,000 = Rs. 5,00,000

Estimated cost of repair / replacement = Rs. 5,00,000 x 10% = Rs. 50,000.

Question 13 : May – 2022 – Paper

Alloy Fabrication Limited is engaged in manufacturing of iron and steel rods. The company is in the process of finalisation of the accounts for the year ended 31st March, 2022 and needs your advice on the following issues in line with the provisions of AS-29 .

(i) On 1st April, 2019, the company installed a huge furnace in their plant. The furnace has a lining that needs to be replaced every five years for technical reasons. At the Balance Sheet date 31st March, 2022, the company does not provide any provision for replacement of lining of the furnace.

(ii) A case has been filed against the company in the consumer court and a notice for levy of a penalty of 50 Lakhs has been received. The company has appointed a lawyer to defend the case for a fee of Rs.5 Lakhs. 60% of the fees have been paid in advance and rest 40% will be paid after finalisation of the case. There are 70% chances that the penalty may not be levied.

Solution :

(i) A provision should be recognized only when an enterprise has a present obligation arising from a past event or obligation. In the given case, there is no present obligation but a future one, therefore no provision is recognized as per AS 29. The cost of replacement of lining of furnace is not recognized as a provision because it is a future obligation. Even a legal requirement does not require the company to make a provision for the cost of replacement because there is no present obligation. Even the intention to incur the expenditure depends on the company deciding to continue operating the furnace or to replace the lining.

(ii) 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 70% chances that the penalty may not be levied. Accordingly, Alloy Fabrication Ltd. should not make the provision for penalty. The matter is disclosed as a contingent liability unless the probability of any outflow is regarded as remote.

However, a provision should be made for remaining 40% fees of the lawyer amounting Rs. 2,00,000 in the financial statements of financial year 2021-2022.

Question 14 : Nov – 2022 – RTP

Chaos Limited is in the process of finalizing its accounts for the year ended 31st March, 2022. It seeks your advice in the following cases:

(i) Chaos Limited entered into an agreement to supply 1 lac face masks to D Limited by 30th April, 2022 failing which it will have to pay a penalty of Rs. 10 per item not supplied. On 31st March, 2022 Chaos Limited assessed that it could only supply 50,000 face masks to D Limited by 30th April, 2022.

(ii) Chaos Limited has filed a court case in 2014-2015 against its competitors. It is evident to its lawyers 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.

(iii) A new regulation has been passed in 2021-22 by the healthcare ministry to upgrade facilities. Deadline set by the government is 31.03.2023. The company estimates an expenditure of Rs. 10,00,000 for the said upgrade.

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:

(a) an entity has a present obligation (legal or constructive) as a result of a past event;

(b) it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation; and

(c) a reliable estimate can be made of the amount of the obligation. If these conditions are not met, no provision shall be recognised."

Accounting treatment under the given scenarios:

(i) In this case, there is no present obligation arising out of a past event as the goods are scheduled for delivery on 30th April, 2022 and there is no delay as at 31st March, 2022. Hence, there is no present obligation to pay the penalty in the current year. Therefore, no provision can be recognized in the instant case.

(ii) On 31st March, 2022, 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.

(iii) Under new regulation, an entity is required to upgrade its facilities by 31st March, 2023. However, on 31st March, 2022, 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 recognised on 31st March, 2022 for upgrading the facilities by 31st March, 2023.

Question 15 : Nov – 2022 – Paper

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 (?)
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 as a separate entity. Ascertain the amount of contingent loss and the accounting treatment in respect thereof as per AS - 29.

Thanks ....

CHAPTER 13

DISSOLUTION OF PARTNERSHIP FIRM

Question 1 : May – 2020 – RTP

Ram, Wazir and Adil give you the following Balance Sheet as on 31st March, 2019:

Liabilities		Rs.	Assets		Rs.
Ram's Loan		15,000	Plant and Machinery at cost		30,000
Capital Accounts:			Fixtures and Fittings		2,000
Ram	30,000		Stock		10,400
Wazir	10,000		Debtors	18,400	
Adil	2,000	42,000	Less: Provision	(400)	18,000
Sundry Creditors		17,800	Joint Life Policy		15,000
Loan on Hypothecation of Stock		6,200	Patents and Trademarks		10,000
Joint Life Policy Reserve		12,400	Cash at Bank		8,000
		93,400			**93,400**

The partners shared profits and losses in the ratio of Ram 4/9, Wazir 2/9 and Adil 1/3. Firm was dissolved on 31st March, 2019 and you are given the following information:

(a) Adil had taken a loan from insurers for Rs. 5,000 on the security of Joint Life Policy. The policy was surrendered and Insurers paid a sum of Rs. 10,200 after deducting Rs. 5,000 for Adil's loan and Rs. 300 as interest thereon.

(b) One of the creditors took some of the patents whose book value was Rs. 6,000 at a valuation of Rs. 4,500. The balance to that creditor was paid in cash.

(c) The firm had previously purchased some shares in a joint stock company and had written them off on finding them useless. The shares were now found to be worth Rs. 3,000 and the loan creditor agreed to accept the shares at this value.

(d) The remaining assets realized the following amount:

	Rs.
Plant and Machinery	17,000
Fixtures and Fittings	1,000
Stock	9,000
Debtors	16,500

Patents at 50% of their book value.

(e) The liabilities were paid and a total discount of Rs. 500 was allowed by the creditors.

(f) The expenses of realization amounted to Rs. 2,300.

You are required to prepare the Realization Account, Bank Account and Partners' Capital Accounts in columnar form. Also provide necessary working notes in your answer.

Solution :

Realisation Account

	Rs.			Rs.
To Plant and machinery	30,000	By Provision for doubtful debts		400
To Fixtures and fittings	2,000	By Loan on hypothecation of stock (W.N.3)		3,000
To Stock	10,400	By Creditors (W.N.2)		500
To Debtors	18,400	By Joint Life Policy A/c (W.N.4)		12,900
To Patents and Trademarks (W.N.5)	5,500	By Bank		
To Bank	2,300	Plant and machinery	17,000	
		Fixtures and fittings	1,000	
		Stock	9,000	
		Debtors	16,500	
		Patents and Trademarks	2,000	45,500
		By Partners' Capital Accounts		
		Ram	2,800	
		Wazir	1,400	
		Adil	2,100	6,300
	68,600			**68,600**

Bank Account

	Rs.		Rs.
To Balance b/d	8,000	By Adil's Capital A/c- drawings	5,300
To Joint Life Policy	15,500	By Loan on hypothecation of stock	3,200
To Realisation A/c	45,500	By Creditors	12,800
To Adil's Capital A/c	5,400	By Realisation A/c (expenses)	2,300
		By Ram's Loan A/c	15,000
		By Ram's Capital A/c	27,200
		By Wazir's Capital A/c	8,600
	74,400		**74,400**

Partner's Capital Accounts

	Ram Rs.	Wazir Rs.	Adil Rs.		Ram Rs.	Wazir Rs.	Adil Rs.
To Bank			5,300	By Balance b/d	30,000	10,000	2,000
To Realisation A/c	2,800	1,400	2,100	By Bank A/c (bal.fig.)			5,400

To Bank (Bal. Fig.)	27,200	8,600					
	30,000	**10,000**	**7,400**		**30,000**	**10,000**	**7,400**

Working Notes :

1. **Ram's Loan Account**

	Rs.		Rs.
To Bank A/c	15,000	By Balance b/d	15,000
	15,000		**15,000**

2. **Sundry Creditors Account**

	Rs.		Rs.
To Patents and Trademarks A/c	4,500	By Balance b/d	17,800
To Realisation A/c	500		
To Bank A/c	12,800		
	17,800		**17,800**

3. **Loan on Hypothecation of Stock Account**

	Rs.		Rs.
To Realisation A/c	3,000	By Balance b/d	6,200
To Bank A/c	3,200		
	6,200		**6,200**

4. **Joint Life Policy Account**

	Rs.		Rs.
To Balance b/d	15,000	By Joint Life Policy Reserve A/c	12,400
To Realisation A/c	12,900	By Bank A/c (10,200 + 5,300)	15,500
	27,900		**27,900**

5. **Patent and Trademarks Account**

	Rs.		Rs.
To Balance b/d	10,000	By Creditors A/c	4,500
		By Realisation A/c	1,500
		By Realisation A/c (bal.fig.)	4,000*
	10,000		**10,000**

Question 2 : Nov – 2020 – RTP

Amit, Sumit and Kumar are partners sharing profit and losses in the ratio 2:2:1. The partners decided to dissolve the partnership on 31st March, 2020 when their Balance Sheet was as under:

Liabilities	Rs.	Assets	Rs.
Capital Accounts:		Land & Building	1,35,000

Amit	55,200	Plant & Machinery		45,000
Sumit	55,200	Furniture		25,500
General Reserve	61,500	Investments		15,000
Kumar's Loan A/c	15,000	Book Debts	60,000	
Loan from D	1,20,000	Less: Prov. for bad debts	(6,000)	54,000
Trade Creditors	30,000	Stock		36,000
Bills Payable	12,000	Bank		13,500
Outstanding Salary	7,500	Capital Withdrawn:		
		Kumar		32,400
Total	**3,56,400**	**Total**		**3,56,400**

The following information is given to you:

(i) Realization expenses amounted to Rs. 18,000 out of which Rs. 3,000 was borne by Amit.

(ii) A creditor agreed to takeover furniture of book value Rs. 12,000 at Rs. 10,800. The rest of the creditors were paid off at a discount of 6.25%.

(iii) The other assets realized as follows:

Furniture	- Remaining taken over by Kumar at 90% of book value
Stock	- Realized 120% of book value
Book Debts	- Rs. 12,000 of debts proved bad, remaining were fully realized
Land & Building	- Realized Rs. 1,65,000
Investments	- Taken over by Amit at 15% discount

(iv) For half of his loan, D accepted Plant & Machinery and Rs. 7,500 cash. The remaining amount was paid at a discount of 10%.

(v) Bills payable were due on an average basis of one month after 31st March, 2020, but they were paid immediately on 31st March @ 6% discount "per annum".

Prepare the Realization Account, Bank Account and Partners' Capital Accounts in columnar form in the books of Partnership firm.

Solution :

Realization Account

	Rs.			Rs.
To Land and Building	1,35,000	By Provision for bad debts		6,000
To Plant and Machinery	45,000	By Loan from D		1,20,000
To Furniture	25,500	By Trade creditors		30,000
To Investments	15,000	By Bills payable		12,000
To Book debts	60,000	By Outstanding salary		7,500
To Stock	36,000	By Kumar - Furniture taken over (13,500 x .9)		12,150
To Bank (Realization expenses)	15,000	By Bank A/c -		
To Amit– Realization expenses	3,000	Stock Realized	43,200	
To Bank A/c -		Land & Building	1,65,000	
Bill payable	11,940	Debtors	48,000	2,56,200
D's Loan	7,500	By Amit (Investment taken over)		12,750

		Rs.		Rs.
D's Loan		54,000		
Creditors		18,000		
Salary		7,500		
To Profit trs/f to partners' capital Accounts				
Amit	9,264			
Sumit	9,264			
Kumar	4,632	23,160		
		4,56,600		**4,56,600**

Bank Account

	Rs.		Rs.
To Balance b/d	13,500	By Realization A/c	
To Realization A/c (assets realized)	2,56,200	(payment of liabilities: 11,940+ 7,500 + 54,000 15,000 + 18,000 + 7,500)	1,13,940
To Kumar	12,618	By Amit	79,314
		By Sumit	89,064
	2,82,318		**2,82,318**

Partners' Capital Accounts

	Amit Rs.	Sumit Rs.	Kumar Rs.		Amit Rs.	Sumit Rs.	Kumar Rs.
To Balance b/d			32,400	By Balance b/d	55,200	55,200	
To Realization A/c (Investment taken over)	12,750			By Kumar's Loan			15,000
To Realization A/c (Furniture taken over)			12,150	By General Reserve	24,600	24,600	12,300
To Bank A/c	79,314	89,064		By Realization A/c (expense)	3,000		
				By Realization A/c (profit)	9,264	9,264	4,632
				By Bank A/c			12,618
	92,064	**89,064**	**44,550**		**92,064**	**89,064**	**44,550**

Working Notes :

1. Payment for Bills Payable

Particulars	Amount (Rs.)
Bills Payable as per Balance Sheet	12,000
Less: Discount for early payment {12,000 x 6% x (1/12)}	60
Amount Paid in Cash	11,940

2. Payment to D's Loan

Particulars	Amount (Rs.)
D's Loan as per Balance Sheet	120,000.00
50% of Loan adjusted as below:	
Plant & Machinery accepted at Book Value (Rs. 45,000) and Rs. 7,500 in cash.	7,500
Balance 50% of Loan adjusted as below:	
In cash after allowing discount of 10% i.e. Rs. 60,000 – Rs. 6,000 = Rs. 54,000.	54,000

3. Payment to Trade Creditors

Particulars	Amount (Rs.)
Trade Creditors as per Balance Sheet	30,000
Less: Furniture of Book Value Rs.12,000 accepted at value Rs.10,800	10,800
	19,200
Less: Discount @ 6.25%	1,200
Amount paid in Cash	18,000

4. Furniture taken over by Kumar

Particulars	Amount (Rs.)
Furniture as per Balance Sheet	25,500
Less: Furniture of Book Value Rs.12000 accepted by trade creditors	12,000
	13,500
Less: 10% of Book Value	1,350
Value of Furniture taken over by Kumar	12,150

Question 3 : Nov – 2020 – RTP

Explain the provisions related with liability of Limited Liability Partnership (LLP) and its partners as per LLP Act, 2008.

Solution :

Under section 27 (3) of the LLP Act, 2008 an obligation of an LLP arising out of a contract or otherwise, shall be solely the obligation of the LLP. The limitations of liability of an LLP and its partners are as follows:

- The Liabilities of an LLP shall be met out of the properties of the LLP;
- A partner is not personally liable, directly or indirectly (for an obligation of an LLP arising out of a contract or otherwise), solely by reason of being a partner in the LLP;
- An LLP is not bound by anything done by a partner in dealing with a person, if:
    - The partner does not have the authority to act on behalf of the LLP in doing a particular act; and
    - The other person knows that the partner has no authority or does not know or believe him to be a partner in the LLP

- The liability of the LLP and the partners perpetrating fraudulent dealings shall be unlimited for all or any of the debts or other liabilities of the LLP.

Question 4 : Nov – 2020 – RTP / Nov – 2020 – Paper

What are circumstances when LLP can be wound up by the Tribunal. Explain in brief.

Solution :

Under section 64 of the LLP Act, 2008, an LLP may be wound up by the Tribunal:

- If the LLP decides that it should be wound up by the Tribunal;
- If for a period of more than six months, the number of partners of the LLP is reduced below two;
- If the LLP is unable to pay its debts;
- If the LLP has acted against the interests of the integrity and sovereignty of India, the security of the state or public order;

If the LLP has defaulted in the filing of the Statement of Account and Solvency with the Registrar for five consecutive financial years;

Question 5 : Nov – 2020 – Paper

Mohan and Sohan were carrying business in partnership, sharing profit and losses equality. The Balance Sheet of the firm as on 31st March 2049 stood as under:

Liabilities		Rs.	Assets		Rs.
Capital Accounts			Leasehold Premises		40,800
Mohan	1,68,000		Plant & Machinery		1,80,000
Sohan	1,56,000	3,24,000	Inventories		72,000
Bank Overdraft		42,000	Trade Receivables		84,000
Trade Payable		72,000	Joint Life Policy		10,800
			Profit & Loss Account		31,200
			Partners Current Account		
			Mohan -	12,000	
			Sohan -	7,200	19,200
Total		**4,38,000**	**Total**		**4,38,000**

The business was carried on till 30th September 2019, The partners withdrew the amounts equal to half the amount of profit made during the period of six months ended on 30th September 2019 equally. The profit was calculated after charging depression @5% per annum on Leasehold premises and 10% per annum on Plant & Machinery.

In the half year, the amounts of Bank overdraft and Trade payables stood reduced by Rs. 18,000 and Rs. 12,000 respectively. On 30th September 2019 the inventories were valued at Rs. 90,000 and Trade Receivables at Rs. 72,000. The Joint Life Policy had been surrendered for Rs. 10,800 before 30th September 2019 and all other terms remained the same as at 31st March 2019.

On 30th September 2019 the firm sold off its business to PKR Ltd. The value of Goodwill was fixed at Rs. 1,20,000 and the rest of the assets and liabilities were values on the basis of their book

values as at 30th September 2019. PKR Ltd. paid the purchase consideration in equity shares of Rs. 10 each.

You are requested to prepare the following

1. Balance Sheet of the firm as at 30th September 2019
2. Realization Account
3. Partners Capital Account showing the final settlement between them

Solution :

(i) Balance Sheet of the Firm as at 30.9.2019

Liabilities	Rs.	Rs.	Assets	Rs.	Rs.
Capital Accounts:			Machinery	1,80,000	
Mohan balance as on 30.9.2019	1,40,400		Less: Depreciation		
Add: Profit for 6 months	15,180		@10% p.a. for 6 months	(9,000)	1,71,000
	1,55,580		Leasehold premises	40,800	
Less: Drawings for 6 months	(7,590)	1,47,990	Less: Written-off @ 5% for 6 months	(1,020)	39,780
Sohan balance as on 30.9.2019	1,33,200		Inventory		90,000
Add: Profit for 6 months	15,180		Trade receivables		72,000
	1,48,380				
Less: Drawings for 6 months	(7,590)	1,40,790			
Trade payables (72,000 – 12,000)		60,000			
Bank overdraft (42,000 – 18,000)		24,000			
		3,72,780			**3,72,780**

(ii) Realization Account

Particulars	Rs.	Particulars	Rs.
To Machinery A/c	1,71,000	By Trade payables A/c	60,000
To Leasehold Premises A/c	39,780	By Bank Overdraft A/c	24,000
To Inventory A/c	90,000	By PKR Ltd. A/c (W.N.1)	4,08,780
To Trade receivables A/c	72,000		
To Mohan Capital A/c	60,000		
To Sohan Capital A/c	60,000		
	4,92,780		**4,92,780**

(iii) Partners' Capital Accounts

Date	Particulars	Mohan	Sohan	Date	Particulars	Mohan	Sohan
1.4.19	To Profit & Loss A/c	15,600	15,600	1.4.19	By Balance b/d	1,68,000	1,56,000
	To Current A/c	12,000	7,200				
30.9.19	Balance c/d	1,40,400	1,33,200				
		1,68,000	**1,56,000**			**1,68,000**	**1,56,000**
30.9.19	To Drawings A/c	7,590	7,590	30.9.19	By Balance b/d	1,40,400	1,33,200
	To Shares in PKR Ltd A/c	2,07,990	2,00,790	30.9.19	By Profit & Loss Appropriation A/c	15,180	15,180
					By Realization A/c	60,000	60,000
		2,15,580	**2,08,380**			**2,15,580**	**2,08,380**

Working Notes:

(1) Ascertainment of purchase consideration

	Rs.	Rs.
Assets:		
Inventory		90,000
Trade receivables		72,000
Machinery less depreciation		1,71,000
Leasehold premises less written off		39,780
		3,72,780
Less: Liabilities:		
Trade payables	60,000	
Bank overdraft	24,000	-84,000
Closing Net Assets		2,88,780
Add: Goodwill		1,20,000
Purchase Consideration		4,08,780

(2) Ascertainment of profit for the 6 month ended 30th September,2019

	Rs.	Rs.
Closing Net Assets		2,88,780
Less: Opening Combined Capital		
Mohan – (1,68,000- 15,600-12,000)	1,40,400	
Sohan – (1,56,000-15,600-7,200)	1,33,200	
Profit after adjustment of Drawings		(2,73,600)
Add: Combined drawings during the 6 month (equal to profit)		15,180
		15,180

Profit for 6 months		30,360

Question 6 : Jan – 2021 – Paper

Ananya Enterprises is a partnership firm is which A, B and C are three partners sharing profits and losses in the ratio of 5 : 3 : 2. The Balance Sheet of the firm as on 31st October, 2019 is as below :

Liabilities	Rs.	Assets	Rs.
Capital :			
A	95,00,000	Land & Buildings	45,00,000
B	75,00,000	Plan & Machinery	65,00,000
C	30,00,000	Furniture & Fixtures	18,00,000
Sundry Creditors	11,00,000	Stock	13,50,000
		Sundry Debtors	7,50,000
		Cash	7,00,000
		Loan A	25,00,000
		Loan B	30,00,000
	2,11,00,000		**2,11,00,000**

On the Balance Sheet date all the three partners have decided to dissolve their partnership and called you to assist them in winding up the affairs of the firm. They also agreed that asset realisation s distributed among them at the end of each month.

A summary of liquidation transaction is as follows :

November, 2019

- Rs.3,00,000 – collected from debtors, balance is uncollectable
- Rs.11,00,000 – received from the sale of entire furniture
- Rs.2,00,000 – liquidation expenses paid
- Rs.6,00,000 – Cash retained in the business at the end of month

December, 2019

- Rs.2,00,000 – Liquidation expenses paid
- As part payment of his capital, C accepted a machinery for Rs.9,00,000 (Book value Rs.6,00,000)
- Rs.2,00,000 – Cash retained in the business at the end of month.

January, 2020

Rs.28,00,000 – Received on the sale of remaining plant and machinery.
Rs.9,00,000 – Received from the sale of entire stock
Rs.1,50,000 – Liquidation expenses paid
Rs.63,00,00 – Received on sale of Land and Buildings
No cash is retained in the business

You are required to prepare a schedule of cash payments amongst the partners by "Highest Relative Capital Method" as on 31st January, 2020.

Solution :

Statement showing distribution of cash

Particulars	Creditors		Capitals		
	Rs.	Rs.	Rs.	Rs.	Rs.
Balance Due after loan		11,00,000	70,00,000	45,00,000	30,00,000
Nov. 2019					
Balance available	7,00,000				
Realization less expenses and cash retained	6,00,000				
Amount available and paid	13,00,000	11,00,000	-	1,20,000	80,000
Balance due		-	70,00,000	43,80,000	29,20,000
Dec. 2019					
Opening balance	6,00,000				
Expenses paid and balance carried forward	4,20,000				
Available for distribution	1,80,000				
Cash paid to B and Machinery given to C			-	1,80,000	9,00,000
Balance due Jan.2020			70,00,000	42,00,000	20,20,000
Opening balance	2,00,000				
Amount realized less expenses	98,50,000				
Amount available and paid to partners	100,50,000				
First, Rs.31,20,000 is paid to A and B in the ratio of 5:3			19,50,000	11,70,000	
Balance (100,50,000 – 31,20,000) Rs. 69,30,000 is paid to A,B and C in the ratio of 5:3:2			34,65,000	20,79,000	13,86,000
Total amount paid			54,15,000	32,49,000	13,86,000
Total loss			15,85,000	9,51,000	6,34,000

Working note:

Calculation of Highest Relative Capital Basis

(1) Scheme of payment for November

Particulars	A Rs.	B Rs.	C Rs.
Balance of Capital Accounts	95,00,000	75,00,000	30,00,000
Less: Loans	(25,00,000)	(30,00,000)	—
	70,00,000	45,00,000	30,00,000
Profit-sharing ratio	5	3	2
Capital Profit sharing ratio	14,00,000	15,00,000	15,00,000
Capital in profit sharing ratio, taking A's capital as base	70,00,000	42,00,000	28,00,000
Excess of C's Capital and B's Capital (A-B)		3,00,000	2,00,000

Profit-sharing ratio		3	2

It means realization up to Rs. 5,00,000 is distributed among B and C in the ratio of 3:2. So excess amount of Rs. 2,00,000 after paying creditors is distributed among B and C in the ratio of 3:2 i.e. Rs.1,20,000 and 80,000 respectively.

(2) Scheme of payment for December

In the month of December C has received machinery amounting Rs. 9,00,000 against his excess capital of Rs. 1,20,000 (2,00,000 – 80,000). Excess capital of B is Rs.3,00,000 out of which Rs.1,20,000 already paid to him, so balance Rs. 1,80,000 available in the month of December will be paid to B.

(3) Scheme of payment for January

Particulars	**A Rs.**	**B Rs.**	**C Rs.**
Balance of Capital Accounts at the end of December	70,00,000	42,00,000	20,20,000
Profit-sharing ratio	5	3	2
Capital Profit sharing ratio	14,00,000	14,00,000	10,10,000
Capital in profit sharing ratio, taking C's capital as base	50,50,000	30,30,000	20,20,000
Excess Capital	19,50,000	11,70,000	

Since Rs. 19,50,000 and 11,70,000 is already in the ratio of 5:3, so amount realized up to Rs. 31,20,000 is distributed among A and B in the ratio of 5:3.

After that any amount realized is distributed among all the three partners in the ratio of 5:3:2.

Question 7 : May – 2021 – RTP

X, Y and Z are in partnership sharing profits and losses in the ratio of 5:4:4. The Balance Sheet of the firm as on 31st March, 2020 is as below:

Liabilities	**Rs.**	**Assets**	**Rs.**
X's Capital	60,000	Factory Building	96,640
Y's Capital	40,000	Plant and Machinery	65,100
Z's Capital	50,000	Trade Receivable	21,600
Y's Loan	18,000	Inventories	49,560
Creditors	66,000	Cash at Bank	1,100
	2,34,000		**2,34,000**

On Balance Sheet date, all the three partners have decided to dissolve their partnership. Since the realisation of assets was protracted, they decided to distribute amounts as and when feasible and for this purpose they appoint Z who was to get as his remuneration 1% of the value of the assets realised other than cash at bank and 10% of the amount distributed to the partners.

Assets were realised piecemeal as under:

	Rs.
First instalment	74,600
Second instalment	69,301
Third instalment	40,000
Last instalment	28,000

Dissolution expenses were provided for estimated amount of	Rs.12,000
The creditors were settled finally for	Rs.63,600

You are required to prepare a statement showing distribution of cash amongst the partners by "Highest Relative Capital Method".

Solution :

Statement showing distribution of cash amongst the partners

		Creditors	Y's Loan	Capitals		
				X (Rs.)	Y (Rs.)	Z (Rs.)
Balance Due		66,000	18,000	60,000	40,000	50,000
Including 1st Instalment amount with the firm Rs. (1100 + 74,600)	75,700					
Less: Dissolution expenses provided for	(12,000)					
	63,700					
Less: Z's remuneration of 1% on assets realized (74,600 x 1%)	(746)					
	62,954					
Less: Payment made to creditors	(62,954)	(62,954)				
Balance due	Nil	3046				
2nd instalment realised	69,301					
Less: Z's remuneration of 1% on assets realized (69,301 x 1%)	(693)					
	68,608					
Less: Payment made to creditors	(646)	(646)				
Transferred to P& L A/c		2,400				
	67,962					
Less: Payment for Y's loan A/c	(18,000)		(18,000)			
Amount available for distribution to partners	49,962		Nil			

Less: Z's remuneration of 10% of the amount distributed to partners (49,962 x 10/110)	(4,542)					
Balance to be distributed to partners on the basis of HRCM	45,420					
Less: Paid to Z (W.N.)	(2,000)					(2,000)
	43,420					48,000
Less: Paid to X and Z in 5:4 (W.N.)	(18,000)			(10,000)	-	(8,000)
Balance due	25,420			50,000	40,000	40,000
Less: Paid to X, Y & Z in 5:4:4	25,420		-	(9,778)	(7,821)	(7,821)
	Nil					
Amount of 3rd instalment	40,000			40,222	32,179	32,179
Less: Z's remuneration of 1% on assets realized (40,000 x 1%)	(400)					
	39,600					
Less: Z's remuneration of 10% of the amount distributed to partners (39,600 x 10/110)	(3,600)					
	36,000					
Less: Paid to X, Y, Z in 5:4:4 for (W.N.)	(36,000)			(13,846)	(11,077)	(11,077)
	Nil			26,376	21,102	21,102
Amount of 4th and last instalment	28,000					
Less: Z's remuneration of 1% on assets realized (28,000 x 1%)	(280)					
	27,720					
Less: Z's remuneration of 10% of the amount distributed to partners (27,720 x 10/110)	(2,520)					
	25,200					
Less: Paid to X, Y and Z in 5:4:4	(25,200)			(9,692)	(7,754)	(7,754)
	Nil					
Loss suffered by partners				16,684	13,348	13,348
						13,348

Working Note:

(i) Rs. 1100 added to the first instalment received on sale of assets represents the Cash in Bank

(ii) The amount due to Creditors at the end of the utilization of First Instalment is Rs. 3046. However, since the creditors were settled for Rs. 63,600 only the balance Rs.646 were paid and the balance Rs. 2400 was transferred to the Profit & Loss Account.

(iii) **Highest Relative Capital Basis**

	X **Rs.**	**Y** **Rs.**	**Z** **Rs.**
Balance of Capital Accounts (A)	60,000	40,000	50,000
Profit sharing ratio	5	4	4
Capital Profit sharing ratio	12,000	10,000	12,500
Capital in profit sharing ratio taking Y's Capital as base (B)	50,000	40,000	40,000
Excess of X's Capital and Z's Capital (A-B) = (C)	10,000	nil	10,000
Again repeating the process			
Profit sharing ratio	5		4
Capital Profit sharing ratio	2,000		2,500
Capital in profit sharing ratio taking X's Capital as base (D)	10,000		8,000
Excess of Z's Capital (C-D) = (E)	nil		2,000

Therefore, firstly Rs.2,000 is to be paid to Z, then X and Z to be paid in proportion of 5:4 upto Rs. 18,000 to bring the capital of all partners X, Y and Z in proportion to their profit sharing ratio. Thereafter, balance available will be paid in the profit sharing ratio 5:4:4 to all partners viz X, Y and Z.

Question 8 : May – 2021 – RTP

Write short note on Designated Partners in a Limited Liability Partnership and what are their liabilities.

Solution :

"Designated partner" means any partner designated as such pursuant to section 7 of the Limited Liability Partnerships (LLPs) Act, 2008. As per section 7 of the LLP Act, every limited Liability Partnership shall have at least 2 designated Partners who are individuals and at least one of them shall be a resident in India.

Provided that in case of Limited Liability Partnership in which all the partners are bodies corporate or in which one or more partners are Individuals and bodies corporate, at least 2 individuals who are partners of such limited liability Partnership or Nominees of such Bodies corporate shall act as designated partners.

"Liabilities of designated partners"

As per Section 8 of LLP Act, unless expressly provided otherwise in this Act, a designated partner shall be-

(a) responsible for the doing of all acts, matters and things as are required to be done by the limited liability partnership in respect of compliance of the provisions of this Act including filing of any document, return, statement and the like report pursuant to the provisions of this Act and as may be specified in the limited liability partnership agreement; and;

(b) liable to all penalties imposed on the limited liability partnership for any contravention of those provisions.

Question 9 : Nov – 2021 – RTP

P and Q were partners sharing profits equally of P & Q Co. Their Balance Sheet as on March 31, 2021 was as follows:

Balance Sheet as on 31st March, 2021

Equity and Liabilities		Rs.	Assets	Rs.
Capitals:			Bank	30,000
P	1,00,000		Debtors	25,000
Q	50,000	1,50,000	Stock	35,000
Creditors		20,000	Furniture	40,000
Q's current account		10,000	Machinery	60,000
Reserves		15,000	P's current account	10,000
Bank overdraft		5,000		
		2,00,000		**2,00,000**

The firm was dissolved on the above date:

P took over 50% of the stock at 10% less on its book value, and the remaining stock was sold at a gain of 15%. Furniture and Machinery realized for Rs. 30,000 and Rs. 50,000 respectively; There was an unrecorded investment which was sold for Rs. 25,000; Debtors realized 90% only and Rs. 1,245 were recovered for bad debts written off last year; There was an outstanding bill for repairs which had to be paid for Rs. 2,000.

You are required to prepare Realization Account, Partners' capital accounts (including transfer of current account balances) and Bank Account in the books of the firm.

Solution :

Particulars		Rs.	Particulars		Rs.
To Debtors	25,000		By Creditors		20,000
To Stock	35,000		By Bank overdraft		5,000
To Furniture	40,000		Bank:		
To Machinery	60,000	1,60,000	Investment	25,000	
To Bank :			Furniture	30,000	
Creditors	20,000		Machinery	50,000	
Bank overdraft	5,000		Debtors (90%)	22,500	
Outstanding bill	2,000	27,000	Stock	20,125	
Profit transferred to:			Bad debts Recovered	1,245	1,48,870
P's capital	1,310		P's capital		15,750
Q's capital	1,310	2,620	(stock taken over)		

	1,89,620		**1,89,620**

Partners' Capital Accounts

Particulars	P	Q	Particulars	P	Q
To P's current Account	16,940		By Balance b/d	1,00,000	50,000
To Bank	83,060	68,810	By Q's current Account		18,810
	1,00,000	**68,810**		**1,00,000**	**68,810**

Bank Account

	Rs.		Rs.
To Balance b/d	30,000	By Realization	27,000
to Realization	1,48,870	By P's capital	83,060
		By Q's capital	68,810
	1,78,870		**1,78,870**

Working Note:

Partners' Current Accounts

	P	Q		P	Q
To Balance b/d	10,000		By Balance b/d		10,000
To Realization	15,750		By Reserves	7,500	7,500
To Q's capital		18,810	By Realization (profit)	1,310	1,310
			By P's Capital	16,940	
	25,750	**18,810**		**25,750**	**18,810**

Question 10 : Nov – 2021 – RTP

Differentiate on ordinary partnership firm with an LLP (Limited Liability Partnership) in respect of the following:

(1) Applicable Law
(2) Perpetual Succession
(3) Ownership of Assets
(4) Liability of Partners/Members
(5) Principal-Agent Relationship.

Solution :

Key Elements	Partnerships	LLPs
Applicable Law	Indian Partnership Act 1932	The Limited Liability Partnerships Act, 2008
Perpetual Succession	Partnerships do not have perpetual succession	It has perpetual succession and individual partners may come and go

Ownership of Assets	Firm cannot own any assets. The partners own the assets of the firm	The LLP as an independent entity can own assets
Liability of Partners/ Members	Unlimited: Partners are severally and jointly liable for actions of other partners and the firm and their liability extends to personal assets	Limited to the extent of their contribution towards LLP except in case of intentional fraud or wrongful act of omission or commission by a partner.
Principal-Agent Relationship	Partners are the agents of the firm and of each other	Partners are agents of the firm only and not of other partners

Question 11 : Dec – 2021 – Paper

State the circumstances when Garner v/s Murray rule is not applicable.

Solution :

Non-Applicability of Garner vs Murray rule:

1. When the solvent partner has a debit balance in the capital account.
   Only solvent partners will bear the loss of capital deficiency of insolvent partner in their capital ratio. If incidentally, a solvent partner has a debit balance in his capital account, he will escape the liability to bear the loss due to insolvency of another partner.
2. When the firm has only two partners.
3. When there is an agreement between the partners to share the deficiency in capital account of the insolvent partner.
4. When all the partners of the firm are insolvent.

Question 12 : May – 2022 – RTP

The firm of M/s Om has four partners - A,B,C & D and as of 31st March, 2021, its Balance Sheet stood as follows :

Equity and Liabilities	**Rs.**	**Assets**	**Rs.**
Capital A/cs:		Land	50,000
A	2,00,000	Building	2,50,000
B	2,00,000	Office equipment	1,25,000
C	1,00,000	Computers	70,000
Current A/cs:		Debtors	4,00,000
A	50,000	Stocks	3,00,000
B	1,50,000	Cash at Bank	75,000
C	1,10,000	Other Current Assets	22,600
Loan from NBFC	5,00,000	Current A/c:	
Current Liabilities	70,000	D	87,400
	13,80,000		**13,80,000**

The partners have been sharing profits and losses in the ratio of 4:4:1:1. It has been agreed to dissolve the firm on 1.4.2021 on the basis of the following understanding:

(a) The following assets are to be adjusted to the extent indicated with respect to the book values:

Land	200%
Building	120%
Computers	70%
Debtors	95%
Stocks	90%

(b) In the case of the loan, the lenders are to be paid at their insistence a prepayment premium of 1%.

(c) D is insolvent and no amount is recoverable from him. His father, C, however, agrees to bear 50% of his deficiency. The balance of the deficiency is agreed to be apportioned according to law.

(d) The assets are realized at the agreed (adjusted) values.

Assuming that the realization of the assets and discharge of liabilities is carried out immediately, show the Cash A/c, Realization Account and the Partners' capital accounts (including their current accounts).

Solution :

In the books of M/s Om

Cash Account (Bank Column)

	Rs.			Rs.
To Balance b/d	75,000	By Realisation A/c-		
To Realization A/c (Realization of Sundry assets)	12,46,600	(Payment of sundry liabilities)		5,75,000
		By Partners' Capital A/cs:		
		A	2,42,600	
		B	3,42,600	
		C	1,61,400	7,46,600
	13,21,600			**13,21,600**

Realization Account

		Rs.			Rs.
To Land		50,000	By Current Liabilities		70,000
To Building		2,50,000	By Loan from NBFC		5,00,000
To Office equipment		1,25,000	By Cash A/c:		
To Computers		70,000	Land	1,00,000	
To Debtors		4,00,000	Building	3,00,000	
To Stocks		3,00,000	Office Equip.	1,25,000	
To Other Current Assets		22,600	Computers	49,000	

To Cash A/c:			Debtors	3,80,000	
Current liabilities	70,000		Stocks	2,70,000	
Loan from NBFC	5,05,000	5,75,000	Other Current Assets	22,600	12,46,600
To Partners' Current A/cs:					
Profit on realisation:					
A	9,600				
B	9,600				
C	2,400				
D	2,400	24,000			
		18,16,600			**18,16,600**

Partners' Capital Accounts

	A Rs.	B Rs.	C Rs.	D Rs.		A Rs.	B Rs.	C Rs.	D Rs.
To Partners' Current A/cs Transfer	–	–	–	85,000	By Balance b/d	2,00,000	2,00,000	1,00,000	–
To D A/c 50% of deficiency	–	–	42,500	–	By Partners' Current A/cs transfer	59,600	1,59,600	1,12,400	–
To D A/c - balance of deficiency borne in capital ratio of other partners (2:2:1)	17,000	17,000	8,500	–	By C A/c	–	–	–	42,500
To Cash A/c - final Settlement	2,42,600	3,42,600	1,61,400	–	– 50% of deficiency				
					By A A/c	–	–	–	17,000
					By B A/c	–	–	–	17,000
					By C A/c	–	–	–	8,500
	2,59,600	**3,59,600**	**2,12,400**	**85,000**		**2,59,600**	**3,59,600**	**2,12,400**	**85,000**

Partners' Current Accounts

	A Rs.	B Rs.	C Rs.	D Rs.		A Rs.	B Rs.	C Rs.	D Rs.
To Balance b/d	–	–	–	87,400	By Balance b/d	50,000	1,50,000	1,10,000	–
To Partners' Capital A/cs (transfer)	59,600	1,59,600	1,12,400	–	By Realisation A/	9,600	9,600	2,400	2,400
					By Partners' Capital A/cs (transfer)	–	–	–	85,000
	59,600	**1,59,600**	**1,12,400**	**87,400**		**59,600**	**1,59,600**	**1,12,400**	**87,400**

Question 13 : May – 2022 – RTP

Explain the nature of a Limited Liability Partnership. Under what circumstances, an LLP may be wound up voluntarily or by the Tribunal?

Solution :

A limited liability partnership is a body corporate formed and incorporated under the LLP Act, 2008 and is a legal entity separate from that of its partners. A limited liability partnership shall have perpetual succession and any change in the partners of a limited liability partnership shall not affect the existence, rights, or liabilities of the limited liability partnership.

Under the LLP Act, 2008 an LLP may be wound up voluntarily or by the Tribunal and such LLP so wound up may be dissolved. LLP may be wound up by the Tribunal in the following circumstances:

- If the LLP decides that it should be wound up by the Tribunal;
- If for a period of more than six months, the number of partners of the LLP is reduced below two;
- If the LLP is unable to pay its debts;
- If the LLP has acted against the interests of the integrity and sovereignty of India, the security of the state or public order;
- If the LLP has defaulted in the filing of the Statement of Account and Solvency with the Registrar for five consecutive financial years;
- If the Tribunal is of the opinion that it is just and equitable that the LLP be wound up

Question 14 : May – 2022 – Paper

Ajay, Vijay and Sanjay have been in partnership for a number of years, sharing profits and losses in the ratio 7 : 7 : 4 as a wholesale stationers running business under the name "AVS Traders". On 31st March, 2021, it was found that some frauds were committed by Sanjay during the year 2020-2021. So, it was decided to dissolve the partnership business on 31st March, 2021 when their Balance sheet stood as under :

Balance Sheet as at 31st March, 2021

Liabilities		Amount (Rs.)	Assets	Amount (Rs.)
Capital accounts:			Building	1,90,000
Ajay	1,80,000		Inventory	1,30,000
Vijay	1,80,000	3,60,000	Investments	50,000
General Reserve		36,000	Trade Debtors	70,000
Trade Creditors		80,000	Cash & Bank	26,000
Bills payables		30,000	Sanjay's Capital (overdrawn)	40,000
		5,06,000		**5,06,000**

Additional Information:

(i) Following frauds were committed by Sanjay :

(1) Investments costing Rs.8,000 were sold by Sanjay at Rs.11,000 and the funds were transferred to his personal account. This sale was omitted from firm's books.

(2) A cheque for Rs.7,000 received from trade debtors was not recorded in the books and was misappropriated by Sanjay.

(ii) A trade creditor agreed to take over investments of the book value of Rs.9,000 at Rs.13,000. The rest of the trade creditors were paid off at a discount of 10%.

(iii) Other assets were realised as follows :

Inventory	Rs.1,20,000
Building	110% of book value
Investments	The rest of the investments were sold at a profit of Rs.7,000
Trade Debtors	The rest of the trade debtors were realised at a discount of 10%

(iv) The Bills payables were settled at a discount of Rs.500.
(v) The expenses of dissolution amounted to ? 8,060.
(vi) It was found out, that realisation from Sanjay's private assets would be Rs.7,000.

You are required to prepare :
(1) Realisation Account
(2) Cash & Bank Account
(3) Partner's Capital Account
(All workings should form part of your answer)

Solution :

Realization Account

Particulars		Rs.	Particulars		Rs.
To Building		1,90,000	By Trade creditors		80,000
To Inventory		1,30,000	By Bills payable		30,000
To Investment		50,000	By Cash		
To Trade Debtors		70,000	Building	2,09,000	
To Cash - Trade creditors paid (W.N.1)		60,300	Inventory	1,20,000	
To Cash-expenses		8,060	Investments (W.N.2)	40,000	
To Cash-bills payable (30,000-500)		29,500	Trade Debtors (W.N. 3)	56,700	4,25,700
To Partners' Capital A/cs			By Sanjay's Capital A/c (Trade Debtors-unrecorded)		7,000
Ajay	6,160		By Sanjay's Capital A/c (Investments- unrecorded)		11,000
Vijay	6,160				
Sanjay	3,520	15,840			
		5,53,700			**5,53,700**

Cash and Bank Account

Particulars		Rs.	Particulars	Rs.
To Balance b/d		26,000	By Realization A/c- Trade creditors paid	60,300
To Realization A/c– assets realized			By Realization A/c-bills payable	29,500
Building	2,09,000		By Realization A/c- expenses	8,060
Inventory	1,20,000		By Capital accounts:	

Investments (W.N.2)	40,000		Ajay	1,80,420
Trade Debtors (W.N.3)	56,700	4,25,700	Vijay	1,80,420
To Sanjay's capital A/c		7,000		
		4,58,700		**4,58,700**

Partners' Capital Accounts

Particulars	Ajay Rs.	Vijay Rs.	Sanjay Rs.	Particulars	Ajay Rs.	Vijay Rs.	Sanjay Rs.
To Balance b/d			40,000	By Balance b/d	1,80,000	1,80,000	-
To Trade Debtors-misappropriation			7,000	By General reserve	14,000	14,000	8,000
To Investment-misappropriation			11,000	By Realization profit	6,160	6,160	3,520
To Sanjay's capital A/c (W.N. 4)	19,740	19,740		By Cash A/c			7,000
To Cash A/c	1,80,420	1,80,420		By Ajay's capital A/c			19,740
				By Vijay's capital A/c			19,740
	2,00,160	**2,00,160**	**58,000**		**2,00,160**	**2,00,160**	**58,000**

Working Notes:

1. Amount paid to Trade creditors

	Rs.
Book value	80,000
Less: Creditors taking over investments	(13,000)
	67,000
Less: Discount @ 10%	(6,700)
	60,300

2. Amount received from sale of investments

	Rs.
Book value	50,000
Less: Misappropriated by Sanjay	(8,000)
	42,000
Less: Taken over by a trade creditor	(9,000)
	33,000
Add: Profit on sale of investments	7,000
	40,000

3. Amount received from Trade debtors

	Rs.
Book value	70,000

Less: Unrecorded receipt	(7,000)
	63,000
Less: Discount @ 10%	(6,300)
	56,700

4. Deficiency of Sanjay

	Rs.
Balance of capital as on 31st March, 2021	40,000
Debtors-misappropriation	7,000
Investment-misappropriation	11,000
	58,000
Less: Realization Profit	(3,520)
General reserve	(8,000)
Contribution from private assets	(7,000)
Net deficiency of capital	39,480

This deficiency of Rs. 39,480 in Sanjay's capital account will be shared by other partners Ajay and Vijay in their capital ratio of 1:1

Accordingly,

Ajay's share of deficiency = [39,480/2] = Rs. 19,740

Vijay's share of deficiency = [39,480/2] = Rs. 19,740

Question 15 : Nov – 2022 – RTP

The partners P, Q & R have called you to assist them in winding up the affairs of their partnership on 31.12.2020. Their balance sheet as on that date is given below :

Equity & Liabilities	**Amount Rs.**	**Assets**	**Amount Rs.**
Capital Accounts:		Land & Building	50,000
P	65,000	Plant & Machinery	46,000
Q	50,500	Furniture & Fixture	10,000
R	32,000	Stock	14,500
Creditors	16,000	Debtors	14,000
		Cash at Bank	9,000
		Loan- P	13,000
		Loan- Q	7,000
Total	**1,63,500**	**Total**	**1,63,500**

(a) The partners share profit and losses in the ratio of 4:3:2.

(b) Cash is distributed to the partners at the end of each month.

(c) A summary of liquidation transactions are as follows:

January 2021

- Rs. 9,000 - collected from debtors; balance is uncollectable.
- Rs. 8,000 - received from the sale of entire furniture
- Rs. 1,000 - Liquidation expenses paid.

- Rs. 6,000 - Cash retained in the business at the end of month

February 2021
- Rs. 1,000 - Liquidation expenses paid.
- As part payment of his capital, R accepted a machinery for Rs. 9,000 (book value Rs. 3,500)
- Rs. 2,000 - Cash retained in the business at the end of month

March 2021
- Rs. 38,000 - received on the sale of remaining plant and machinery.
- Rs. 10,000 - received from the sale of entire stock.
- Rs. 1,700 - Liquidation expenses paid.
- Rs. 41,000 - Received on sale of land & building.
- No Cash is retained in the business.

You are required to prepare a schedule of cash payments amongst the partners by "Higher Relative Capital Method"

Solution :

Particulars	**Cash**	**Creditors**	**Capitals**		
	Rs.	**Rs.**	**P (Rs.)**	**Q (Rs.)**	**R (Rs.)**
Balance due after loan		16,000	52,000	43,500	32,000
January					
Balance available	9,000				
Realization less expenses and cash retained	10,000				
Amount available and paid	19,000	(16,000)	-	-	(3,000)
Balance due	-	-	52,000	43,500	29,000
February					
Opening Balance	6,000				
Expenses paid and cash carried forward	3,000				
Available for distribution	3,000				
Cash paid to Q and Machinery given to R			-	3,000	9,000
Balance due	-		52,000	40,500	20,000
March					
Opening Balance	2,000				
Amount realized less expenses	87,300				
Amount paid to partners	89,300		41,689	32,767	14,844
Loss			10,311	7,733	5,156

Working Note:

(i) Highest Relative Capital Basis

	P (Rs.)	Q (Rs.)	R (Rs.)
Scheme of payment for January 2021			
Balance of Capital Accounts	65,000	50,500	32,000
Less: Loans	(13,000)	(7,000)	-
(A)	52,000	43,500	32,000
Profit Sharing Ratio	4	3	2
Capital / Profit sharing Ratio	13,000	14,500	16,000
Capital in profit sharing ratio, taking P's capital as base (B)	52,000	39,000	26,000
Excess of R's capital and Q's Capital (A – B) (i)		4,500	6,000
Profit Sharing Ratio		3	2
Capital / Profit sharing Ratio		1,500	3,000
Capital in profit sharing ratio, taking Q's capital as base (ii)		4,500	3,000
Excess of R's Capital over Q's capital (i – ii)			3,000

(ii) Scheme of distribution of available cash for March:

	P (Rs.)	Q (Rs.)	R (Rs.)
Balance of Capital Accounts at end of February (A)	52,000	40,500	20,000
Profit Sharing Ratio	4	3	2
Capital / Profit sharing Ratio	13,000	13,500	10,000
Capital in profit sharing ratio, taking R's capital as base (B) (i)	40,000	30,000	20,000
Excess of P's Capital and Q's Capital (A – B) (i)	12,000	10,500	
Profit Sharing Ratio	4	3	
Capital / Profit sharing Ratio	3,000	3,500	
Capital in profit sharing ratio taking P's capital as base (ii)	12,000	9,000	
Excess of Q's Capital over P's Capital (i – ii)	-	1,500	
Payment Rs. 1500 (C)		(1,500)	
Balance of Excess Capital (i –C)	12,000	9,000	
Payment Rs. 21000 (D)	(12,000)	(9,000)	
Balance due (A – C – D)	40,000	30,000	20,000
Balance cash Payment (Rs. 89,300 – Rs. 22,500) = Rs. 66,800 (E)	(29,689)	(22,267)	(14,844)
Total Payment (Rs. 89,000) (C + D +E) (iii)	41,689	32,767	14,844
Loss (A – iii)	10,311	7,733	5,156

Question 16 : Nov – 2022 – Paper

M, N and O were in partnership sharing profits and losses in the ratio of 3 : 2 : 1. There was no provision in the agreement for interest on capitals or drawings.

M died on 31st March, 2021 and on that date, the partners' balances were as under:

Capital Account: M – Rs.75,000 (Cr); N – Rs.50,000 (Cr); O – Rs.25,000 (Cr)

Current Account: M – Rs.50,000 (Cr); N – Rs.37,500 (Cr); O – Rs.12,500 (Dr)

By the partnership agreement, the sum due to M's estate was required to be paid within a period of 3 years, and minimum instalment of Rs.37,500 each were to be paid, the first such instalment falling due immediately after death and the subsequent instalments at half-yearly intervals. Interest @ 6% was to be credited half-yearly.

In ascertaining M's share, Goodwill (not recorded in the books) was to be valued at Rs.1,12,500 and the assets, excluding the Joint Assurance Policy (mentioned below) were valued at Rs.75,000 in excess of the book values.

No Goodwill account was raised and no alteration was made to the book values of fixed assets. The Joint Assurance Policy shown in the books at Rs.50,000 matured on 01.04.2021, realizing Rs.65,000; payment of Rs.37,500 each were made to M's Executors on 01.04.2021, 30.09.2021 and 31.03.2022. N and O continued trading on the same terms and conditions as previously and the net profit for the year ending 31.03.2022 (before charging the interest due to M's estate) amounted to Rs.65,000. During that period, the partners' drawings were N – Rs.18,750 and Rs.10,000.

On 01.04.2022, the partnership was dissolved and an offer to purchase the business as a going concern for Rs.2,25,000 was accepted on that day. A cheque for that sum was received on 30.06.2022.

The balance due to M's estate, including interest, was paid on 30.06.2022 and on that day, N and O received the sums due to them.

You are required to write-up the Partners' Capital Accounts and Partners' Current Accounts from 01.04.2021 to 30.06.2022. Show also the account of executors of M.

Thanks ....

Rahul Malkan

CHAPTER 14

CONVERSION OF PARTNERSHIP INTO A COMPANY

Question 1 : May – 2021 – RTP

Om, Sai and Radhe share profits and losses of a business as to 3:2:1 respectively. Their balance sheet as at 31st March, 2020 was as follows:

Liabilities	Rs.	Assets	Rs.
Capital Accounts:		Land and Building	1,40,000
Om	70,000	Machinery	50,000
Sai	80,000	Motor Car	28,000
Radhe	10,000	Furniture	12,000
General Reserve	22,000	Investments	18,000
Radhe's Loan	33,000	Stock	18,000
Mrs. Om's loan	15,000	Bills receivable	20,000
Creditors	96,000	Loose tools	7,000
Bills Payable	14,000	Debtors	38,000
Bank overdraft	60,000	Cash	1,000
		Radhe's current A/c	56,000
		Profit and Loss A/c	12,000
	4,00,000		**4,00,000**

The partners decide to convert their firm into a Joint Stock Company. For this purpose ABC Ltd. was formed with an authorized capital of Rs. 10,00,000 divided into Rs. 100 equity Shares. The business of the firm was sold to the company as at the date of balance sheet given above on the following terms:

(i) Motor car, furniture, investments, loose tools, debtors and cash are not to be taken over by the company.

(ii) Liabilities for bills payable and bank overdraft are to be taken over by the company.

(iii) The purchase price is settled at Rs. 1,95,500 payable as to Rs. 75,500 in cash and the balance in company's fully paid shares of Rs. 100 each.

(iv) The remaining assets and liabilities of the firm are directly disposed of by the firm as per details given below:
Investments are taken over by Om for Rs. 13,000; debtors realize in all Rs. 20,000; Motor Car, furniture and loose tools fetch Rs. 24,000, Rs. 4,000, and Rs. 1,000 respectively. Om agrees to pay his wife's loan. The creditors were paid Rs. 94,000 in final settlement of their claims. The realization expenses amount to Rs. 500. Radhe's loan was transferred to his capital account.

(v) The equity share received from the vendor company are to be divided among the partners in profit-sharing ratio.

You are required to prepare Realization account, Partners' capital accounts, Cash account, ABC Ltd. account and Shares in ABC Ltd. account in the books of the partnership firm.

Solution :

In the books of Partnership Firm

Realization Account

Particulars	Rs.	Rs.	Particulars	Rs.	Rs.
To Land and Building		1,40,000	By Trade creditors		96,000
To Machinery		50,000	By Bills Payable		14,000
To Motor Car		28,000	By Bank overdraft		60,000
To Furniture		12,000	By Mrs. Om's loan		15,000
To Investments		18,000	By ABC Ltd. (Purchase price)		1,95,500
To Loose tools		7,000			
To Stock		18,000	By Om's Capital A/c (Investments taken over)		13,000
To Bill receivable		20,000			
To Debtors		38,000	By Cash A/c:		
To Om's Capital A/c (Mrs. Om's Loan)		15,000	Debtors	20,000	
To Cash A/c:			Motor Car	24,000	
Creditors	94,000		Furniture	4,000	
Realization expenses	500	94,500	Loose tools	1,000	49,000
To Profit on Realization transferred to:					
Om's Capital A/c	1,000				
Sai's Capital A/c	667				
Radhe's Capital A/c	333	2,000			
		4,42,500			**4,42,500**

ABC Ltd. Account

Particulars	Rs.	Particulars	Rs.
To Realization A/c	1,95,500	By Cash A/c	75,500
		By Shares in ABC Ltd.	1,20,000
	1,95,500		**1,95,500**

Partners' Capital Accounts

Particulars	Om Rs.	Sai Rs.	Radhe Rs.	Particulars	Om Rs.	Sai Rs.	Radhe Rs.
To Profit and Loss A/c	6,000	4,000		By Balance b/d	70,000	80,000	10,000
To Realization A/c	13,000	-		By Radhe's Loan A/c	-	-	33,000

To Radhe's Current A/c	-	-		By General reserve	11,000	7,333	3,667
To shares in ABC Ltd.	60,000	40,000		By Realization A/c	1,000	667	333
To Cash A/c	18,000	44,000		By Realization A/c (Mrs. Om's loan A/c)	15,000	-	-
				By Cash A/c	-	-	31,000
	97,000	**88,000**	**78,000**		**97,000**	**88,000**	**78,000**

Shares in ABC Ltd. Account

Particulars	Rs.	Particulars	Rs.
To ABC Ltd. Account	1,20,000	By Om's Capital A/c	60,000
		By Sai's Capital A/c	40,000
		By Radhe's Capital A/c	20,000
	1,20,000		**1,20,000**

Cash Account

Particulars	Rs.	Particulars	Rs.
To Balance b/d	1,000	By Realization A/c (Liabilities and expenses)	94,500
To ABC Ltd.	75,500	By Om's Capital A/c	18,000
To Realization A/c (realization of assets)	49,000	By Sai's Capital A/c	44,000
To Radhe's Capital A/c	31,000		
	1,56,500		**1,56,500**

Question 2 : July – 2021 – Paper

A Partnership firm C and Co. consist of partners P and Q sharing Profits and Losses in the ratio 4 : 1. The firm H and Co. consists of Partners Q and R sharing Profits and Losses in the ratio 3 : 2. On 31st March, 2021, it was decided to amalgamate both the firms and form a new firm CH & Co., wherein P, Q, R would be partners sharing Profits and Losses in the ratio of 6 : 3 : 1.

The summarized Balance Sheets of both the firms as on 31st March, 2021 were as follows :

Liabilities	C & Co.	H & Co.	Assets	C & Co.	H & Co.
	(Rs. in 000)	(Rs. in 000)		(Rs. in 000)	(Rs. in 000)
Capital			Cash in hand/bank	160	120
P	600	–	Debtors	240	320
Q	400	300	Stock	200	80
R	–	200	Vehicles	–	350
Reserve	200	150	Machinery	480	–
Creditors	480	220	Building	600	–
Total	**1,680**	**870**	**Total**	**1,680**	**870**

The following were the terms of amalgamation :

(i) Goodwill of C and Co. was valued at Rs.2,80,000 and the Goodwill of H and Co. was valued at Rs.1,60,000. Goodwill account is not to be opened in the books of the new firm but to be adjusted through the Capital accounts of the partners.

(ii) Building, Machinery and Vehicles are to be taken over at Rs.8,00,000, Rs.4,00,000 and Rs.3,00,000 respectively.

(iii) Provision for doubtful debts at Rs.20,000 in respect of C and Co. and Rs.10,000 in respect of H and Co. are to be provided.

You are required to :

(i) Show how the Goodwill value will be adjusted amongst the partners.

(ii) Prepared the Balance Sheet of CH & Co. as at 31st March, 2021 by keeping Partner's capital in their profit sharing ratio taking capital of 'Q' as the basis. The excess or deficiency to be kept in the respective Partner's Current Accounts.

Solution :

(i) Adjustment for raising and writing off of goodwill

	Raised in old profit-sharing ratio		**Total**	**Written off in new ratio**	**Difference**
	C & Co.	**H & Co.**			
	4:01 **Rs.**	**3:02** **Rs.**	**Rs.**	**6:03:01** **Rs.**	**Rs.**
P	2,24,000	---	2,24,000 Cr.	2,64,000 Dr.	40,000 Dr.
Q	56,000	96,000	1,52,000 Cr.	1,32,000 Dr.	20,000 Cr.
R	---	64,000	64,000 Cr.	44,000 Dr.	20,000 Cr.
	2,80,000	1,60,000	4,40,000	4,40,000	Nil

(ii) Balance Sheet of CH & Co. (New firm) as on 31.3.2021

Liabilities	**Rs.**	**Assets**	**Rs.**
Capital Accounts:		Vehicle	3,00,000
P	16,68,000	Machinery	4,00,000
Q	8,34,000	Building	8,00,000
R	2,78,000	Stock	2,80,000
Creditors	7,00,000	Debtors	5,30,000
		Cash & Bank	2,80,000
		Current Accounts:	
		P	8,68,000
		R	22,000
	34,80,000		**34,80,000**

Working Notes:

1. Balance of Capital Accounts at the time of amalgamation of firms

C & Co.

Particulars	P's Capital (Rs.)	Q's Capital (Rs.)
C & Co. Profit and loss sharing ratio 4:1		
Balance as per Balance Sheet	6,00,000	4,00,000
Add: Reserves	1,60,000	40,000
Revaluation profit (Building)*	1,60,000	40,000
Less: Revaluation loss (Machinery)	(64,000)	(16,000)
Provision for doubtful debt	(16,000)	(4,000)
	8,40,000	4,60,000

H & Co.

Particulars	Q's Capital (Rs.)	R's Capital (Rs.)
H & Co. Profit and loss sharing ratio 3:2		
Balance as per Balance sheet	3,00,000	2,00,000
Add: Reserves	90,000	60,000
Less: Revaluation (vehicle)	(30,000)	(20,000)
Provision for doubtful debts	(6,000)	(4,000)
	3,54,000	2,36,000

2. Balance of Capital Accounts in the balance sheet of the new firm as on 31.3.2021

Particulars	P Rs.	Q Rs.	R Rs.
Balance b/d: C & Co.	8,40,000	4,60,000	--
H & Co.	--	3,54,000	2,36,000
	8,40,000	8,14,000	2,36,000
Adjustment for goodwill	(40,000)	20,000	20,000
	8,00,000	8,34,000	2,56,000
Total capital Rs. 27,80,000 (Q's capital i.e. Rs. 8,34,000 x 10/3) to be contributed in 6:3:1 ratio.	16,68,000	8,34,000	2,78,000
Deficiency Transferred to Current Account	8,68,000	---	22,000

Question 3 : Nov – 2021 – RTP

The following is the Balance Sheet of M/s. R and S as on 31st March, 2019:

Equity and Liabilities	Rs.	Assets	Rs.
Capital Accounts:		Machinery	54,000
R	50,000	Furniture	5,000
S	30,000	Investments (non-trading)	50,000

Reserves	20,000	Stock	20,000
Loan Account of S	15,000	Debtors	21,000
Creditors	40,000	Cash	5,000
	1,55,000		**1,55,000**

It was agreed that Mr. T is to be admitted for a fourth share in the future profits from 1st April, 2019. He is required to contribute cash towards goodwill and Rs. 15,000 towards capital.

The following further information is furnished:

(a) R & S share the profits in the ratio 3 : 2.

(b) R was receiving salary of Rs. 750 per month from the very inception of the firm in 2012 in addition to share of profit.

(c) The future profit ratio between R, S & T will be 2:1:1. R will not get any salary after the admission of T.

(d) It was agreed that the value of goodwill of the firm shall be determined on the basis of 3 years' purchase of the average profits from business of the last 5 years. Goodwill was not to be raised in the books. The particulars of the profits are as under:

Year ended	**Profit/(Loss)**
31st March, 2015	25,000
31st March, 2016	12,500
31st March, 2017	(2,500)
31st March, 2018	35,000
31st March, 2019	30,000

The above Profits and Losses are after charging the Salary of R. The Profit of the year ended 31st March, 2015 included an extraneous profit of Rs. 40,000 and the loss for the year ended 31st March, 2017 was on account of loss by strike to the extent of Rs. 20,000.

(e) The cash trading profit for the year ended 31st March, 2020 was Rs. 50,000 before depreciation.

(f) The partners had drawn each Rs. 1,000 per month as drawings.

(g) The value of other assets and liabilities as on 31st March, 2020 were as under:

	Rs.
Machinery (before depreciation)	60,000
Furniture (before depreciation)	10,000
Investment	50,000
Stock	15,000
Debtors	30,000
Creditors	20,000

(h) Provide depreciation @ 10% on Machinery and @ 5% on Furniture on the closing balance and interest is accumulated @ 6% on S's loan. The loan along with interest would be repaid within next 12 months.

(i) Investments (non -trading) are held from inception of the firm and interest is received @ 10% p.a.

(j) The partners applied for conversion of the firm into Karma Ltd., a Private Limited Company. Certificate was received on 1st April, 2020. They decided to convert Capital Accounts of

the partners into share capital in the ratio of 2:1:1 on the basis of a total capital as on 31st March, 2020. If necessary, partners have to subscribe to fresh capital or withdraw.

Prepare the Profit and Loss Account of the firm for the year ended 31st March, 2020 and the Balance Sheet of the Company as at 1st April, 2020.

Solution :

M/s R, S and T

Profit and Loss Account for the year ending on 31st March, 2020

	Rs.		Rs.
To Depreciation on Machinery	6,000	By Trading Profit	50,000
To Depreciation on furniture	500	By Interest on Investment	5,000
To Interest on S's loan	900		
To Net Profit to :			
R's Capital A/c	23,800		
S's Capital A/c	11,900		
T's Capital A/c	11,900		
	55,000		**55,000**

Balance Sheet of the Karma Pvt. Ltd. as at 1st April, 2020

		Notes No.	Rs.
I	**Equity and Liabilities**		
	Shareholders' funds		
	Share capital		1,41,600
	Current liabilities		
	Short term borrowings	1	15,900
	Trade payables		20,000
	Total		**1,77,500**
II	**Assets**		
	Non-current assets		
	Property, plant & Equipment (PPE)	2	63,500
	Non-current investments		50,000
	Current assets		
	Inventories		15,000
	Trade receivables		30,000
	Cash and cash equivalents		19,000
	Total		**1,77,500**

Notes to Accounts

			Rs.
1	**Short term borrowings**		
	Loan from S		15,900
2	**PPE**		

	Machinery	54,000	
	Furniture	9,500	63,500

Working Notes:

1. Calculation of goodwill

	2014-15 Rs.	2015-16 Rs.	2016-17 Rs.	2017-18 Rs.	2018-19 Rs.
Profits/(Loss)	25,000	12,500	-2,500	35,000	30,000
Adjustment for extraneous profit of 2014-15 and abnormal loss of 2016-17	(40,000)	-	20,000	-	-
	(15,900)	12,500	17,500	35,000	30,000
Add: Salary of R (750 x12)	9,000	9,000	9,000	9,000	9,000
	(6,000)	21,500	26,500	44,000	39,000
Less: Interest on non- trading investment	(5,000)	(5,000)	(5,000)	(5,000)	(5,000)
	(11,000)	16,500	21,500	39,000	34,000
Total Profit from 2015-16 to 2018-19					1,11,000
Less: Loss for 2014-15					(11,000)
					1,00,000
Average Profit					20,000
Goodwill equal to 3 years' purchase					60,000
Contribution from T for ¼ share					15,000

2. Calculation of sacrificing ratio of Partners R and S on admission of T

	Old share	New share	Sacrificing share	Gaining share
R	3/5	1/2	$\frac{3}{5}-\frac{1}{2}=\frac{6-5}{10}=\frac{1}{10}$	
S	2/5	1/4	$\frac{2}{5}-\frac{1}{4}=\frac{8-5}{20}=\frac{3}{20}$	
T		1/4		1/4

3. Goodwill adjustment entry through Partners' capital accounts (in their sacrificing ratio of 2:3)

		Rs.	Rs.
T' s capital A/c	Dr.	15,000	
To R's capital A/c			6,000
To S' s capital A/c			9,000
(T's share in goodwill adjusted through R and S)			

4. Partners' Capital Accounts

	R Rs.	S Rs.	T Rs.		R Rs.	S Rs.	T Rs.
To Drawings (1,000 x 12)	12,000	2,000	12,000	By Balance b/d	50,000	30,000	-
To R	-	-	6,000	By General Reserve	12,000	8,000	-
To S	-	-	9,000	By T	6,000	9,000	-
To Balance c/d	79,800	46,900	14,900	By Bank (15,000 + 15,000)	-	-	30,000
				By Profit & Loss A/c	23,800	11,900	11,900
	91,800	**58,900**	**41,900**		**91,800**	**58,900**	**41,900**

5. Balance Sheet of the firm as on 31st March, 2020

Equity and Liabilities	Rs.	Rs.	Assets	Rs.	Rs.
R's Capital	79,800		Machinery	60,000	
S's Capital	46,900		Less: Depreciation	(6,000)	54,000
T's Capital	14,900	1,41,600	Furniture	10,000	
			Less: Depreciation	(500)	9,500
S's Loan	15,000		Investments		50,000
Add: Interest due	900	15,900	Stock-in-trade		15,000
Creditors		20,000	Debtors		30,000
			Cash (W.N.6)		19,000
		1,77,500			**1,77,500**

6. Cash balance as on 31.3.2020

	Rs.	Rs.
Cash trading profit		50,000
Add: Investment Interest		5,000
Add: Decrease in Stock Balance		5,000
		60,000
Less: Increase in Debtors	9,000	
Less: Decrease in Creditors	20,000	(29,000)
		31,000
Add: Opening cash balance	5,000	
Add: Cash brought in by T	30,000	35,000
		66,000
Less: Drawings (12,000 +12,000 +12,000)	36,000	
Less: Additions to Machine (60,000 - 54,000)	6,000	
Furniture (10,000 - 5,000)	5,000	(47,000)
Closing cash balance		19,000

7. Distribution of shares – Conversion into Company

	Rs.
Capital : R	79,800

S		46,900
T		14,900
Share Capital		1,41,600
Distribution of shares :	R (1/2)	70,800
	S (1/4)	35,400
	T (1/4)	35,400

R and S should withdraw capital of Rs. 9,000 (Rs. 79,800 – Rs. 70,800) and Rs.11,500 (Rs. 46,900 – Rs. 35,400) respectively and T should subscribe shares of Rs. 20,500 (Rs.35,400 – Rs. 14,900).

Question 4 : Dec – 2021 – Paper

TJM & Sons is a partnership firm consisting of T, J and M who share profits and losses in the ratio of 2:2:1 and JEK Limited is another company doing similar business.

The firm (TJM & Sons) and the company (JEK Ltd.) provide you the following ledger balances as on 31.03.2021 :

	TJM & Sons (Rs.)	JEK Ltd. (Rs.)
Debit Balances :		
Plant & Machinery	7,50,000	24,00,000
Furniture & Fixtures	75,000	3,37,500
Inventories	3,00,000	12,75,000
Trade receivables	3,00,000	12,37,500
Cash at Bank	15,000	6,00,000
Cash in hand	60,000	1,50,000
Credit Balances		
Equity share capital : Equity shares of Rs.10 each		30,00,000
Partners Capitals		
T	3,00,000	
J	4,50,000	
M	1,50,000	
General Reserve	1,50,000	10,50,000
Trade Payables	4,50,000	19,50,000

On the balance sheet date, it was decided that the firm TJM & Sons be dissolved and all the assets (except cash in hand and cash at bank) and all the liabilities of the firm be taken over by JEK Limited by issuing 75,000 shares of Rs.10/- each at a premium of Rs.4/- per share. Plant & Machinery and Furniture & Fixtures are to be revalued at Rs.8,50,000 and Rs.1,00,000 respectively.

Partners of TJM & Sons agreed to divided the shares issued by JEK Limited in the profit sharing ratio and bring necessary cash for settlement of their capital.

The trade payable of TJM & Sons includes Rs.1,50,000 payable to JEK Limited. An unrecorded liability of Rs.37,500 of TJM & Sons must also be taken over by JEK Ltd.

You are required to prepare :

(i) Realisation account, Partners' capital accounts and cash in hand / Bank account in the books of TJM & Sons.

(ii) Pass journal entries in the books of JEK Limited for acquisition of TJM & Sons.

Solution :

(i) **In the books of TJM& Sons**

Realization Account

Particulars		Rs.	Particulars	Rs.
To Plant & Machinery		7,50,000	By Trade payable	4,50,000
To Furniture & Fixture		75,000	By JEK Ltd. (Refer W.N.)	10,50,000
To Inventories		3,00,000		
To Trade receivables		3,00,000		
To Partners' Capital Accounts (Profit):				
T's Capital A/c	30,000			
J's Capital A/c	30,000			
M's Capital A/c	15,000	75,000		
		15,00,000		**15,00,000**

Partners' Capital Accounts

Particulars	T Rs.	J Rs.	M Rs.	Particulars	T Rs.	J Rs.	M Rs.
To Shares in JEK Ltd.	4,20,000	4,20,000	2,10,000	By Balance b/d	3,00,000	4,50,000	1,50,000
To Cash	-	1,20,000	-	By General Reserve	60,000	60,000	30,000
				By Realization A/c	30,000	30,000	15,000
				By Cash	30,000	-	15,000
	4,20,000	**5,40,000**	**2,10,000**		**4,20,000**	**5,40,000**	**2,10,000**

Cash and Bank Account

Particulars	Cash Rs.	Bank Rs.	Particulars	Cash Rs.	Bank Rs.
To Balance b/d	60,000	15,000	By Cash A/c (Contra)		15,000
To Bank A/c (Contra)*	15,000		By J	1,20,000	
To T	30,000				
To M	15,000				
	1,20,000	**1,20,000**		**1,20,000**	**1,20,000**

(ii) Journal Entries in the Books of JEK Ltd.

			Dr. (Rs.)	Cr. (Rs.)
1	Business Purchase Account	Dr.	10,50,000	
	To Liquidators of TJM& Sons			10,50,000
	(Being business of TJM& Sons purchased and payment due)			
2	Plant and Machinery A/c	Dr.	8,50,000	
	Furniture and Fixture A/c	Dr.	1,00,000	
	Inventories A/c	Dr.	3,00,000	
	Trade Receivables A/c	Dr.	3,00,000	
	To Trade Payables			4,50,000
	To Unrecorded Liability			37,500
	To Business Purchase Account			10,50,000
	To Capital Reserve (B.F.)			12,500
	(Being take over of all assets and liabilities)			
3	Liquidators of TJM& Sons	Dr.	10,50,000	
	To Equity Share Capital Account			7,50,000
	To Securities Premium Account			3,00,000
	(Being purchase consideration discharged in the form of shares of Rs. 10 each issued at a premium of Rs. 4 each)			
4	Trade Payables Account	Dr.	1,50,000	
	To Trade Receivables Account			1,50,000
	(Being mutual owing eliminated)			

Working Note:

Computation of purchase consideration:

75,000 Equity shares of Rs.14 each = Rs. 10,50,000

Equity shares to be given to partners :

T = 30,000 Shares @ Rs. 14 = Rs. 4,20,000

J = 30,000 shares @ Rs. 14 = Rs. 4,20,000

M = 15,000 shares @ Rs. 14 = Rs. 2,10,000

Question 5 : May – 2022 – RTP

U and V were in partnership with sharing of profit and loss equally. The firm's Balance sheet as at 31/12/2021 (for 9 months) was :

Equity and Liabilities		Rs.	Assets	Rs.
Partners' Capital Accounts:			Plant	1,85,000
U	1,50,000		Building	1,00,000
V	1,80,000	3,30,000	Debtors	85,000
Sundry Creditors		90,000	Stock	56,000

Bank Overdraft	83,000	Profit & Loss A/c (Dr. balance)		60,000
		Partners' Drawings Accounts:		
		U	8,000	
		V	9,000	17,000
Total	**5,03,000**	**Total**		**5,03,000**

The operations of the business were carried on till 31/03/2022. U and V both withdrew in equal amount half the amount of profit made during the current period of three months after charging depreciation of Rs. 5,000 on plant and after writing off 5% of building. During the current period of three months, creditors were reduced by Rs. 50,000 and bank overdraft by Rs. 50,000. The stock was valued at Rs. 24,000 and debtors at Rs. 40,500 on 31st March, 2022. The other items remained the same as at 31/12/2021.

On 31/03/2022, the firm sold its business to UV Limited. The value of goodwill was estimated at Rs. 1,84,000 and the remaining assets were valued on the basis of the balance sheet as on 31/03/2022 except building and stock, which were valued as below:

Building Rs. 1,20,000

Stock Rs. 36,000

UV Limited paid the purchase consideration in equity shares of Rs. 10 each. You are required to prepare (with necessary working notes):

(i) Balance sheet of the firm as at 31/03/2022.

(ii) Realization account and

(iii) Partners' capital accounts showing the final settlement between them.

Solution :

(i) **Balance Sheet of the Firm as at 31.3.2022**

Liabilities	**Rs.**	**Assets**	**Rs.**	**Rs.**
Capital Accounts:		Plant	1,85,000	
U's capital	1,18,750	Less: Depreciation	(5,000)	1,80,000
V's capital	1,47,750	Building	1,00,000	
Sundry Creditors (90,000 – 50,000)	40,000	Less: Written off	(5,000)	95,000
		Stock		24,000
Bank overdraft (83,000 – 50,000)	33,000	Sundry Debtors		40,500
	3,39,500			**3,39,500**

(ii) **Realization Account**

Particulars	**Rs.**	**Particulars**	**Rs.**
To Plant A/c	1,80,000	By Sundry Creditors A/c	40,000
To Building A/c	95,000	By Bank Overdraft A/c	33,000
To Stock A/c	24,000	By UV Ltd. A/c (W.N.2)	4,87,500

To Sundry Debtors A/c	40,500		
To U's Capital A/c	1,10,500		
To V's Capital A/c	1,10,500		
	5,60,500		**5,60,500**

(iii) **Partners' Capital Accounts**

Date	Particulars	U Rs.	V Rs.	Date	Particulars	U Rs.	V Rs.
1.1.22	To Profit & Loss A/c	30,000	30,000	1.1.22	By Balance b/d	1,50,000	1,80,000
	To Drawings A/c	8,000	9,000	31.3.22	By Profit (W.N.1)	13,500	13,500
31.3.22	To Drawings (W.N.1)	6,750	6,750				
	To Balance c/d	1,18,750	1,47,750				
		1,63,500	**1,93,500**			**1,63,500**	**1,93,500**
30.3.22	To Shares in UV Ltd. A/c	2,29,250	2,58,250	31.3.22	By Balance b/d	1,18,750	1,47,750
				31.3.22	By Realization A/c	1,10,500	1,10,500
		2,29,250	**2,58,250**			**2,29,250**	**2,58,250**

Working Notes:

(1) Ascertainment of profit for the 3 months ended 31st March,2022

	Rs.	Rs.
Assets:		
Stock		24,000
Sundry Debtors		40,500
Plant less depreciation		1,80,000
Building		95,000
		3,39,500
Less: Liabilities:		
Sundry Creditors	40,000	
Bank overdraft	33,000	(73,000)
Closing net assets		2,66,500
Less: Opening adjusted capitals		
U (1,50,000 – 30,000 – 8,000)	1,12,000	
V (1,80,000 – 30,000 – 9,000)	1,41,000	2,53,000
Profit net of drawings		13,500
Add: Combined drawings during the 3 months (equal to half of profit) = 13,500 X 2		27,000
Combined drawings for 3 months		13,500

(2) Ascertainment of purchase consideration

	Rs.	Rs.
Assets:		
Stock		36,000
Sundry Debtors		40,500
Plant less depreciation		1,80,000
Building		1,20,000
		3,76,500
Less: Liabilities:		
Sundry Creditors	40,000	
Bank overdraft	33,000	(73,000)
Net Assets value taken by UV Ltd.		3,03,500
Add: Goodwill		1,84,000
Purchase Consideration paid by equity shares in UV Ltd. at Rs. 10 each		4,87,500

Question 6 : Nov – 2022 – RTP

A and V, sharing profits and losses equally, desired to convert their business into a limited company on 31st December, 2021 when their balance sheet stood as follows:

Equity & Liabilities	Rs.	Rs.	Assets	Rs.
Sundry creditors		1,92,000	Sundry debtors	2,40,000
Loan creditors		1,60,000	Bills receivable	40,000
Bank overdraft		64,000	Stock in trade	1,44,000
Reserve fund		24,000	Patents	32,000
Capital accounts:			Plant and machinery	64,000
A	1,60,000		Land and building	2,40,000
V	1,60,000	3,20,000		
		7,60,000		**7,60,000**

(a) The goodwill of the firm was to be valued at two years' purchase of the profits average of the previous three years.

(b) The loan creditor agreed to accept 7½% redeemable preference shares in settlement of his claim.

(c) Land and buildings and plant and machinery were to be valued at Rs. 4,00,000 and Rs. 96,000 respectively.

(d) The vendors were to be allotted equity shares.

(e) The past working results of the firm showed that they had made profits of Rs. 1,20,000 in 2019, Rs. 1,44,000 in 2020 and Rs. 1,68,000 in 2021 after setting aside Rs. 8,000 to reserve fund each year.

You are required to show realisation account and partners' capital accounts in the books of the firm assuming that all the transactions are duly completed.

Solution :

Books of A and V

Realisation Account

	Rs.	Rs.		Rs.
To Sundry debtors		2,40,000	By Sundry creditors	1,92,000
To Bills receivable		40,000	By Loan creditors	1,60,000
To Stock in trade		1,44,000	By Bank overdraft	64,000
To Patents		32,000	By Purchasing Company	8,40,000
To Plant and Machinery		64,000	(W.N. 2)	
To Land and Building		2,40,000		
To Capital A/c (Profit)				
A	2,48,000			
V	2,48,000	4,96,000		
		12,56,000		**12,56,000**

Partners' Capital Accounts

	A Rs.	V Rs.		A Rs.	V Rs.
To Shares in Purchasing Company	4,20,000	4,20,000	By Balance b/d	1,60,000	1,60,000
			By Reserves	12,000	12,000
			By Realization A/c	2,48,000	2,48,000
	4,20,000	**4,20,000**		**4,20,000**	**4,20,000**

Working Notes:

1. Goodwill = (1,20,000 + 1,44,000 + 1,68,000 + 24,000*)/3 x 2 Years = 3,04,000

   *Profit transferred to reserve @ Rs. 8,000 for 3 years.

2. Calculation of Purchase Consideration

	Rs.	Rs.
Assets taken over:		
Goodwill (W.N.1)		3,04,000
Land and Buildings		4,00,000

Plant and Machinery		96,000
Debtors		2,40,000
Bills Receivable		40,000
Stocks		1,44,000
Patents		32,000
		12,56,000
Less: Liabilities taken over:		
Creditors	1,92,000	
Loan Creditors	1,60,000	
Bank Overdraft	64,000	4,16,000
Purchase Consideration		8,40,000

Thanks ....

CHAPTER 15

EMPLOYEE STOCK OPTION PLANTS

Question 1 : May – 2018 – Paper

Suvidhi Ltd. offered 50 shares to each of its 1500 employees on 1st April 2017 for Rs. 30. Option would be exercisable within a year it is vested. The shares issued under the plan shall be subject to lock-in on transfer for three years from the grant date. The market price of shares of the company is Rs. 50 per share on grant date. Due to post vesting restrictions on transfer, the fair value of shares issued under the plan is estimated at Rs. 38 per share.

On 31st March, 2018,1200 employees accepted the offer and paid Rs. 30 per share purchased. Nominal value of each share is Rs. 10.

Record the issue of shares in the books of the company under the aforesaid plan.

Solution :

Journal Entries in the books of Suvidhi Ltd.

Date			Debit (Rs.)	Credit (Rs.)
31.3.18	Bank A/c (60,000 shares x Rs. 30)	Dr.	18,00,000	
	Employees stock compensation expense A/c		4,80,000	
	To Share Capital A/c (60,000 shares x Rs. 10)			6,00,000
	To Securities Premium (60,000 shares x Rs. 28)			16,80,000
	(Being shares issued under ESOP @ Rs. 30 to 1,200 employees)			
	Profit & Loss A/c	Dr.	4,80,000	
	To Employees stock compensation expense			4,80,000
	(Being Employees stock compensation expense transferred to Profit & Loss A/c)			

Working Note:

Fair value of an option = Rs. 38 – Rs. 30 = Rs. 8

Number of shares issued = 1,200 employees x 50 shares/employee = 60,000 shares

Fair value of ESOP which will be recognized as expenses in the year 2017-2018

= 60,000 shares x Rs. 8 = Rs. 4,80,000

Vesting period = 1 year

Expenses recognized in 2017-2018 = Rs. 4,80,000

Question 2 : Nov – 2018 – Paper / Nov – 2020 - Paper

Lucky Ltd. grants 100 stock options to each of its 1,500 employees on 1-4-2014 for Rs. 40, depending upon the employees at the time of vesting of options. Options would be exercisable within a year it is vested. The market price of the share is Rs. 70 each. These options will vest at the end of year 1 if the earning of Lucky Ltd. is 15%, or it will vest at the end of the year 2 if the average earning of two years is 13% or lastly it will vest at the end of the third year if the average earning of 3 years will be 10% 8,000, unvested options lapsed on 31-3-2015. 6,000 unvested options lapsed on 31-3-2016 and finally 4,000 unvested options lapsed on 31-3-2017.

The earnings of Lucky Ltd. for the three financial years ended on 31st March, 2015; 2016 and 2017 are 14%, 10% and 8% respectively.

1,250 employees exercised their vested options within a year and remaining options were unexercised at the end of the contractual life.

You are required to give the necessary journal entries for the above and also prepare the statement showing compensation expense to be recognized at the end of each year.

Solution :

Date	Particulars		Debit (Rs.)	Credit (Rs.)
31.3.2015	Employees compensation expense A/c	Dr.	21,30,000	
	To ESOS outstanding A/c			21,30,000
	(Being compensation expense recognized in respect of the ESOP i.e. 100 options each granted to 1,500 employees at discount of Rs. 30 each, amortised on straight line basis over vesting years (Refer W.N.)			
	Profit and Loss A/c	Dr.	21,30,000	
	To Employees compensation expenses A/c			21,30,000
	(Being expenses transferred to profit and Loss A/c)			
31.3.2016	Employees compensation expenses A/c	Dr.	5,90,000	
	To ESOS outstanding A/c			5,90,000
	(Being compensation expense recognized in respect of the ESOP- Refer W.N.)			
	Profit and Loss A/c	Dr.	5,90,000	
	To Employees compensation expenses A/c			5,90,000
	(Being expenses transferred to profit and Loss A/c)			
31.3.2017	Employees compensation Expenses A/c	Dr.	12,40,000	
	To ESOS outstanding A/c			12,40,000
	(Being compensation expense recognized respect of the ESOP- Refer W.N.)			
	Profit and Loss A/c	Dr.	12,40,000	

	To Employees compensation expenses A/c (Being expenses transferred to profit and Loss A/c)			12,40,000
2018-19	Bank A/c (1,250 x100 x40) ESOS outstanding A/c [(39,60,000 x 1,25,000/ 1,32,000] To Equity share capital (1250 x 100 x 10) To Securities premium A/c [(1250 x 100 x (70-10)] (Being 1,25,000 options exercised at an exercise price of Rs. 40 each)	Dr. Dr.	50,00,000 37,50,000	 12,50,000 75,00,000
31.3.2019	ESOS outstanding A/c To General Reserve A/c (Being ESOS outstanding A/c on lapse of 7,000 options at the end of exercise of option period transferred to General Reserve A/c)	Dr.	2,10,000	 2,10,000

Working Note :

Statement showing compensation expense to be recognized at the end of:

Particulars	Year 1 2014-15	Year 2 2015-16	Year 3 2016-17
Number of options expected to vest*	1,42,000 options	1,36,000 options	1,32,000 options
Total compensation expense accrued (70-40)	Rs. 42,60,000	Rs. 40,80,000	Rs. 39,60,000
Compensation expense of the year	42,60,000 x 1/2 = Rs. 21,30,000	40,80,000 x 2/3 = Rs. 27,20,000	Rs. 39,60,000
Compensation expense recognized previously	Nil	Rs. 21,30,000	Rs. 27,20,000
Compensation expenses to be recognized for the year	Rs. 21,30,000	Rs. 5,90,000	Rs. 12,40,000

*It is assumed that each share is of Rs. 10 each and Lucky Ltd. expects all the options to be vested after deducting actual lapses during the year.

Question 3 : May – 2019 – RTP

A company has its share capital divided into shares of Rs.10 each. On 1-1-20X1, it granted 7,500 employees stock options at Rs.50, when the market price was Rs.140. The options were to be exercised between 1-3-20X2 to 31-03-20X2. The employees exercised their options for 7,200 shares only; remaining options lapsed. Pass the necessary journal entries for the year ended 31-3-20X2, with regard to employees' stock options.

Solution :

In the books of Company
Journal Entries

Date.	Particulars		Dr. Rs.	Cr. Rs.
1-3-X2 to 31-3-X2	Bank A/c (7,200 x 50)	Dr.	3,60,000	
	Employees compensation expenses A/c	Dr.	6,48,000	
	To Equity Share Capital A/c (7,200 x 10)			72,000
	To Securities Premium A/c (7,200 x Rs. 130)			9,36,000
	(Being allotment to employees 7,200 shares of Rs. 10 each at a premium of Rs. 130 at an exercise price of Rs. 50 each)			
31-3-X2	Profit and Loss account	Dr.	6,48,000	
	To Employees compensation expenses A/c			6,48,000
	(Being transfer of employees compensation expenses)			

Working Notes:

1. Employee Compensation Expenses = Discount between Market Price and option price = Rs. 140 – Rs. 50 = Rs. 90 per share = Rs. 90 x 7,200 = Rs. 6,48,000 in total.
2. Securities Premium Account = Rs. 50 – Rs. 10 = Rs. 40 per share + Rs. 90 per share on account of discount of option price over market price = Rs. 130 per share = Rs. 130 x 7,200= Rs. 9,36,000 in total.

Question 4 : May – 2019 – Paper

Bee Ltd. has its share capital divided into Equity Shares of Rs.10 each. On 1st April, 2017, the company offered 250 shares to each of its 520 employees at Rs.60 per share, when the market price was Rs.150 per share. The options were to be exercised between 01-03-2018 to 31-03-2018. 410 employees accepted the offer and paid Rs.60 per share on purchased shares and the remaining options lapsed.

The company closes its books on 31st March every year.

You are required to show Journal Entries (with narrations) as would appear in the books of Bee Ltd. for the year ended 31st March, 2018 with regard to employees stock options.

Solution :

Journal Entries in the books of Bee Ltd.

Date	Particulars		Debit (Rs.)	Credit (Rs.)
1.3.18 to 31.3.18	Bank A/c (1,02,500 x Rs. 60)	Dr.	61,50,000	
	Employee compensation expense A/c (1,02,500 x Rs.90)	Dr.	92,25,000	
	To Equity share capital A/c (1,02,500 x Rs.10			10,25,000

	To Securities premium A/c (1,02,500 x Rs.140) (Being shares issued to the employees against the options vested to them in pursuance Employee Stock Option Plan)		1,43,50,000
31.3.18	Profit and Loss A/c Dr. To Employee compensation expense (Being transfer of employee compensation expenses to Profit and Loss Account)	92,25,000	 92,25,000

Question 5 : Nov – 2019 – RTP

The following particulars in respect of stock options granted by a company are available:

Grant date	April 1, 2016
Number of employees covered	50
Number of options granted per employee	1,000
Fair value of option per share on grant date (Rs.)	9

The options will vest to employees serving continuously for 3 years from vesting date, provided the share price is Rs. 65 or above at the end of 2018-19.
The estimates of number of employees satisfying the condition of continuous employment were 48 on 31/03/17, 47 on 31/03/18. The number of employees actually satisfying the condition of continuous employment was 45.
The share price at the end of 2018-19 was Rs. 68.
You are required to compute expenses to be recognised in each year in the books of the company.

Solution :

The vesting of options is subject to satisfaction of two conditions viz. service condition of continuous employment for 3 years and market condition that the share price at the end of 2018-19 is not less than Rs. 65. The company should recognise value of option over 3-year vesting period from 2016-17 to 2018-19.

Year 2016-17

Fair value of option per share = Rs. 9
Number of shares expected to vest under the scheme = 48 × 1,000 = 48,000
Fair value = 48,000 × Rs. 9 = Rs. 4,32,000
Expected vesting period = 3 years
Value of option recognised as expense in 2016-17 = Rs. 4,32,000 /3 = Rs. 1,44,000

Year 2017-18

Fair value of option per share = Rs. 9
Number of shares expected to vest under the scheme = 47 × 1,000 = 47,000
Fair value = 47,000 × Rs. 9 = Rs. 4,23,000
Expected vesting period = 3 years
Cumulative value of option to recognise as expense in 2016-17 and 2017-18
= (Rs. 4,23,000/ 3) × 2 = Rs. 2,82,000

Value of option recognised as expense in 2016-17 = Rs. 1,44,000
Value of option recognised as expense in 2017-18
= Rs. 2,82,000 – Rs. 1,44,000 = Rs. 1,38,000

Year 2018-19

Fair value of option per share = Rs. 9
Number of shares actually vested under the scheme = 45 × 1,000 = 45,000
Fair value = 45,000 × Rs. 9 = Rs. 4,05,000
Vesting period = 3 years
Cumulative value of option to recognise as expense in 2016-17, 2017-18 and 2018-19 = Rs. 4,05,000
Value of option recognised as expense in 2016-17 and 2017-18 = Rs. 2,82,000
Value of option recognised as expense in 2018-19 = Rs. 4,05,000 – Rs. 2,82,000 = Rs. 1,23,000

Question 6 : Nov – 2019 – Paper

On 1st April, 2018, XYZ Ltd., offered 150 shares to each of its 750 employees at Rs.60 per share. The employees are given a year to accept the offer. The shares issued under the plan shall be subject to lock-in period on transfer for three years from the grant date. The market price of shares of the company on the grant date is Rs.72 per share. Due to post-vesting restrictions on transfer, the fair value of shares issued under the plan is estimated at Rs.67 per share.
On 31st March, 2019, 600 employees accepted the offer and paid Rs.60 per share purchased. Nominal value of each share is Rs.10.
You are required to record the issue of shares in the books of the XYZ Ltd., under the aforesaid plan.

Solution :

Fair value of an option = Rs. 67(considered on grant date) – Rs. 60 = Rs. 7
Number of shares issued = 600 employees x 150 shares/employee = 90,000 shares
Fair value of ESOP = 90,000 shares x Rs. 7 = Rs. 6,30,000
Vesting period = 1 year
Expenses recognized in 2018-19 = Rs. 6,30,000

Date.	Particulars		Dr. Rs.	Cr. Rs.
31.03.2019	Bank (90,000 shares x Rs. 60)	Dr.	54,00,000	
	Employees stock compensation expense A/c	Dr.	6,30,000	
	To Share Capital (90,000 shares x Rs. 10)			9,00,000
	To Securities Premium (90,000shares x Rs. 57)			51,30,000
	Being option accepted by 600 employees & payment made @ Rs. 60 per share)			
	Profit & Loss A/c	Dr.	6,30,000	
	To Employees stock compensation expense A/c			6,30,000
	Being Employees stock compensation expense transferred to Profit & Loss A/c)			

Question 7 : May – 2020 – RTP

On 1st April, 2019, a company offered 100 shares to each of its 400 employees at Rs.25 per share. The employees are given a month to accept the shares. The shares issued under the plan shall be subject to lock-in to transfer for three years from the grant date i.e. 30th, April 2019. The market price of shares of the company on the grant date is Rs.30 per share. Due to post-vesting restrictions on transfer, the fair value of shares issued under the plan is estimated at Rs.28 per share.

Up to 30th April, 2019, 50% of employees accepted the offer and paid Rs.25 per share purchased. Nominal value of each share is Rs.10. You are required to record the issue of shares in the books of the company under the aforesaid plan.

Solution :

Fair value of an option = Rs. 28

Difference between Fair value and Issue Price =Rs. 28 – Rs. 25 = 3.

Number of employees accepting the offer = 400 employees x 50% = 200 employees

Number of shares issued = 200 employees x 100 shares/employee = 20,000 shares

Employee Compensation Expenses recognized in 2019-20 =20,000 shares x Rs. 3 = Rs. 60,000

Securities Premium A/c = Rs. 28 – 10 = Rs. 18 per share = 20,000 x 18 = Rs. 3,60,000

Journal Entry

Date.	Particulars		Dr. Rs.	Cr. Rs.
30.04.2019	Bank (20,000 shares x Rs. 25)	Dr.	5,00,000	
	Employees compensation expense A/c	Dr.	60,000	
	To Share Capital			2,00,000
	To Securities Premium			3,60,000
	(Being stock purchase option accepted by 200 employees for 100 shares each at Rs. 25 per share on a Fair Value of Rs. 28 per share)			

Note: Employees compensation expenses amounting Rs. 60,000 will ultimately be charged to profit & loss account.

Question 8 : Nov – 2020 – RTP

Kaushal Ltd. has its share capital divided into equity shares of Rs.10 each. On 1.1.2020 it granted 5,000 employee stock options at Rs.30 per share, when the market price was Rs.50 per share. The options were to be exercised till the month of March, 2020. The employees exercised their options for 3,600 shares only and the remaining options lapsed. Show Journal entries (with narration) as would appear in the books of the company till the month of March, 2020 relating to ESOPs as the company closes its books on 31st March every year.

Solution :

Journal Entries in the books of Kaushal Ltd.

Date.	Particulars		Dr. Rs.	Cr. Rs.
1.3.2020 to 31.3.2020	Bank A/c	Dr.	1,08,000	
	Employee compensation expense A/c	Dr.	72,000	
	To Equity share capital A/c			36,000
	To Securities premium A/c			1,44,000
	(Being shares issued to the employees against the options vested to them in pursuance of Employee Stock Option Plan)			
31.3.2020	Profit and Loss A/c	Dr.	72,000	
	To Employee compensation expenses A/c			72,000
	(Being transfer of employee compensation expenses transfer to Profit and Loss Account)			

Working Note:

Market Price = Rs.50 per share and stock option price = Rs.30, Hence, the difference Rs.50 – Rs.30 = Rs.20 per share is equivalent to employee cost or employee compensation expense and will be charged to P&L Account as such for the number of options exercised i.e. 3,600 shares.

Question 9 : Jan – 2021 – Paper

Raja Ltd. has its share capital divided into equity shares of Rs.10 each. On 01.08-2019, it granted 2,500 employees stock options at Rs.50 per share, when the market price was Rs.140 per share. The options were to be exercised between 1-10-2019 to 31-03-2020. The employees exercised their options for 2,400 share only and the remaining options lapsed. Raja Ltd. close its books of accounts on 31st March, every year.

You are required to pass the necessary Journal Entries (including narration) for the year ended 31-03-2020, with regard to employees stock options and give working notes also.

Solution :

Journal Entries in the books of Raja Ltd.

			Rs.	Rs.
1.10.19 to 31.3.20	Bank A/c	Dr.	1,20,000	
	Employee compensation expense A/c	Dr.	2,16,000	
	To Equity share capital A/c			24,000
	To Securities premium A/c			3,12,000
	(Being shares issued to the employees against the options vested to them in pursuance of Employee Stock Option Plan)			
31.3.20	Profit and Loss A/c	Dr.	2,16,000	
	To Employee compensation expense A/c			2,16,000

	(Being transfer of employee compensation expenses to Profit and Loss Account)		

No entry is passed when stock options are granted to employees. Hence, no entry will be passed on 1st August, 2019;

Working Note:

Market Price = Rs. 140 per share and stock option price = 50, Hence, the difference 140 – 50 = Rs.90 per share is equivalent to employee cost or employee compensation expense and will be charged to P&L Account as such for the number of options exercised i.e. 2,400 shares. Hence, Employee compensation expenses will be 2,400 shares X Rs. 90 = Rs. 2,16,000

Question 10 : May – 2021 – RTP

Define the following terms:

(i) Vesting Period; (ii) Grant Date.

Solution :

(i) **Vesting Period**: It is the time period between grant date and the date on which all the specified vesting conditions of an employee share-based payment plan is to be satisfied.

(ii) **Grant Date:** It is the date at which the enterprise and its employees agree to the terms of an employee share-based payment plan. At grant date, the enterprise confers on the employees the right to cash or shares of the enterprise, provided the specified vesting conditions, if any, are met. If that agreement is subject to an approval process, (for example, by shareholders), grant date is the date when that approval is obtained.

Question 11 : May – 2021 – RTP

PQ Ltd. grants 100 stock options to each of its 1,000 employees on 1-4-2018, conditional upon the employee remaining in the company for 2 years. The fair value of the option is Rs. 18 on the grant date and the exercise price is Rs. 55 per share. Number of employees expected to satisfy service conditions are 930 in the 1st year and 850 in the 2nd year. However, 880 employees actually completed 2 year vesting period.

You are required to calculate ESOP cost to be amortized by PQ Ltd. in the years 2018-2019 and 2019-2020.

Solution :

Calculation of ESOP cost to be amortized

	2018-2019	**2019-2020**
Fair value of options per share	Rs.18	Rs.18
No. of options expected to vest under the scheme	93,000 (930 x 100)	88,000 (880 x 100)
Fair value of options	Rs.16,74,000	Rs.15,84,000
Value of options recognized as expenses	8,37,000 (Rs.16,74,000 / 2)	7,47,000 (Rs.15,84,000 – Rs.8,37,000)

Question 12 : July – 2021 – Paper

At the beginning of the year 1, Harmony Limited grants 600 options to each of its 1000 employees. The contractual life of option granted is 6 years.
Other relevant information is a follows :

Vesting Period	3 years
Exercise period	3 years
Expected Life	5 years
Exercise Price	Rs.100
Market Price	Rs.100
Expected Forfeitures per year	3%

The option granted vest according to a graded schedule of 25% at the end of the year 1, 25% at the end of the year 2 and the remaining 50% at the end of the year 3.
You are required to calculate total compensation expenses for the options expected to vest and cost and cumulative cost to be recognized at the end of all the three years assuming that expected forfeiture rate does not change during the vesting period when the Intrinsic value of the options at the grant date is Rs.7 per options.

Solution :

Since the options granted have a graded vesting schedule, the enterprise segregates the total plan into different groups, depending upon the vesting dates and treats each of these groups as a separate plan. The enterprise determines the number of options expected to vest under each group as below:

Vesting Date (Year-end)		**Options expected to vest**
1	600 options x 1,000 employees x 25% x 0.97	1,45,500 options
2	600 options x 1,000 employees x 25% x 0.97 x 0.97	1,41,135 options
3	600 options x 1,000 employees x 50% x 0.97x 0.97 x 0.97	2,73,802 options
Total options expected to vest		5,60,437 options

In case of intrinsic value method, total compensation expense for the options expected to vest would be

Vesting Date (End of year)	**Expected Vesting (No. of Options)**	**Value per Option (Rs.)**	**Compensation Expense (Rs.)**
1	1,45,500	7	10,18,500
2	1,41,135	7	9,87,945
3	2,73,802	7	19,16,614
	5,60,437		39,23,059

Total compensation expense of Rs. 39,23,059, determined at the grant date, would be attributed to the years 1, 2 and 3 as below:

Vesting Date (End of year)	Cost to be recognized		
	Year 1	Year 2	Year 3
1	10,18,500		
2	4,93,972.50*	4,93,972.50	
3	6,38,871	6,38,871	6,38,872
Cost for the year	21,51,343.50	11,32,843.50	6,38,872
Cumulative cost	21,51,343.50	32,84,187	39,23,059

* Alternatively, it may be rounded off as Rs. 4,93,972 in year 1 and Rs. 4,93,973 in year 2.

Question 13 : Nov – 2021 – RTP

On 1st April, 2020, XYZ Ltd., offered 150 shares to each of its 750 employees at Rs. 60 per share. The employees are given a year to accept the offer. The shares issued under the plan shall be subject to lock-in period on transfer for three years from the grant date. The market price of shares of the company on the grant date is Rs. 72 per share. Due to post-vesting restrictions on transfer, the fair value of shares issued under the plan is estimated at Rs. 67 per share on the grant date. On 31st March, 2021, 600 employees accepted the offer and paid Rs. 60 per share purchased. Face value of each share is Rs. 10. You are required to record the issue of shares in the books of the XYZ Ltd., under the aforesaid plan.

Solution :

Fair value of an option = Rs. 67 – Rs. 60 = Rs. 7

Number of shares issued = 600 employees x 150 shares/employee = 90,000 shares

Fair value of ESOP = 90,000 shares x Rs. 7 = Rs. 6,30,000

Vesting period = 1 year

Expenses recognized in 2020-21 = Rs. 6,30,000

Date	Particulars		Rs.	Rs.
31.03.2021	Bank (90,000 shares x Rs. 60)	Dr.	54,00,000	
	Employees stock compensation expense A/c	Dr.	6,30,000	
	To Share Capital (90,000 shares x Rs. 10)			9,00,000
	To Securities Premium (90,000 shares x Rs. 57)			51,30,000
	(Being option accepted by 600 employees & payment made @ Rs. 60 per share)			
	Profit & Loss A/c	Dr.	6,30,000	
	To Employees stock compensation expense A/c			6,30,000
	(Being Employees stock compensation expense transferred to Profit & Loss A/c)			

Question 14 : Nov – 2021 – RTP

Define the following terms:

(i) Vesting (ii) Exercise Period

(iii) Grant date (iv) Exercise Price

Solution :

(i) **Vesting**: It means the process by which the employee is given the right to apply for the shares of the company against the option granted to him under the employees' stock option plan.

(ii) **Exercise Period:** It is the time period after vesting within which the employee should exercise his right to apply for shares against the option vested in him in pursuance of the employees' stock option plan.

(iii) **Grant Date**: It is the date at which the enterprise and its employees agree to the terms of an employee share-based payment plan. At grant date, the enterprise confers on the employees the right to cash or shares of the enterprise, provided the specified vesting conditions, if any, are met.

(iv) **Exercise Price**: It is the price payable by the employee for exercising the option granted to him in pursuance of employees' stock option scheme.

Question 15 : Dec – 2021 – Paper

A Company grants 2,000 Employees Stock Option on 1st April, 2018 at Rs.60 when the market price is Rs.170. The vesting period is 2.5 years and the maximum exercise period is 1 year. 600 unvested options lapse 01.05.2020. 1200 options are exercised on 30.06.2021. 200 vested options lapse at the end of the exercise period. You are required to pass necessary journal entries with narrations.

Solution :

Journal Entries in the books of Company

Date	Particulars		Dr. (Rs.)	Cr. (Rs.)
31.3.2019	Employees compensation expense account	Dr.	88,000	
	To Employee stock option outstanding account			88,000
	(Being compensation expenses recognized in respect of the employee stock option)			
	Profit and loss account			
	To Employees compensation expenses account			
	(Being expenses transferred to profit and loss account at year end)			
31.3.2020	Employees compensation expenses account	Dr.	88,000	
	To Employee stock option outstanding account			88,000
	(Being compensation expense recognized in respect of the employee stock)			
	Profit and loss account	Dr.	88,000	
	To Employees compensation expenses account			88,000

	(Being expenses transferred to profit and loss account at year end)		
31.3.2021	Employee stock option outstanding account (W.N.2) Dr. To General Reserve account (W.N.2) (Being excess of employees compensation expenses transferred to general reserve account)	22,000	 22,000
30.6.2021	Bank A/c (1,200 × Rs. 60) Dr. Employee stock option outstanding account (1,200 × Rs. 110) Dr. To Equity share capital account (1,200 × Rs. 10) To Securities premium account (1,200 x Rs. 160) (Being 1,200 employee stock option exercised at an exercise price of Rs. 60 each)	72,000 1,32,000	 12,000 1,92,000
01.10.2021	Employee stock option outstanding account (W.N.3) Dr. Rs.To General reserve account (W.N.3) (Being ESOS outstanding A/c on lapse of 200 options at the end of exercise of option period transferred to General Reserve A/c)	22,000	 22,000

Working Notes:

1. Compensation expenses recognized in respect of the employee stock option:

   2,000 options granted to employees at a discount of Rs. 110 each to be amortized on Straight line basis over $2\frac{1}{2}$ years

   2,000 stock options x Rs. 110 / 2.5 years = Rs. 88,000

2. On 31.3.2021, company will examine its actual forfeitures and make necessary adjustments, if any, to reflect expenses for the number of options that actually vested. Considering that 1400 stock options have completed 2.5 years vesting period, the expense to be recognized during the year is in negative i.e.

No. of options actually vested 1,400 x 110 (170 – 60 = 110)	Rs. 1,54,000
Less: Expenses recognized Rs. (88,000 + 88,000)	(Rs. 1,76,000)
Excess expense transferred to general reserve	Rs. 22,000

3. Similarly, on 1.10.2021, Employee Stock Option Outstanding Account will be

No. of options actually vested (1,200 × 110)	Rs. 1,32,000
Less: Expenses recognized	(Rs. 1,54,000)
Excess expense transferred to general reserve	Rs. 22,000

Question 16 : May – 2022 – RTP

Define the following terms:

(i) Vesting

(ii) Grant date

(iii) Exercise Price

Solution :

(i) **Vesting** means to become an entitlement. Under an employee stock option plan, a counterparty's right to receive cash, other assets or equity instruments of the enterprise vests when the counterparty's entitlement is no longer conditional on the satisfaction of any vesting conditions.

(ii) **Grant Date** is the date at which the enterprise and another party (i.e. an employee) agree to an employee stock option plan, being when the enterprise and the counterparty have a shared understanding of the terms and conditions of the arrangement. At grant date, the enterprise confers on the counterparty the right to cash, other assets, or equity instruments of the enterprise, provided the specified vesting conditions, if any, are met. If that agreement is subject to an approval process (for example, by shareholders), grant date is the date when that approval is obtained.

(iii) **Exercise Price** is the price payable by the counterparty for exercising the option granted to him/her/it in pursuance of the employee stock option plan.

Question 17 : May – 2022 – RTP

Noor Ltd. has its share capital divided into equity shares of Rs. 10 each. On 1.1.2021 it granted 4,000 employee stock options at Rs. 40 per share, when the market price was Rs. 60 per share. Fair value per option was Rs. 20. The options were to be exercised between 15th March, 2021 and 31st March, 2021. The employees exercised their options for 2,500 shares only and the remaining options lapsed. The company closes its books on 31st March every year. You are required to give Journal entries (with narration) as would appear in the books of the company for the year ended 31st March, 2021.

Solution :

Journal Entries in the books of Noor Ltd.

			Rs.	**Rs.**
15.03.2021	Bank A/c (2,500 shares x Rs. 40)	Dr.	1,00,000	
to	Employee compensation expense A/c	Dr.	50,000	
31.3.2021	(2,500 shares x Rs. 20)			
	To Equity share capital A/c			25,000
	(2,500 shares x Rs. 10)			
	To Securities premium A/c			1,25,000
	(2,500 shares x Rs. 50)			
	(Being shares issued to the employees against the options vested to them pursuance of Employee Stock Option Plan)			
31.3.2021	Profit and Loss A/c	Dr.	50,000	
	To Employee compensation expenses A/c			50,000

	(Being transfer of employee compensation expenses transfer to Profit and Loss Account)		

Working Notes:

1. No entry is passed when stock options are granted to employees. Hence no entry will be passed on 1 January 2021.
2. Fair value per option i.e. Rs. 20 per option is the employee cost or employee compensation expense and will be charged to P&L Account for the number of options exercised.

Question 18 : May – 2022 – Paper

On 1st April, 2021, a company offered 100 shares to each of its 5,000 employees at Rs.50 per share. The employees are given a year to accept the offer. The shares issued under the plan shall be subject to lock-in on transfer for three years from the grant date. The market price of shares of the company on the grant date is Rs.60 per share. Due to post-vesting restrictions on transfer, the fair value of shares issued under the plan is estimated at Rs.56 per share and fair value per option worked out to be Rs.6.

On 31st March, 2022, 4,000 employees accepted the offer and paid Rs.50 per share purchased. Nominal value of each share is Rs.10.

You are required to pass journal entries (with narration) as would appear in the books of the company up to 31st March, 2022.

Solution :

Fair value of an option = Rs. 56 – Rs. 50 = Rs. 6

Number of shares issued = 4,000 employees x 100 shares = 4,00,000 shares

Fair value of ESOP = 4,00,000 shares x Rs. 6 = Rs. 24,00,000

Vesting period = 1 year

Expenses recognized in 2021 – 22 = Rs. 24,00,000

Date	Particulars		Rs.	Rs.
31.03.2022	Bank (4,00,000 shares x Rs. 50)	Dr.	2,00,00,000	
	Employees stock compensation expense A/c	Dr.	24,00,000	
	To Share Capital (4,00,000 shares x Rs. 10)			40,00,000
	To Securities Premium (4,00,000 shares x Rs. 46)			1,84,00,000
	(Being option accepted by 4,000 employees & payment made @ Rs. 56 share)			
	Profit & Loss A/c	Dr.	24,00,000	
	To Employees stock compensation expense A/c			24,00,000
	(Being Employees stock compensation expense transferred to Profit & Loss A/c)			

Question 19 : Nov – 2022 – RTP

Mehta Ltd. grants 1,500 stock options to its employees on 1.4.2019 at Rs. 50. The vesting period is two and a half years. The maximum exercise period is one year. Market price on that date is Rs. 80. Fair value per option is Rs. 30. All the options were exercised on 31.7.2022. Give the necessary journal entries if the face value of equity share is Rs. 10 per share.

Solution :

Books of Mehta Ltd.

Journal Entries

Date	Particulars		Debit Rs.	Credit Rs.
31.3.2020	Employees Compensation Expense Account	Dr.	18,000	
	To Employees Stock Option Outstanding Account			18,000
	(Being compensation expense recognized in respect of 1,500 options granted to employees at discount of Rs. 30 each, amortized on straight line basis over 2½ years) (Refer WN)			
	Profit and Loss Account	Dr.	18,000	
	To Employees Compensation Expense Account			18,000
	(Being employees compensation expense of the year transferred to P&L A/c)			
31.3.2021	Employees Compensation Expense Account	Dr.	18,000	
	To Employees Stock Option Outstanding Account			18,000
	(Being compensation expense recognized in respect of 1,500 options granted to employees at discount of Rs. 30 each, amortized on straight line basis over 2½ years) (Refer WN)			
	Profit and Loss Account	Dr.	18,000	
	To Employees Compensation Expense Account			18,000
	(Being employees compensation expense of the year transferred to P&L A/c)			
31.3.2021	Employees Compensation Expense Account	Dr.	9,000	

	To Employees Stock Option Outstanding Account (Being balance of compensation expense amortized Rs. 45,000 less Rs. 36,000) (Refer WN)			9,000
	Profit and Loss Account To Employees Compensation Expense Account (Being employees compensation expense of the year transferred to P&L A/c)	Dr.	9,000	9,000
31.7.2022	Bank Account (Rs. 50 × 1,500) To Equity Share Capital Account To Securities Premium Account (Being exercise of 1,500 options at an exercise price of Rs. 50)	Dr.	75,000	15,000 60,000
31.7.2022	Stock Option Outstanding A/c (Rs. 30 x 1,500) To Securities Premium Account (Being the balance in the Employees Stock Option Outstanding Account transferred to Securities Premium A/c)	Dr.	45,000	45,000

Working Notes:

1. Total employees compensation expense = 1,500 x (Rs. 80 – Rs. 50) = Rs. 45,000
2. Employees compensation expense has been written off during 2½ years on straight line basis as under:
   I year = Rs. 18,000 (for full year)
   II year = Rs. 18,000 (for full year)
   III year = Rs. 9,000 (for half year)

Question 20 : Nov – 2022 – Paper

At the beginning of year 1, an enterprise grants 1,000 stock options to a senior executive, conditional upon the executive remaining in the employment of the enterprise until the end of year 3. The exercise price is Rs.400. However, the exercise price drops to Rs.300 if the earnings of the enterprise increase by at-least an average of 10 percent per year over the three-year period. On the grant date, the enterprise estimates that the fair value of the stock options, with an exercise price of Rs.300, is Rs.160 per option. If the exercise price is Rs.400, the enterprise estimates that the stock options have a fair value of Rs.120 per option.

During year 1, the earnings of the enterprise increased by 12 percent, and the enterprise expects that earnings will continue to increase at this rate over the next two years. The enterprise,

therefore, expects that the earnings target will be achieved, and hence the stock options will have an exercise price of Rs.300.

During year 2, the earnings of the enterprise increased by 13 percent and the enterprise continues to expect that the earnings target will be achieved.

During year 3, the earnings of the enterprise increased by only 3 percent, and therefore the earnings target was not achieved. The executive completes three years' service, and therefore satisfies the service condition. Because the earnings target was not achieved, the 1,000 vested stock options have an exercise price of Rs.400.

You are required to calculate the amount to be charged to Profit and Loss Account every year on account of compensation expenses.

Thanks ....

CHAPTER 16

BUY BACK OF SECURITIES & EQUITY SHARES WITH DIFFERENTIAL RIGHTS

Question 1 : May – 2018 – Paper

Alpha Ltd. furnishes the following summarized Balance Sheet as at 31st March, 2017:

	Rs. In lakhs	Rs. In lakhs
Equity & Liabilities		
Shareholders' Funds		
Equity share capital (fully paid up shares of Rs.10 each)		2,400
Reserves and Surplus		
Securities Premium	350	
General Reserve	530	
Capital Redemption Reserve	400	
Profit & Loss Account	340	1,620
Non-current Liabilities		
12% Debentures		1,500
Current Liabilities		
Trade Payables	1,490	
Other Current Liabilities	390	1,880
Total		**7,400**
Assets		
Non-current Assets		
Fixed Assets		4,052
Current Assets		
Current Investments	148	
Inventories	1,200	
Trade Receivables	520	
Cash and Bank	1,480	3,348
Total		**7,400**

(i) On 1st April, 2017, the company announced buy-back of 25% of its equity shares @ Rs. 15 per share. For this purpose, it sold all its investment for Rs. 150 lakhs.

(ii) On 10th April, 2017 the company achieved the target of buy-back.

(iii) On 30th April, 2017, the company issued one fully paid up equity share of Rs. 10 each by way of bonus for every four equity shares held by the equity shareholders by capitalization of Capital Redemption Reserve.

You are required to pass necessary journal entries and prepare the Balance Sheet of Alpha Ltd. after bonus issue.

Solution :

In the books of Alpha Limited
Journal Entries

Date 2017	Particulars		Debit	Credit
			(Rs. in lakhs)	
1-Apr	Bank A/c	Dr.	150	
	To Investment A/c			148
	To Profit on sale of investment			2
	(Being investment sold on profit)			
10-Apr	Equity share capital A/c	Dr.	600	
	Securities premium A/c	Dr.	300	
	To Equity shares buy back A/c			900
	(Being the amount due to equity shareholders on buy back)			
	Equity shares buy back A/c	Dr.	900	
	To Bank A/c			900
	(Being the payment made on account of buy back of 60 Lakh Equity Shares)			
10-Apr	General reserve A/c	Dr.	530	
	Profit and Loss A/c	Dr.	70	
	To Capital redemption reserve (CRR) A/c			600
	(Being amount equal to nominal value of buy back shares from free reserves transferred to capital redemption reserve account as per the law)			
30-Apr	Capital redemption reserve A/c	Dr.	450	
	To Bonus shares A/c (W.N.1)			450
	(Being the utilization of capital redemption reserve issue bonus shares)			
	Bonus shares A/c	Dr.	450	
	To Equity share capital A/c			450
	(Being issue of one bonus equity share for every four equity shares held)			
	Profit on sale of Investment	Dr.	2	
	To Profit and Loss A/c			2
	(Profit on sale transfer to Profit and Loss A/c)			

Note: For transferring amount equal to nominal value of buy back shares from free reserves to capital redemption reserve account, the amount of Rs. 340 lakhs from P & L A/c and the balance from general reserve may also be utilized. The combination of different set of amounts (from

General Reserve and Profit and Loss Account) aggregating Rs. 600 lakhs may also be considered for the purpose of transfer to CRR.

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

	Particulars	Notes	Amount (Rs. in Lakhs)
I.	**Equity and Liabilities**		
	(1) Shareholder's Funds		
	(a) Share Capital	1	2,250
	(b) Reserves and Surplus	2	872
	(2) Non-Current Liabilities		
	(a) Long-term borrowings - 12% Debentures		1,500
	(3) Current Liabilities		
	(a) Trade payables		1,490
	(b) Other current liabilities		390
	Total		**6,502**
II.	**Assets**		
	(1) Non-current assets		
	(a) Fixed assets		
	(i) Tangible assets		4,052
	(2) Current assets		
	(a) Current investments		
	(b) Inventory		1,200
	(c) Trade receivables		520
	(d) Cash and cash equivalents (W.N. 2)		730
	Total		**6,502**

Notes to Accounts

				Rs. in lakhs
1.	Share Capital			
	Equity share capital (225 lakh fully paid up shares of Rs. 10 each)			2,250
2.	Reserves and Surplus			
	General Reserve	530		
	Less: Transfer to CRR	(530)		
	Capital Redemption Reserve	400		
	Add: Transfer due to buy-back of shares from P/L	70		
	Add: Transfer due to buy-back of shares from Gen. res.	530		
	Less: Utilisation for issue of bonus shares	(450)	550	
	Securities premium	350		
	Less: Adjustment for premium paid on buy back	300)	50	
	Profit & Loss A/c	340		

	Add: Profit on sale of investment	2		
	Less: Transfer to CRR	(70)	272	872

Working Notes:

1. **Amount of equity share capital** = 2,400 - 600 (buyback) + 450 (Bonus shares) = 2,250
2. **Cash at bank after issue of bonus shares**

	Rs. in lakhs
Cash balance as on 1st April, 2017	1480
Add: Sale of investments	150
	1630
Less: Payment for buy back of shares	(900)
	730

Question 2 : Nov – 2018 – Paper

Equity capital is held by L, M, N and O in the proportion of 30:40:20:10. A, B, C and D hold Preference share capital in the proportion of 40:30:10:20. If the paid up Equity Share capital of the company is Rs.60 lakhs and Preference share capital is Rs.30 lakhs, find the voting rights of shareholders (in percentage) in case of resolution of winding up of the company.

Solution :

L, M, N and O hold Equity capital is held by in the proportion of 30:40:20:10 and A, B, C and D hold preference share capital in the proportion of 40:30:10:20. As the paid up equity share capital of the company is Rs.60 Lakhs and Preference share capital is Rs. 30 Lakh (2:1), then relative weights in the voting right of equity shareholders and preference shareholders will be 2/3 and 1/3.

The respective voting right of various shareholders will be

L	=	2/3 X 30/100 =	3/15	=	20%
M	=	2/3 X 40/100 =	4/15	=	26.67%
N	=	2/3 X 20/100 =	2/15	=	13.33%
O	=	2/3 X 10/100 =	1/15	=	6.67%
A	=	1/3 X 40/100 =	4/30	=	13.33%
B	=	1/3 X 30/100 =	3/30	=	10%
C	=	1/3 X 10/100 =	1/30	=	3.33%
D	=	1/3 X 20/100 =	2/30	=	6.67%

Question 3 : May – 2019 – RTP

Alpha Limited furnishes the following summarized Balance Sheet as at 31st March, 2017:

Liabilities	(Rs. In lakhs)	Assets	(Rs. In lakhs)
Equity share capital (fully paid up shares of Rs.10 each)	2,400	Machinery	3,600
Securities premium	350	Furniture	450
General reserve	530	Investment	148

Capital redemption reserve	400	Inventory	1,200
Profit & loss A/c	340	Trade receivables	500
12% Debentures	1,500	Cash at bank	1,500
Trade payables	1,400		
Other current liabilities	478		
	7,398		**7,398**

On 1st April, 2017, the company announced the buy back of 25% of its equity shares @ Rs.15 per share. For this purpose, it sold all of its investments for Rs.150 lakhs.

On 5th April, 2017, the company achieved the target of buy back.

You are required to:

(1) Pass necessary journal entries for the buy-back.

(2) Prepare Balance Sheet of Alpha Limited after buy-back of the shares.

Solution :

In the books of Alpha Limited
Journal Entries

Date. 2017	Particulars		Dr. (Rs. In lakhs)	Cr. (Rs. In lakhs)
1-Apr	Bank A/c	Dr.	150	
	To Investment A/c			148
	To Profit on sale of investment			2
	(Being investment sold on profit)			
5-Apr	Equity share capital A/c	Dr.	600	
	Securities premium A/c	Dr.	300	
	To Equity shares buy back A/c			900
	(Being the amount due to equity shareholders on buy back)			
	Equity shares buy back A/c	Dr.	900	
	To Bank A/c			900
	(Being the payment made on account of buy back of 60 Lakh Equity Shares)			
5-Apr	General reserve A/c	Dr.	530	
	Profit and Loss A/c	Dr.	70	
	To Capital redemption reserve A/c			600
	(Being amount equal to nominal value of bought back shares from free reserves transferred to capital redemption reserve account as per the law)			

Balance Sheet (After Buy Back)

		Particulars	Notes	Amount (Rs. in Lakhs)
I.		**Equity and Liabilities**		
(1)		**Shareholder's Funds**		
	a	Share Capital	1	1,800
	b	Reserves and Surplus	2	1,322
(2)		**Non-Current Liabilities**		
	a	Long-term borrowings - 12% Debentures		1,500
(3)		**Current Liabilities**		
	a	Trade payables		1,400
	b	Other current liabilities		478
		Total		**6,500**
II.		**Assets**		
(1)		**Non-current assets**		
	a	Property, Plant & Equipment		
		(i) Tangible assets	3	4,050
(2)		**Current assets**		
	a	Current investments		
	b	Inventory		1,200
	c	Trade receivables		5,00
	d	Cash and cash equivalents (W.N.)		750
		Total		**6,500**

Notes to Accounts

				(Rs. in Lakhs)
1	**Share Capital**			
	Equity share capital (Fully paid up shares of Rs.10 each)			1800
2	**Reserves and Surplus**			
	General Reserve	530		
	Less: Transfer to CRR	(530)	-	
	Capital Redemption Reserve	400		
	Add: Transfer due to buy-back of shares from P/L	70		
	Transfer due to buy-back of shares from Gen. res.	530	1,000	
	Securities premium	350		
	Less: Adjustment for premium paid on buy back	(300)	50	
	Profit & Loss A/c	340		
	Add: Profit on sale of investment	2		
	Less: Transfer to CRR	(70)	272	1,322
3	**Tangible assets**			
	Machinery		3,600	
	Furniture		450	4,050

Working Note :
Cash at bank after buy-back

	Rs. in lakhs
Cash balance as on 1st April, 2017	1,500
Add: Sale of investments	150
	1,650
Less: Payment for buy back of shares	(900)
	750

Question 4 : May – 2019 – RTP

Explain the conditions under Companies (Share Capital and Debentures) Rules, 2014, to deal with equity shares with differential rights.

Solution :

In exercise of the power conferred under Section 43(a)(ii), the central government announced Rule 4 under Companies (Share Capital and Debentures) Rules, 2014, to deal with equity shares with differential rights.

The rules lay down the following conditions to be compulsorily complied with:

(a) The articles of association of the company authorizes the issue of shares with differential rights;

(b) The issue of shares is authorized by an ordinary resolution passed at a general meeting of the shareholders: Provided that where the equity shares of a company are listed on a recognized stock exchange, the issue of such shares shall be approved by the shareholders through postal ballot;

(c) The shares with differential rights shall not exceed twenty-six percent of the total post-issue paid up equity share capital including equity shares with differential rights issued at any point of time;

(d) The company having consistent track record of distributable profits for the last three years;

(e) The company has not defaulted in filing financial statements and annual returns for three financial years immediately preceding the financial year in which it is decided to issue such shares;

(f) The company has no subsisting default in the payment of a declared dividend to its shareholders or repayment of its matured deposits or redemption of its preference shares or debentures that have become due for redemption or payment of interest on such deposits or debentures or payment of dividend;

(g) The company has not defaulted in payment of the dividend on preference shares or repayment of any term loan from a public financial institution or State level financial institution or scheduled Bank that has become repayable or interest payable thereon or dues with respect to statutory payments relating to its employees to any authority or default in crediting the amount in Investor Education and Protection Fund to the Central Government;

(h) The company has not been penalized by Court or Tribunal during the last three years of any offence under the Reserve Bank of India Act, 1934, the Securities and Exchange Board of India Act, 1992, the Securities Contracts Regulation Act, 1956, the Foreign Exchange Management Act, 1999 or any other special Act, under which such companies being regulated by sectoral regulators.

Question 5 : May – 2019 – Paper

Following is the summarized Balance Sheet of Super Ltd. as on 31st March, 2018.

Liabilities	In Rs.
Share Capital	
Equity Shares of Rs.10 each fully paid up	17,00,000
Reserves & Surplus	
Revenue Reserve	23,50,000
Securities Premium	2,50,000
Profit & Loss Account	2,00,000
Infrastructure Development Reserve	1,50,000
Secured Loan	
9% Debentures	22,50,000
Unsecured Loan	8,50,000
Current Maturities of Long term borrowings	15,50,000
	93,00,000
Assets	
Fixed Assets	
Tangible Assets	58,50,000
Current Assets	
Current Assets	34,50,000
	93,00,000

Super Limited wants to buy back 35,000 equity shares of Rs.10 each fully paid up on 1st April, 2018 at Rs.30 per share.

Buy Back of shares is fully authorised by its articles and necessary resolutions have been passed by the company towards this. The payment for buy back of shares will be made by the company out of sufficient bank balance available as part of the Current Assets.

Comment with calculations, whet her the Buy Back of shares by the company is within the provisions of the Companies Act, 2013.

Solution :

Determination of maximum no. of shares that can be bought back as per the Companies Act, 2013

1. Shares Outstanding Test

Particulars	(Shares)
Number of shares outstanding	1,70,000
25% of the shares outstanding	42,500

2. Resources Test: Maximum permitted limit 25% of Equity paid up capital + Free Reserves

Particulars	
Paid up capital (Rs.)	17,00,000
Free reserves (Rs.) (23,50,000 + 2,50,000 + 2,00,000)	28,00,000
Shareholders' funds (Rs.)	45,00,000
25% of Shareholders fund (Rs.)	11,25,000
Buy back price per share	Rs. 30
Number of shares that can be bought back (shares)	37,500
Actual Number of shares proposed for buy back	35,000

3. Debt Equity Ratio Test: Loans cannot be in excess of twice the Equity Shareholder's Funds post Buy Back

	Particulars	Rs.
(a)	Loan funds (Rs.) (22,50,000+8,50,000+15,50,000)	46,50,000
(b)	Minimum equity to be maintained after buy back in the ratio of 2:1 (Rs.) (a/2)	23,25,000
(c)	Present equity/shareholders fund (Rs.)	45,00,000
(d)	Future equity/shareholders fund (Rs.) (see W.N.) (45,00,000 – 5,43,750)	39,56,250*
(e)	Maximum permitted buy back of Equity (Rs.) [(d) – (b)]	16,31,250
(f)	Maximum number of shares that can be bought back @ Rs. 30 per share	54,375 shares
(g)	Actual Buy Back Proposed	35,000 Shares

Summary statement determining the maximum number of shares to be bought back

Particulars	Number of shares
Shares Outstanding Test	42,500
Resources Test	37,500
Debt Equity Ratio Test	54,375
Maximum number of shares that can be bought back [least of the above]	37,500

Company qualifies all tests for buy-back of shares and it can buy back maximum 37,500 shares on 1st April, 2018.

However, company wants to buy-back only 35,000 equity shares @ Rs. 30. Therefore, buy-back of 35,000 shares, as desired by the company is within the provisions of the Companies Act, 2013.

Working Note :

Amount transferred to CRR and maximum equity to be bought back will be calculated by simultaneous equation method.

Suppose amount transferred to CRR account is 'x' and maximum permitted buy-back of equity is 'y'.

Then

(45,00,000 – x) – 23,25,000 = y (1)

$(\frac{y}{30} \times 10) = x$ Or 3x = y (2)

by solving the above equation, we get

x = Rs. 5,43,750

y = Rs. 16,31,250

Question 6 : Nov – 2019 – RTP

Umesh Ltd. resolves to buy back 4 lakhs of its fully paid equity shares of Rs.10 each at Rs.22 per share. This buyback is in compliance with the provisions of the Companies Act and does not exceed 25% of Company's paid up capital in the financial year. For the purpose, it issues 1 lakh 11 % preference shares of Rs.10 each at par, the entire amount being payable with applications. The company uses Rs.16 lakhs of its balance in Securities Premium Account apart from its adequate balance in General Reserve to fulfill the legal requirements regarding buy-back. Give necessary journal entries to record the above transactions.

Solution :

Journal Entries in the books of Umesh Ltd.

	Particulars		**Dr. Rs.**	**Cr. Rs.**
1	Bank A/c	Dr.	10,00,000	
	To 11% Preference share application & allotment A/c			10,00,000
	(Being receipt of application money on preference shares)			
2	11% Preference share application & allotment A/c	Dr.	10,00,000	
	To 11% Preference share capital A/c			10,00,000
	(Being allotment of 1 lakh preference shares)			
3	General reserve A/c	Dr.	30,00,000	
	To Capital redemption reserve A/c			30,00,000
	(Being creation of capital redemption reserve for buy back of shares)			
4	Equity share capital A/c	Dr.	40,00,000	
	Premium payable on buyback A/c	Dr.	48,00,000	
	To Equity shareholders/Equity shares buy back A/c			88,00,000
	(Amount payable to equity shareholder on buy back)			
5	Equity shareholders/ Equity shares buy back A/c	Dr.	88,00,000	
	To Bank A/c			88,00,000

	(Being payment made for buy back of shares)		
6	Securities Premium A/c Dr. General reserve A/c Dr. To Premium payable on buyback A/c (Being premium on buyback charged from securities premium and general reserve)	16,00,000 32,00,000	 48,00,000

Working Notes :

1. Calculation of amount used from General Reserve Account

		Rs.
Amount paid for buy back of shares (4,00,000 shares x Rs. 22)		88,00,000
Less: Proceeds from issue of Preference Shares (1,00,000 shares x Rs.10)		(10,00,000)
Less: Utilization of Securities Premium Account		(16,00,000)
Balance used from General Reserve Account		62,00,000
* Used under Section 68 for buy back	32,00,000	
Used under Section 69 for transfer to CRR (W.N 2)	30,00,000	
	62,00,000	

2. Amount to be transferred to Capital Redemption Reserve account

	Rs.
Nominal value of shares bought back (4,00,000 shares x Rs.10)	40,00,000
Less: Nominal value of Preference Shares issued for such buy back (1,00,000 shares x Rs.10)	(10,00,000)
Amount transferred to Capital Redemption Reserve Account	30,00,000

Question 7 : Nov – 2019 – RTP

What is meant by "equity shares with differential rights". Can preference shares be also issued with differential rights?

Solution :

Equity shares with Differential Rights means the share with dissimilar rights as to dividend, voting or otherwise. Preference shares cannot be issued with differential rights. It is only the equity shares, which are issued.

Question 8 : Nov – 2019 – RTP

L, M, N and O hold Equity capital in the proportion of 30:30:20:20 in AB Ltd. X, Y, Z and K hold preference share capital in the proportion of 40:30:20:10.

You are required to identify the voting rights of shareholders in case of resolution of winding up of the company if the paid-up capital of the company is Rs.80 Lakh and Preference share capital is Rs.40 Lakh.

Solution :

L, M, N and O hold Equity capital in the proportion of 30:30:20:20 and X, Y, Z and K hold preference share capital in the proportion of 40:30:20:10. As the paid-up equity share capital of the company is Rs. 80 Lakhs and Preference share capital is Rs. 40 Lakh (2:1), then relative weights in the voting right of equity shareholders and preference shareholders will be 2/3 and 1/3. The respective voting right of various shareholders will be

L = 2/3 X 30/100 = 3/15
M = 2/3 X 30/100 = 3/15
N = 2/3 X 20/100 = 2/15
O = 2/3 X 20/100 = 2/15
X = 1/3 X 40/100 = 2/15
Y = 1/3 X 30/100 = 1/10
Z = 1/3 X 20/100 = 1/15
K = 1/3 X 10/100 = 1/30

Question 9 : Nov – 2019 – Paper

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	10,00,000	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	5,50,000	43,50,000
Non-Current Liabilities		
12% Debenture		12,50,000
Current Liabilities and Provisions		5,50,000
Total		**1,21,50,000**
Assets		
Fixed Assets		
Tangible Assets		1,00,75,000
Current Assets		
Investment	3,00,000	
Inventory	2,00,000	
Cash and Bank	15,75,000	20,75,000
Total		**1,21,50,000**

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			2,50,000
	(Being 10% preference share issued to finance buy back)			
3	Bank A/c	Dr.	1,50,000	
	To Investment A/c			1,00,000
	To Profit on sale of investment			50,000
	(Being investment sold on profit)			
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 Rs.36)			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 buy back 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 To Bonus shares A/c (W.N.1) (Being the utilization of capital redemption reserve to issue 37,500 bonus shares)	Dr.	7,50,000	7,50,000
8	Bonus shares A/c To Equity share capital A/c (Being issue of 3 bonus equity share for every 15equity shares held)	Dr.	7,50,000	7,50,000

*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	Notes	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**

Note 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)		12,50,000	57,50,000
2	Reserves and Surplus			
	Capital Reserve		1,00,000	
	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	(2,60,000)	Nil	
	Capital Redemption Reserve			
	Transfer due to buy-back of shares from P&L	10,00,000		
	Less: Utilisation for issue of bonus shares	(7,50,000)	2,50,000	
	Profit & Loss A/c	20,00,000		
	Add: Profit on sale of investment	50,000		
	Less: Transfer to CRR	(4,40,000)	16,10,000	
	Dividend equalization reserve	(5,50,000)	5,50,000	27,10,000
3	Long-term borrowings - 12% Debentures	12,50,000		
	- 14% Debentures	3,00,000		15,50,000

Working Notes:

1. Amount of bonus shares = [(2,50,000 -25%)3/15] x 20 = 37,500 x 20=7,50,000
2. 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	1,50,000
	23,35,000
Less: Payment for buy back of shares	(22,50,000)
	85,000

Question 10 : May – 2020 – RTP

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

Equity & Liabilities	Rs. Lakhs	Assets	Rs. Lakhs
Share Capital:		Fixed Assets	14,000
Equity shares of Rs.10 each Fully Paid Up	8,000	Investments	2,350
10% Redeemable Pref. Shares of Rs.10 each Fully Paid Up	2,500	Cash at Bank	2,300
Reserves & Surplus		Other Current Assets	8,250
Capital Redemption Reserve	1,000		
Securities Premium	800		
General Reserve	6,000		
Profit & Loss Account	300		
Secured Loans:			
9% Debentures	5,000		
Current Liabilities:			
Trade payables	2,300		
Sundry Provisions	1,000		
	26,900		**26,900**

On 1st April, 2019 the Company redeemed all its Preference Shares at a Premium of 10% and bought back 10% of its Equity Shares at Rs.20 per Share. In order to make cash available, the Company sold all the Investments for Rs.2,500 lakhs.

You are required to pass journal entries for the above and prepare the Company's Balance sheet immediately after buyback of equity shares and redemption of preference shares.

Solution :

(i) Journal Entries in the books of C Ltd. (Rs. in lakhs)

	Particulars		Dr. Rs.	Cr. Rs.
1	Bank A/c	Dr.	2,500	
	To Investments A/c			2,350
	To Profit and Loss A/c			150
	(Being investment sold on profit for the purpose of buy-back)			
2	10% Redeemable Preference Share Capital A/c	Dr.	2,500	
	Premium on Redemption of Preference Shares A/c	Dr.	250	
	To Preference Shareholders A/c			2,750
	(Being redemption of preference share capital at premium of 10%)			
3	Securities Premium A/c	Dr.	250	

	To Premium on Redemption of Preference Shares A/c (Being premium on redemption of preference shares adjusted through securities premium)		250
4	Equity Share Capital A/c Dr. Premium on buyback Dr. To Equity buy-back A/c (Being Equity Share bought back, Share Capital cancelled, and Premium on Buyback accounted for)	800 800	 1,600
5	Securities Premium A/c (800-250) Dr. General Reserve A/c Dr. To Premium on Buyback A/c (Being premium on buyback provided first out of securities premium and the balance out of general reserves.)	550 250	 800
6	Preference Shareholders A/c Dr. Equity buy-back A/c Dr. To Bank A/c (Being payment made to preference shareholders and equity shareholders)	2,750 1,600	 4,350
7	General Reserve Account Dr. To Capital Redemption Reserve Account (Being amount transferred to capital redemption reserve account towards face value of preference shares redeemed and equity shares bought back)	3,300	 3,300

(ii) Balance Sheet of C Ltd. (after Redemption and Buyback) (Rs. Lakhs)

		Particulars	Notes	Rs.
I.		**EQUITY AND LIABILITIES**		
1		**Shareholders' Funds:**		
	a	Share Capital	1	7,200
	b	Reserves and Surplus	2	7,200
2		**Non-Current Liabilities:**		
	a	Long Term Borrowings	3	5,000
3		**Current Liabilities:**		
	a	Trade payables		2,300
	b	Short Term Provisions		1,00

		Total		**22,700**
II.		ASSETS		
1		**Non-Current Assets**		
		PPE		14,000
2		**Current Assets:**		
	a	Cash and Cash equivalents (W N)		450
	b	Other Current Assets		8,250
		Total		**22,700**

Notes to Accounts

				Rs.
1	**Share Capital**			
	720 lakh Equity Shares of Rs. 10 each Fully Paid up (80 lakh Equity Shares bought back)			7,200
2	**Reserves and Surplus**			
	General Reserve	6,000		
	Less: Adjustment for premium paid on buy back	(250)		
	Less: Transfer to CRR	(3,300)	2,450	
	Capital Redemption Reserve	1,000		
	Add: Transfer due to buy-back of shares from Gen. res.	3,300	4,300	
	Securities premium	800		
	Less: Adjustment for premium paid on redemption of preference shares	(250)		
	Less: Adjustment for premium paid on buy back	(550)		
	Profit & Loss A/c	300		
	Add: Profit on sale of investment	150	450	7,200
3	**Long-term borrowings**			
	Secured			
	9 % Debentures			5,000

Working Notes :

Bank Account

Receipts	**Amount (Rs. Lakhs)**	**Payments**	**Amount (Rs. Lakhs)**
To balance b/d	2,300	By Preference Shareholders A/c	2,750

To Investment A/c (sale Proceeds)	2,500	By Equity Shareholders A/c	1,600
		By Balance c/d (Balancing figure)	450
	4,800		**4,800**

Question 11 : May – 2020 – RTP

Can preference shares be also issued with differential rights? Explain in brief.

Solution :

No. Preference shares cannot be issued with differential rights. It is only the equity shares, which are issued with differential rights.

Question 12 : May – 2020 – RTP

Explain the conditions under Companies (Share Capital and Debentures) Rules, 2014, to deal with equity shares with differential rights.

Solution :

In exercise of the power conferred under Section 43(a)(ii), the central government announced Rule 4 under Companies (Share Capital and Debentures) Rules, 2014, to deal with equity shares with differential rights.

The rules lay down the following conditions to be compulsorily complied with:

(a) The articles of association of the company authorizes the issue of shares with differential rights;

(b) The issue of shares is authorized by an ordinary resolution passed at a general meeting of the shareholders: Provided that where the equity shares of a company are listed on a recognized stock exchange, the issue of such shares shall be approved by the shareholders through postal ballot;

(c) The shares with differential rights shall not exceed twenty-six percent of the total post-issue paid up equity share capital including equity shares with differential rights issued at any point of time;

(d) The company having consistent track record of distributable profits for the last three years;

(e) The company has not defaulted in filing financial statements and annual returns for three financial years immediately preceding the financial year in which it is decided to issue such shares;

(f) The company has no subsisting default in the payment of a declared dividend to its shareholders or repayment of its matured deposits or redemption of its preference shares or debentures that have become due for redemption or payment of interest on such deposits or debentures or payment of dividend;

(g) The company has not defaulted in payment of the dividend on preference shares or repayment of any term loan from a public financial institution or State level financial institution or scheduled Bank that has become repayable or interest payable thereon or dues with respect to statutory payments relating to its employees to any authority or

default in crediting the amount in Investor Education and Protection Fund to the Central Government;

(h) The company has not been penalized by Court or Tribunal during the last three years of any offence under the Reserve Bank of India Act, 1934, the Securities and Exchange Board of India Act, 1992, the Securities Contracts Regulation Act, 1956, the Foreign Exchange Management Act, 1999 or any other special Act, under which such companies being regulated by sectoral regulators.

Question 13 : Nov – 2020 – RTP

Pratham Ltd. (a non-listed company) has the following Capital structure as on 31st March, 2020:

Particulars	Rs.	Rs.
Equity Share Capital (shares of Rs.10 each fully paid)		30,00,000
Reserves & Surplus		
General Reserve	32,50,000	
Security Premium Account	6,00,000	
Profit & Loss Account	4,30,000	
Revaluation Reserve	6,20,000	49,00,000
Loan Funds		42,00,000

You are required to compute by Debt Equity Ratio Test, the maximum number of shares that can be bought back in the light of above information, when the offer price for buy back is Rs.30 per share.

Solution :

Debt Equity Ratio Test

	Particulars	Rs.
(a)	Loan funds	42,00,000
(b)	Minimum equity to be maintained after buy back in the ratio of 2:1 (Rs. in crores)	21,00,000
(c)	Present equity shareholders fund (Rs. in crores)	72,80,000
(d)	Future equity shareholder fund (Rs. in crores) (See Note 2)	59,85,000 (72,80,000-12,95,000)
(e)	Maximum permitted buy back of Equity (Rs. in crores) [(d) – (b)] (See Note 2)	38,85,000 (by simultaneous equation)
(f)	Maximum number of shares that can be bought back @ Rs. 30 per share (shares in crores) (See Note 2)	1,29,500 (by simultaneous equation)

Working Notes :

1. Shareholders' funds'

Particulars	Number of shares
Paid up capital	30,00,000
Free reserves (32,50,000 +6,00,000+4,30,000)	42,80,000
	72,80,000

2. As per section 68 of the Companies Act, 2013, amount transferred to CRR and maximum equity to be bought back will be calculated by simultaneous equation method.
Suppose amount equivalent to nominal value of bought back shares transferred to CRR account is 'x' and maximum permitted buy-back of equity is 'y'.
Equation 1 : (Present equity – Nominal value of buy-back transfer to CRR) – Minimum equity to be maintained = Maximum permissible buy-back of equity
(72,80,000 – x) – 21,00,000 = y (1)
Since 51,80,000 – x = y

Equation 2 : $\left(\frac{\text{Maximum buy - back}}{\text{Offer price for buy - back}} \times \text{Nominal Value}\right)$
= Nominal value of the shares bought –back to be transferred to CRR
= $\left(\frac{y}{30} \times 10\right)$ = x
3x = y (2)
x = Rs. 12,95,000 crores and y = Rs. 38,85,000 crores

Question 14 : Nov – 2020 – RTP / May – 2021 – RTP

What do you mean by equity shares with differential rights? Explain in brief. Can preference shares be also issued with differential rights?

Solution :

Equity shares with Differential Rights means the share with dissimilar rights as to dividend, voting or otherwise. No; the preference shares cannot be issued with differential rights.

Question 15 : Nov – 2020 – RTP / Nov – 2020 – Paper / Jan – 2021 – Paper / May – 2021 – RTP

E, F, G and H hold Equity Capital in Alpha Co. in the proportion of 30:30:20:20. S, T,U and V hold preference share capital in the proportion of 40:30:10:20. If the paid up capital of the company is Rs.120 Lakh and Preference share capital is Rs. 60 Lakh, You are required to calculate their voting rights in case of resolution of winding up of the company.

Solution :

E, F, G and H hold Equity capital is held by in the proportion of 30:30:20:20 and S,T,U and V hold preference share capital in the proportion of 40:30:10:20. As the paid up equity share capital of the company is Rs. 120 Lakhs and Preference share capital is Rs. 60 Lakhs (ratio of 2:1), then relative weights in the voting right of equity shareholders and preference shareholders will be 2/3 and 1/3. The respective voting right of various shareholders will be:

E	=	2/3 X 30/100 =	3/15
F	=	2/3 X 30/100 =	3/15
G	=	2/3 X 20/100 =	2/15
H	=	2/3 X 20/100 =	2/15
S	=	1/3 X 40/100 =	2/15
T	=	1/3 X 30/100 =	1/10

U = 1/3 X 10/100 = 1/30
V = 1/3 X 20/100 = 1/15

Question 16 : Jan – 2021 – Paper

The Directors of Umang Ltd. passed a resolution to buyback 5,00,000 numbers of its fully paid equity shares of Rs.10 each at Rs.15 per share. This buyback in compliance with the provisions of the Companies Act, 2013

For this purpose, the company.

(i) Sold its investments of Rs.30,00,000 for Rs.25,00,000.

(ii) Issued 20,000, 12% preference shares of Rs.100 each at par, the entire amount being payable with application.

(iii) Used Rs.15,00,000 of its Securities Premium Account apart from its adequate balance in General Reserve to fulfill the legal requirements regarding buy-back.

(iv) The company has necessary cash balance for the payment to shareholders.

You are required to pass necessary Journal entries (including narration) regarding buy-back of shares in the books of Umang Ltd.

Solution :

Journal Entries in the books of Umang Ltd.

			Dr. Rs.	Cr. Rs.
1	Bank A/c	Dr.	25,00,000	
	Profit and Loss A/c	Dr.	5,00,000	
	To Investment A/c			30,00,000
	(Being investment sold for the purpose of buy-back of Equity Shares)			
2	Bank A/c	Dr.	20,00,000	
	To 12% Pref. Share capital A/c			20,00,000
	(Being 12% Pref. Shares issued for Rs. 20,00,000)			
3	Equity share capital A/c	Dr.	50,00,000	
	Premium payable on buy-back	Dr.	25,00,000	
	To Equity shares buy-back A/c/ Equity shareholders A/c			75,00,000
	(Being the amount due on buy-back of equity shares)			
4	Equity shares buy-back A/c/ Equity shareholders A/c	Dr.	75,00,000	
	To Bank A/c			75,00,000
	(Being payment made for buy-back of equity shares)			
5	Securities Premium A/c	Dr.	15,00,000	
	General Reserve A/c	Dr.	10,00,000	
	To Premium payable on buy-back			25,00,000

	(Being premium payable on buy-back charged from Securities premium)		
6	General Reserve A/c Dr.	30,00,000	
	To Capital Redemption Reserve A/c		30,00,000
	(Being creation of capital redemption reserve to the extent of the equity shares bought back after deducting fresh pref. shares issued)		

Question 17 : May – 2021 – RTP

M/s. Vriddhi Infra Ltd. (a non-listed company) provide the following information as on 31.3.2020:

	Rs.
Land and Building	21,50,000
Plant & Machinery	15,00,000
Non- current Investment	2,00,000
Trade Receivables	5,50,000
Inventories	1,80,000
Cash and Cash Equivalents	40,000
Share capital : 1,00,000 Equity Shares of Rs. 10 each fully paid up	10,00,000
Securities Premium	3,00,000
General Reserve	2,50,000
Profit & Loss Account (Surplus)	1,50,000
10% Debentures (Secured by floating charge on all assets)	20,00,000
Unsecured Loans	8,00,000
Tarde Payables	1,20,000

On 21st April, 2020 the Company announced the buy back of 15,000 of its equity shares @ Rs. 15 per share. For this purpose, it sold all its investment for Rs. 2.50 lakhs.

On 25th April, 2020, the company achieved the target of buy back. On 1st May, 2020 the company issued one fully paid up share of Rs. 10 each by way of bonus for every eight equity shares held by the equity shareholders.

You are required to pass necessary Journal Entries for the above transactions.

Solution :

In the books of Vriddhi Infra Ltd.

Journal Entries

Date 2020	Particulars	Dr. Rs.	Cr. Rs.
21-Apr	Bank A/c Dr.	2,50,000	
	To Investment A/c		2,00,000
	To Profit on sale of investment		50,000
	(Being investment sold on profit)		

Date	Particulars		Dr. (Rs.)	Cr. (Rs.)
25-Apr	Equity share capital A/c Securities premium A/c To Equity shares buy back A/c (Being the amount due to equity shareholders on buy back)	Dr. Dr.	1,50,000 75,000	 2,25,000
	Equity shares buy back A/c To Bank A/c (Being the payment made on account of buy back of 15,000 Equity Shares)	Dr.	2,25,000	 2,25,000
	General Reserve A/c OR P & L A/c To Capital redemption reserve A/c (Being amount equal to nominal value of buy back shares transferred from free reserves capital redemption reserve account as per the law)	Dr.	1,50,000	 1,50,000
1-May	Capital redemption reserve A/c To Bonus shares A/c (W.N.1) (Being the utilization of capital redemption reserve to issue bonus shares)	Dr.	1,06,250	 1,06,250
	Bonus shares A/c To Equity share capital A/c (Being issue of one bonus equity share for every ten equity shares held)	Dr.	1,06,250	 1,06,250

Working Note:

Amount of bonus shares $= \left[(1{,}00{,}000 - 15{,}000) \times \frac{1}{8}\right] \times 10$

= Rs. 1,06,250

Question 18 : July – 2021 – Paper

A company provides the following 2 possible Capital Structure as on 31st March, 2021 :

Particulars	**Situation 1**	**Situation 2**
Equity Share Capital	30,00,000	30,00,000
(Share of Rs.10 each, fully paid up)		
Reserves & Surplus		
General Reserve	12,00,000	12,00,000
Securities Premium	6,00,000	6,00,000
Profit & Loss	2,10,000	2,10,000
Statutory Reserve	4,20,000	4,20,000
Loan Funds	25,00,000	1,20,00,000

The company is planning to offer buy back of Equity Share at a price of Rs.30 per equity share.

You are required to calculate maximum permissible number of equity shares that can be bought back in the both situations as per Companies Act, 2013 and are also required to pass necessary Journal Entries in the situation where the buy back is possible.

Solution :

Statement determining the maximum number of shares to be bought back

Number of shares (in crores)

Particulars	When loan fund is	
	Rs. 25,00,000	**Rs. 1,20,00,000**
Shares Outstanding Test (W.N.1)	75,000	75,000
Resources Test (W.N.2)	41,750	41,750
Debt Equity Ratio Test (W.N.3)	94,000	Nil
Maximum number of shares that can be bought back [least of the above]	41,750	Nil

Journal Entries for the Buy-Back (applicable only when loan fund is Rs. 25,00,000)

	Particulars		**Debit**	**Credit**
				Rs.
(a)	Equity shares buy-back account	Dr.	12,52,500	
	To Bank account			12,52,500
	(Being payment for buy-back of 41,750 equity shares of Rs. 10 each @ Rs. 30 per share)			
(b)	Equity share capital account	Dr.	4,17,500	
	Premium Payable on buy-back account	Dr.	8,35,000	
	To Equity shares buy-back account			12,52,500
	(Being cancellation of shares bought back)			
	Securities Premium account	Dr.	6,00,000	
	General Reserve / Profit & Loss A/c	Dr.	2,35,000	
	To Premium Payable on buy-back account			8,35,000
	(Being Premium Payable on buy-back account charged to securities premium and general reserve/Profit & Loss A/c)			
(c)	General Reserve*	Dr.	4,17,500	
	To Capital redemption reserve account			4,17,500
	(Being transfer of free reserves to capital redemption reserve to the extent of nominal value of share capital bought back out of redeemed through free reserves)			

*Profit and Loss account balance amounting Rs. 2,10,000 may also be used and General Reserve may be debited for the balance amount.

Working Notes:

1. Shares Outstanding Test

Particulars	(Shares in crores)
Number of shares outstanding	3,00,000
25% of the shares outstanding	75,000

2. Resources Test

Particulars	
Paid up capital (Rs.)	30,00,000
Free reserves (Rs.) (12,00,000 + 6,00,000 + 2,10,000)	20,10,000
Shareholders' funds (Rs.)	50,10,000
25% of Shareholders fund (Rs.)	Rs. 12,52,500
Buy-back price per share	Rs. 30
Number of shares that can be bought back	41,750 shares

3. Debt Equity Ratio Test: Loans cannot be in excess of twice the Equity Funds post Buy-Back

	Particulars	When loan fund is	
(a)	Loan funds (Rs.)	Rs. 25,00,000	Rs. 1,20,00,000
(b)	Minimum equity to be maintained after buy-back in the ratio of 2:1 (Rs.) (a/2)	12,50,000	60,00,000
(c)	Present equity shareholders fund (Rs.)	50,10,000	50,10,000

Amount transferred to CRR and maximum equity to be bought back will be calculated by simultaneous equation method

Suppose amount transferred to CRR account is 'x' and maximum permitted buy-back of equity is 'y' Then

Equation 1: (Present Equity- Transfer to CRR)- Minimum Equity to be maintained = Maximum Permitted Buy-Back

= (50,10,000 – x) – 12,50,000 = y

= 37,60,000 – x =y (1)

Equation 2: Maximum Permitted Buy-Back *X* Nominal Value Per Share/Offer Price Per Share

y/30 x 10 = x

or

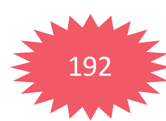
3x = y (2)

by solving the above two equations we get

x = Rs. 9,40,000 and

y = Rs. 28,20,000

In situation 2, first equation will be negative. Buy back not possible in this situation.



Question 19 : July – 2021 – Paper

(i) Explain the meaning of Equity Shares with Differential Rights. Can Preference Shares be also issued with differential rights?

(ii) In Jugnu Limited A, B, C and D hold equity share capital in the proportion of 30 : 30 : 30 : 10 and M, N, O and P hold preference share capital in proportion of 40 : 20 : 30 : 10.

You are required to calculate their voting rights in case of resolution of winding up of the company, if the paid up Equity Share Capital of the company is Rs.100 Lakhs and Preference Share Capital is Rs.50 Lakhs.

Solution :

(i) As per the Companies Act 2013, companies can issue equity shares with differential rights subject to the fulfilment of certain conditions. Companies (Share Capital and Debentures) Rules, 2014 deal with equity shares with differential rights. Differentiation can be done by giving a superior dividend / Superior voting right / diluted voting right to a class of equity shareholders.

Preference shares are not issued with differential rights. It is only the equity shares, which are issued.

(ii) In the given case, the relative weight in the voting right of equity shareholders and preference shareholders will be 2/3 and 1/3. The respective voting right of various shareholders will be

				Relative weights	**Voting Power**
A	=	2/3 X 30/100	=	2/10	20%
B	=	2/3 X 30/100	=	2/10	20%
C	=	2/3 X 30/100	=	2/10	20%
D	=	2/3 X 10/100	=	1/15	6.67%
M	=	1/3 X 40/100	=	2/15	13.33%
N	=	1/3 X 20/100	=	1/15	6.67%
O	=	1/3 X 30/100	=	1/10	10%
P	=	1/3 X 10/100	=	1/30	3.33%

Question 20 : Nov – 2021 – RTP

Rohan Ltd. furnishes the following information as at 31-03-2021.

	(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	10,00,000	60,00,000
Reserves & Surplus:		
Capital Reserve	1,00,000	
Security Premium	12,00,000	
Revenue Reserve	5,00,000	
Profit and Loss	25,50,000	43,50,000

12% Debentures		12,50,000
Current Liabilities and Provisions		5,50,000
Property, Plant and Equipment		1,00,75,000
Current Assets:		
Investment	3,00,000	
Inventory	2,00,000	
Cash and Bank	15,75,000	20,75,000

The shareholders adopted the following resolution on 31st March, 2021:

(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 3,000, 14% debentures of Rs. 100 each at a premium of 20%.

   (b) Issues 2,500, 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.Rs. 2,00,000 in Revenue Reserve.

(5) Later, the company issue three fully paid up equity shares of Rs. 20 each by way of bonus for every 15 equity shares held by the equity shareholders.

You are required to pass the necessary journal entries to record the above transactions.

Solution :

In the books of Rohan Limited
Journal Entries

	Particulars		Rs.	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			2,50,000
	(Being 10% preference share issued to finance buy back)			
3	Bank A/c	Dr.	1,50,000	
	To Investment A/c			1,00,000
	To Profit on sale of investment			50,000
	(Being investment sold on profit)			
4	Equity share capital A/c (62,500 x Rs.20)	Dr.	12,50,000	
	Premium on buyback or Securities premium A/c (62,500 x Rs.16)	Dr.	10,00,000	
	To Equity shares buy back A/c (62,500 x Rs.36)			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 buy back 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			7,50,000
	(Being the utilization of capital redemption reserve to issue 37,500 bonus shares)			
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 15equity shares held)			

Question 21 : Nov – 2021 – RTP

"The rights of a shares of a particular class, once issued, can be varied or altered." Comment on this statement in line with the provisions of the Companies Act.

Solution :

The rights of shares of a particular class, once issued, can be varied or altered:

(a) If provision with respect to such variation is contained in the memorandum or articles of the company; or

(b) In the absence of any such provision in the memorandum or articles, if such variation is not prohibited by the terms of issue of the shares of that class.

However, it would require consent in writing of the holders of not less than three-fourths of the issued shares of that class or by means of a special resolution passed at a separate meeting of the holders of the issued shares of that class. Hence, if equity shareholders series A require a change in their right, of a particular nature, either a special resolution of a specially convened meeting of this class of shareholders will suffice, or otherwise more than 75% shareholders can give their consent in writing. It must be understood that a company having equity shares with voting rights cannot convert them into equity shares with differential voting rights, or vice-versa. However, the variation in their rights should not affect the rights of any other class, say Equity shares 'B' class or Preference shares. In such situation, if variation by one class of shareholders affects the rights of any other class of shareholders, the consent of three-fourths of such other class of shareholders shall also be obtained and the provisions of the Companies Act section shall apply to such variation.

Question 22 : Dec – 2021 – Paper

(i) Can preference shares be also issued with differential rights? Explain in brief?

(ii) Explain the conditions under Companies (share Capital and Debentures) Rules 2014, to deal with equity shares with differential rights.

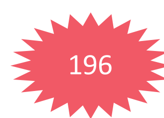
Solution :

(i) No; the preference shares cannot be issued with differential rights. It is only the equity shares, which are issued. Equity shares with Differential Rights means the share with dissimilar rights as to dividend, voting or otherwise.

(ii) As per Share Capital and Debentures Rules, 2014, for equity shares with differential rights, following conditions to be compulsorily complied with:

- The articles of association of the company authorizes the issue of shares with differential rights;
- The issue of shares is authorized by an ordinary resolution passed at a general meeting of the shareholders: Provided that where the equity shares of a company are listed on a recognized stock exchange, the issue of such shares shall be approved by the shareholders through postal ballot;
- The voting power in respect of shares with differential rights shall not exceed seventy four percent of the total voting power including voting power in respect of equity shares with differential rights issued at any point of time;
- The company has not defaulted in filing financial statements and annual returns for three financial years immediately preceding the financial year in which it is decided to issue such shares;
- The company has no subsisting default in the payment of a declared dividend to its shareholders or repayment of its matured deposits or redemption of its preference shares or debentures that have become due for redemption or payment of interest on such deposits or debentures or payment of dividend;
- The company has not defaulted in payment of the dividend on preference shares or repayment of any term loan from a public financial institution or State level financial institution or scheduled Bank that has become repayable or interest payable thereon or dues with respect to statutory payments relating to its employees to any authority or default in crediting the amount in Investor Education and Protection Fund to the Central Government;

  Provided that a company may issue equity shares with differential rights upon expiry of five years from the end of financial year in which such default was made good.
- The company has not been penalized by Court or Tribunal during the last three years of any offence under the Reserve Bank of India Act, 1934, the Securities and Exchange Board of India Act, 1992, the Securities Contracts Regulation Act, 1956, the Foreign Exchange Management Act, 1999 or any other special Act, under which such companies being regulated by sectoral regulators.



Question 23 : Dec – 2021 – Paper

Mohan Ltd. furnishes the following summarised Balance Sheet as on 31st March, 2021.

(Rs. In Lakhs)

	Amount
Equity and Liabilities :	
Shareholder's fund	
Share Capital	
Equity shares of Rs.10 each fully paid	780
6% Redeemable Preference shares of Rs.50 each fully paid up	240
Reserves and Surplus	
Capital Reserves	58
General Reserve	625
Security Premium	52
Profit & Loss	148
Revaluation Reserve	34
Infrastructure Development Reserve	16
Non-current liabilities	
7% Debentures	268
Unsecured Loans	36
Current Liabilities	395
	2652
Assets :	
Non-current Assets	
Plant and Equipment less depreciation	725
Investment at cost	720
Current Assets	1207
	2652

Other information :

(1) The company redeemed preference shares at a premium of 10% on 1st April, 2021.

(2) It also offered buy back the maximum permissible number of equity shares of Rs.10 each at Rs.30 per share on 2nd April, 2021.

(3) The payment for the above was made out of available bank balance, which appeared as a part of the current assets.

(4) The company had investment in own debentures costing Rs.60 lakhs (face value Rs.75 lakhs). The debentures were cancelled on 2nd April, 2021.

(5) On 4th April, 2021 company issued one full paid up equity share of Rs.10 each by way of bonus for every five shares held by the shareholders.

You are required to:

(a) Calculate maximum possible number of equity shares that can be bought back as per Companies Act, 2013 and

(b) Record the Journal Entries for the above mentioned information.

Solution :

(i) Statement determining the maximum number of shares to be bought back

Number of shares (in lakhs)

Particulars	When loan fund is Rs. 304 lakhs
Shares Outstanding Test (W.N.1)	19.5
Resources Test (W.N.2)	11.175
Debt Equity Ratio Test (W.N.3)	29.725
Maximum number of shares that can be bought back [least of the above]	11.175

Thus, the company can buy 11,17,500 Equity shares at Rs. 30 each.

Working Notes:

1. Shares Outstanding Test

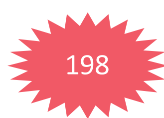
Particulars	(Shares in lakh)
Number of shares outstanding	78
25% of the shares outstanding	19.5

2. Resources Test

Particulars	
Paid up capital (Rs. in lakh)	780
Free reserves (Rs. in lakh) (625+52+148-24-240*)	561
Shareholders' funds (Rs. in lakh)	1341
25% of Shareholders fund (Rs. in lakh)	335.25
Buy-back price per share	30
Number of shares that can be bought back	11.175
Amount transferred to CRR is excluded from free reserves. Premium on redemption also reduced.	

3. Debt Equity Ratio Test: Loans cannot be in excess of twice the Equity Funds post Buy-Back

	Particulars	Rs. In lakh
(a)	Loan funds (Rs.)	304
(b)	Minimum equity to be maintained after buy-back in the ratio of 2:1 (Rs.) (a/2)	152
(c)	Present equity shareholders fund (Rs.)	1341
(d)	Future equity shareholders fund (Rs.) (see W.N.4)	1043.75 (1341-297.25)
(e)	Maximum permitted buy-back of Equity (Rs.) [(d) – (b)]	891.75



(f)	Maximum number of shares that can be bought back @ Rs. 30 per share	29.725
	As per the provisions of the Companies Act, 2013, company	Qualifies

Alternatively, when current liabilities are considered as part of loan funds, in that case Debt Equity Ratio Test will be done as follows:

	Particulars	**Rs. In lakh**
(a)	Loan funds (Rs.)	699
(b)	Minimum equity to be maintained after buy-back in the ratio of 2:1 (Rs.) (a/2)	349.5
(c)	Present equity shareholders fund (Rs.)	1341
(d)	Future equity shareholders fund (Rs.) (see W.N.4)	1093.125 (1341-247.875)
(e)	Maximum permitted buy-back of Equity (Rs.) [(d) – (b)]	743.625
(f)	Maximum number of shares that can be bought back @ Rs. 30 per share	24.7875
	As per the provisions of the Companies Act, 2013, company	Qualifies

4. Amount transferred to CRR and maximum equity to be bought back will be calculated by simultaneous equation method

Suppose amount transferred to CRR account is 'x' and maximum permitted buy-back of equity is 'y' Then

Equation 1: (Present Equity- Transfer to CRR) - Minimum Equity to be maintained = Maximum Permitted Buy-Back

= (1341 – x) – 152 = y

= 1189 – x =y (1)

Equation 2: Maximum Permitted Buy-Back x Nominal Value Per Share/Offer Price Per Share

y/30 x 10 = x or 3x = y (2)

by solving the above two equations we get

x = Rs. 297.25 and y = Rs. 891.75

Alternatively, when current liabilities are considered as part of loan funds, in that case

Equation 1: (Present Equity- Transfer to CRR)- Minimum Equity to be maintained = Maximum Permitted Buy-Back

= (1341 – x) – 349.5 = y

= 991.5 – x =y (1)

Equation 2: Maximum Permitted Buy-Back *X* Nominal Value Per Share/Offer Price Per Share

y/30 x 10 = x or 3x = y (2)

by solving the above two equations we get x = 247.875 and y = 743.625

(ii) **Journal Entries for Buy Back** **(Rs. in lakhs)**

Date	Particulars		Debit	Credit
2021				
1st April	6% Redeemable preference share capital A/c	Dr.	240	
	Premium on redemption of preference shares A/c	Dr.	24	
	To Preference shareholders A/c			264
	(Being preference share capital transferred to shareholders account)			
	Preference shareholders A/c	Dr.	264	
	To Bank A/c			264
	(Being payment made to shareholders)			
	General Reserve or P&L A/c*	Dr.	24	
	To Premium on redemption of preference shares A/c			24
	(Being premium on redemption of preference shares adjusted through securities premium)			
2nd April	Equity shares buy-back A/c	Dr.	335.25	
	To Bank A/c			335.25
	(Being 11.175 lakhs equity shares of Rs. 10 each bought back @ Rs. 30 per share)			
	Equity share capital A/c	Dr.	111.75	
	Securities Premium A/c	Dr.	52	
	General Reserve or P&L A/c	Dr.	171.5	
	To Equity Shares buy-back A/c			335.25
	(Being cancellation of shares bought back)			
	General reserve A/c	Dr.	351.75	
	To Capital redemption reserve A/c			351.75
	(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 ie. 240+ 111.75 lakhs)			
2nd April	7% Debentures A/c	Dr.	75	
	To Investment (own debentures) A/c			60
	To Profit on cancellation of own debentures A/c			15

	(Being cancellation of own debentures costing Rs. 60 lakhs, face value being Rs. 75 lakhs and the balance being profit on cancellation of debentures)			
4th April	Capital Redemption Reserve To Bonus Shares A/c (Being issue of one bonus equity share for every five equity shares held)	Dr.	133.65	133.65
	Bonus shares A/c To Equity share capital A/c (Being bonus shares issued)	Dr.	133.65	133.65

Working Note: Bonus Share to be issued =66.825 (78 - 11.175) lakh shares divided by 5 = 13.365 lakh shares.

Note: *Securities premium has not been utilized for the purpose of premium payable on redemption of preference shares assuming that the company referred in the question is governed by Section 133 of the Companies Act, 2013 and complies with the Accounting Standards prescribed for them. Alternative entry considering otherwise is also possible by utilizing securities premium amount.

Question 24 : Dec – 2021 – Paper

P, Q, R and S hold equity capital in the proportion of 10:40:20:30, K, L, M and N hold preference share capital in the proportion of 20:10:40:30. If the paid up equity share capital of the company is Rs.60 lakhs and Preference Share Capital is Rs.30 lakhs, find their voting rights in case of resolution of winding up of the company.

Solution :

P, Q, R and S hold Equity capital is held by in the proportion of 10:40:20:30 and K, L, M and N hold preference share capital in the proportion of 20:10:40:30. As the paid up equity share capital of the company is Rs. 60 Lakhs and Preference share capital is Rs. 30 Lakh (2:1), then relative weights in the voting right of equity shareholders and preference shareholders will be 2/3 and 1/3.

The respective voting right of various shareholders will be

P = 2/3X10/100 = 1/15

Q = 2/3X40/100 = 4/15

R = 2/3X20/100 = 2/15

S = 2/3X30/100 = 3/15

K = 1/3X20/100 = 1/15

L = 1/3X10/100 = 1/30

M = 1/3X40/100 = 2/15

N = 1/3X30/100 = 1/10

Hence, their relative weights are 1/15 : 4/15 : 2/15 : 3/15: 1/15 : 1/30 : 2/15 : 1/10 or 2 : 8 : 4 : 6 : 2 : 1 : 4 : 3.

Their respectively voting power is P (6.67%), Q (26.67%), R (13.33%), S (20%), K (6.67%), L (3.33%), M (13.33%) and N (10%).

Question 25 : May – 2022 – RTP

Complicated Ltd. (an unlisted company) gives the following information as on 31.3.2021:

Particulars	Amount (Rs.)
Equity shares of Rs. 10 each, fully paid up	13,50,000
Share option outstanding Account	4,00,000
Revenue Reserve	15,00,000
Securities Premium	2,50,000
Profit & Loss Account	1,25,000
Capital Reserve	2,00,000
Unpaid dividends	1,00,000
12% Debentures (Secured)	18,75,000
Advance from related parties (Long term - Unsecured)	10,00,000
Current maturities of long term borrowings	16,50,000
Application money received for allotment due for refund	2,00,000
Property, plant and equipment	46,50,000
Current assets	40,00,000

The Company wants to buy back 25,000 equity shares of Rs. 10 each, on 1st April, 2021 at Rs. 15 per share. Buy back of shares is duly authorized by its Articles and necessary resolution has been passed by the Company for this. The buy-back of shares by the Company is also within the provisions of the Companies Act, 2013. The payment for buy back of shares was made by the Company out of sufficient bank balance available shown as part of Current Assets.

You are required to prepare the necessary journal entries towards buy back of shares and prepare the Balance Sheet of the company after buy back of shares.

Solution :

As per the information given in the question, buy-back of 25,000 shares @ Rs. 15, as desired by the company, is within the provisions of the Companies Act, 2013.

Journal Entries for buy-back of shares

			Debit (Rs.)	Credit (Rs.)
(a)	Equity shares buy-back account	Dr.	3,75,000	
	To Bank account			3,75,000
	Being buy back of 25,000 equity shares of Rs. 10 each @ Rs. 15 per share)			
(b)	Equity share capital account	Dr.	2,50,000	
	Premium payable on buyback account	Dr.	1,25,000	
	To Equity shares buy-back account			3,75,000
	Being cancellation of shares bought back)			
(c)	Securities premium account	Dr.	1,25,000	
	To Premium payable on buyback account			1,25,000

	Being Premium payable on buyback adjusted against securities premium account)		
(d)	Revenue reserve account Dr. To Capital redemption reserve account (Being transfer of free reserves to capital redemption reserve to the extent of nominal value of capital bought back through free reserves)	2,50,000	2,50,000

Balance Sheet of Complicated Ltd. as at 1st April, 2021

	Note No	Amount Rs.
EQUITY AND LIABILITIES		
1 Shareholders' funds		
(a) Share capital	1	11,00,000
(b) Reserves and Surplus	2	23,50,000
2 Non-current liabilities		
(a) Long-term borrowings	3	28,75,000
3 Current liabilities		
(a) Short-term borrowings	4	16,50,000
(b) Other current liabilities	5	3,00,000
Total		82,75,000
ASSETS		
1 Non-current assets		
(a) Property, Plant and Equipment		46,50,000
2 Current assets (Rs. 40,00,000 – Rs. 3,75,000)		36,25,000
Total		82,75,000

Notes to Accounts

			Rs.	Rs.
1.	Share Capital			
	Equity share capital			
	1,10,000 Equity shares of Rs.10 each			11,00,000
2.	Reserves and Surplus			
	Capital Reserve		2,00,000	
	Capital Redemption Reserve		2,50,000	
	Securities premium	2,50,000		
	Less: Utilization for share buy-back (1,25,000)	(1,25,000)	1,25,000	
	Share Option Outstanding Account		4,00,000	
	Revenue reserves	15,00,000		
	Less: Transfer to CRR	(2,50,000)	12,50,000	
	Surplus i.e. Profit and Loss A/c		1,25,000	23,50,000
3.	Long-term borrowings			

	Secured		
	12% Debentures	18,75,000	
	Unsecured loans	10,00,000	28,75,000
4.	Short-term borrowings		
	Current maturities of long-term borrowings		16,50,000
5.	Other Current Liabilities		
	Unpaid dividend	1,00,000	
	Application money received for allotment due for refund	2,00,000	3,00,000

Question 26 : May – 2022 – RTP

Explain the conditions for equity shares with differential rights under the Companies (Share Capital and Debentures) Rules.

Solution :

Companies (Share Capital and Debentures) Rules deal with equity shares with differential rights. The rules lay down the following conditions to be compulsorily complied with:

- The articles of association of the company authorizes the issue of shares with differential rights;
- The issue of shares is authorized by an ordinary resolution passed at a general meeting of the shareholders: Provided that where the equity shares of a company are listed on a recognized stock exchange, the issue of such shares shall be approved by the shareholders through postal ballot;
- The voting power in respect of shares with differential rights shall not exceed seventy four percent of the total voting power including voting power in respect of equity shares with differential rights issued at any point of time;
- The company has not defaulted in filing financial statements and annual returns for three financial years immediately preceding the financial year in which it is decided to issue such shares;
- The company has no subsisting default in the payment of a declared dividend to its shareholders or repayment of its matured deposits or redemption of its preference shares or debentures that have become due for redemption or payment of interest on such deposits or debentures or payment of dividend;

  The company has not defaulted in payment of the dividend on preference shares or repayment of any term loan from a public financial institution or State level financial institution or scheduled Bank that has become repayable or interest payable thereon or dues with respect to statutory payments relating to its employees to any authority or default in crediting the amount in Investor Education and Protection Fund to the Central Government;

  Provided that a company may issue equity shares with differential rights upon expiry of five years from the end of financial year in which such default was made good.

- The company has not been penalized by Court or Tribunal during the last three years of any offence under the Reserve Bank of India Act, 1934, the Securities and Exchange Board of India Act, 1992, the Securities Contracts Regulation Act, 1956, the Foreign Exchange Management Act, 1999 or any other special Act, under which such companies being regulated by sectoral regulators.

Question 27 : May – 2022 – RTP

L,M,N and O hold Equity capital in the proportion of 30:30:20:20 in Hill Ltd. X, Y, Z and K hold preference share capital in the proportion of 40:30:20:10. You are required to identify the voting rights of shareholders in case of resolution of winding up of the company if the paid-up capital of the company is Rs. 60 Lakh and preference share capital is Rs. 30 Lakh.

Solution :

L, M, N and O hold Equity capital is held by in the proportion of 30:30:20:20 and X, Y, Z and K hold preference share capital in the proportion of 40:30:20:10. As the paid-up equity share capital of the company is Rs. 60 Lakhs and Preference share capital is Rs. 30 Lakh (2:1), then relative weights in the voting right of equity shareholders and preference shareholders will be 2/3 and 1/3. The respective voting right of various shareholders will be

L = 2/3X30/100 = 3/15
M = 2/3X30/100 = 3/15
N = 2/3X20/100 = 2/15
O = 2/3X20/100 = 2/15
X = 1/3X40/100 = 2/15

Y = 1/3X30/100 = 1/10
Z = 1/3X20/100 = 1/15
K = 1/3X10/100 = 1/30

Question 28 : May – 2022 – Paper

Quick Ltd. has the following capital structure as on 31st March, 2021 :

		Rs. in Crores	
(1)	Share Capital		462
	(Equity Shares of Rs.10 each, fully paid)		
(2)	Reserves and Surplus:		
	General Reserve	336	
	Securities Premium Account	126	
	Profit and Loss Account	126	
	Statutory Reserve	180	
	Capital Redemption Reserve	87	
	Plant Revaluation Reserve	33	888
(3)	Loan Funds:		
	Secured	2,200	

	Unsecured	320	2,520

On the recommendations of the Board of Directors, on 16th September, 2021, the shareholders of the company have approved a proposal to buy-back of equity shares. The prevailing market value of the company's share is Rs.20 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 50% over market value. The company had sufficient balance in its bank account for the buy-back of shares.

You are required to compute the maxiijium number of shares that can be bought back in the light of the above information and also under a situation where the loan funds of the company were either Rs.1,680 Crores or Rs.2,100 Crores,

Assuming that the entire buy-back is completed by 31st December, 2021, Pass the necessary accounting entries (narrations not required) in the books of the company in each situation.

Solution :

Statement determining the maximum number of shares to be bought back

Number of shares

Particulars	**When loan fund is**		
	Rs. 2,520 crores	**Rs. 1,680 crores**	**Rs. 2,100 crores**
Shares Outstanding Test (W.N.1)	11.55	11.55	11.55
Resources Test (W.N.2)	8.75	8.75	8.75
Debt Equity Ratio Test (W.N.3)	Nil	5.25	Nil
Maximum number of shares that can be bought back [least of the above]	Nil	5.25	Nil

Journal Entries for the Buy-Back
(applicable only when loan fund is Rs. 1,680 crores)

Rs. in crores

	Particulars		**Debit**	**Credit**
(a)	Equity share buy-back account	Dr.	157.5	
	To Bank account			157.5
(b)	Equity share capital account (5.25 x Rs. 10)	Dr.	52.5	
	Securities premium account (5.25 x Rs. 20)	Dr.	105	
	To Equity share buy-back account			157.5
(c)	General reserve account	Dr.	52.5	
	To Capital redemption reserve account			52.5

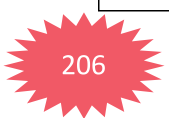
Working Notes:

1. Shares Outstanding Test

Particulars	**(Shares in crores)**
Number of shares outstanding	46.2
25% of the shares outstanding	11.55

2. Resource Test

Particulars	



Paid up capital (Rs. in crores)	462
Free reserves (Rs. in crores) (336+126+126)	588
Shareholders' funds (Rs. in crores)	1,050
25% of Shareholders fund (Rs. in crores)	Rs. 262.5 crores
Buy-back price per share	Rs. 30
Number of shares that can be bought back (shares in crores)	8.75 crores shares

3. Debt Equity Ratio Test

	Particulars	When loan fund is		
		Rs. 2,520 crores	**Rs. 1,680 crores**	**Rs. 2,100 crores**
(a)	Loan funds (Rs. in crores)	2,520	1,680	2,100
(b)	Minimum equity to be maintained after buy-back in the ratio of 2:1 (Rs. in crores)	1,260	840	1,050
(c)	Present equity shareholders fund (Rs. in crores)	1,050	1,050	1,050
(d)	Future equity shareholder fund (Rs. in crores) (See Note 2)	N.A.	997.5 (1,050 - 52.5)	N.A.
(e)	Maximum permitted buy-back of Equity (Rs. in crores) [(d) – (b)] (See Note 2)	Nil	157.5 (by simultaneous equation)	Nil
(f)	Maximum number of shares that can be bought back @ Rs.30 per share (shares in crores) (See Note 2)	Nil	5.25 (by simultaneous equation)	Nil

Note:

1. Under Situations 1 & 3 the company does not qualify for buy-back of shares as per the provisions of the Companies Act, 2013.
2. As per section 68 of the Companies Act, 2013, the ratio of debt owed by the company should not be more than twice the capital and its free reserve after such buy-back.
   Amount transferred to CRR and maximum equity to be bought back will be calculated by simultaneous equation method.
   Suppose amount equivalent to nominal value of bought back shares transferred to CRR account is 'x' and maximum permitted buy-back of equity is 'y'.
   Then
   Equation 1 : (Present equity – Nominal value of buy-back transfer to CRR) – Minimum equity to be maintained= Maximum permissible buy-back of equity
   (1,050 – x) – 840 = y
   Since 210 – x = y
   Equation 2 : $\left(\frac{\text{Maximum buy-back}}{\text{Offer price for buy-back}} \times \text{Nominal Value}\right)$
   = Nominal value of the shares bought – back to be transferred to CRR
   = $\left(\frac{y}{30} \times 10\right)$

Or 3x = y (2)

by solving the above two equations we get

x = Rs. 52.5 crores

y = Rs. 157.5 crores

3. Statutory reserves, capital redemption reserve and plant revaluation reserves are not free reserves.
4. For calculation of debt -equity ratio both secured and unsecured loans have been considered.

Question 29 : May – 2022 – Paper

In a limited company, Equity Share Capital is held by X, Y and Z in the proportion of 30:30: 40. Also A, B and C hold preference share capital in the proportion of 50 : 30 : 20. The company has not paid the dividend to holders of preference share capital for more than 3 years. Given that the paid-up equity share capital of the company is 1 Crore and that of preference share capital is Rs.50 Lakh.

(i) Find out the relative weight in the voting right of equity shareholders and preference shareholders.

(ii) Also the company proposing to issue equity shares with differential voting rights (DVR) to the extent of Rs.50 lakhs. Assuming the company fulfils other conditions pertaining to the issue of shares with DVR. Can the company issue the shares with DVR?

Solution :

(i) The respective voting right of various shareholders will be

X = $2/3 \times 30/100$ = 3/15 OR 20%

Y = $2/3 \times 30/100$ = 3/15 OR 20%

Z = $2/3 \times 40/100$ = 4/15 OR 26.67%

A = $1/3 \times 50/100$ = 1/6 OR 16.67%

B = $1/3 \times 30/100$ = 1/10 OR 10%

C = $1/3 \times 20/100$ = 2/30 OR 6.67%

Hence their relative weights are 3/15: 3/15: 4/15: 1/6: 1/10:2/30 or 6:6:8:5:3:2.

(ii) The voting power in respect of shares with differential rights shall not exceed seventy four percent of the total voting power including voting power in respect of equity shares with differential rights (DVR) issued at any point of time as per Companies (Share Capital and Debentures) Rules.

	Rs.
Existing Equity Share Capital paid up	1,00,00,000.00
Proposed DVR	50,00,000.00
Post DVR Equity Share Capital paid up	1,50,00,000.00
% of shares with DVR to total paid up Equity Share Capital (including Equity Shares with DVR) (Rs. 50,00,000 / Rs. 150,00,000 X 100)	33.33%

In the given case 33.33% of shares with DVR to total post issue paid up Equity Capital (including Equity Shares with DVR) is not exceeding 74%. Hence, the company can issue such equity shares.

Question 30 : Nov – 2022 – RTP

Umesh Ltd. resolves to buy back 4 lakhs of its fully paid equity shares of Rs. 10 each at Rs. 22 per share. This buyback is in compliance with the provisions of the Companies Act and does not exceed 25% of Company's paid up capital in the financial year. For the purpose, it issues 1 lakh 11 % preference shares of Rs. 10 each at par, the entire amount being payable with applications. The company uses Rs. 16 lakhs of its balance in Securities Premium Account apart from its adequate balance in General Reserve to fulfill the legal requirements regarding buy-back. Give necessary journal entries to record the above transactions.

Solution :

Journal Entries in the books of Umesh Ltd.

			Rs.	Rs.
1	Bank A/c	Dr.	10,00,000	
	To 11% Preference share application & allotment A/c			10,00,000
	(Being receipt of application money on preference shares)			
2	11% Preference share application & allotment A/c	Dr.	10,00,000	
	To 11% Preference share capital A/c			10,00,000
	(Being allotment of 1 lakh preference shares)			
3	General reserve A/c	Dr.	30,00,000	
	To Capital redemption reserve A/c			30,00,000
	(Being creation of capital redemption reserve for buy back of shares)			
4	Equity share capital A/c	Dr.	40,00,000	
	Premium payable on buyback A/c	Dr.	48,00,000	
	To Equity shareholders/Equity shares buy back A/c			88,00,000
	(Amount payable to equity shareholder on buy back)			
5	Equity shareholders/ Equity shares buy back A/c	Dr.	88,00,000	
	To Bank A/c			88,00,000
	(Being payment made for buy back of shares)			
6	Securities Premium A/c	Dr.	16,00,000	
	General reserve A/c	Dr.	32,00,000	
	To Premium payable on buyback A/c		48,00,000	
	(Being premium on buyback charged from securities premium and general reserve)			

Working Notes:

1. Calculation of amount used from General Reserve Account

		Rs.
Amount paid for buy back of shares (4,00,000 shares x Rs. 22)		88,00,000
Less: Proceeds from issue of Preference Shares (1,00,000 shares x Rs.10)		-10,00,000
Less: Utilization of Securities Premium Account		-16,00,000
Balance used from General Reserve Account		62,00,000
* Used under Section 68 for buy back	32,00,000	
Used under Section 69 for transfer to CRR (W.N 2)	30,00,000	
	62,00,000	

2. Amount to be transferred to Capital Redemption Reserve account

	Rs.
Nominal value of shares bought back (4,00,000 shares x Rs.10)	40,00,000
Less: Nominal value of Preference Shares issued for such buy back (1,00,000 shares x Rs.10)	(10,00,000)
Amount transferred to Capital Redemption Reserve Account	30,00,000

Question 31 : Nov – 2022 – RTP

(a) What is meant by "equity shares with differential rights". Can preference shares be also issued with differential rights?

(b) L, M, N and O hold Equity capital in the proportion of 30:30:20:20 in AB Ltd. X, Y, Z and K hold preference share capital in the proportion of 40:30:20:10.
You are required to identify the voting rights of shareholders in case of resolution of winding up of the company if the paid-up capital of the company is Rs. 80 Lakh and Preference share capital is Rs. 40 Lakh.

Solution :

(a) Equity shares with Differential Rights means the share with dissimilar rights as to dividend, voting or otherwise. Preference shares cannot be issued with differential rights. It is only the equity shares, which are issued.

(b) L, M, N and O hold Equity capital in the proportion of 30:30:20:20 and X, Y, Z and K hold preference share capital in the proportion of 40:30:20:10. As the paid-up equity share capital of the company is Rs. 80 Lakhs and Preference share capital is Rs. 40 Lakh (2:1), then relative weights in the voting right of equity shareholders and preference shareholders will be 2/3 and 1/3. The respective voting right of various shareholders will be

L	=	$2/3 \times 30/100$	= 3/15
M	=	$2/3 \times 30/100$	= 3/15
N	=	$2/3 \times 20/100$	= 2/15
O	=	$2/3 \times 20/100$	= 2/15
X	=	$1/3 \times 40/100$	= 2/15
Y	=	$1/3 \times 30/100$	= 1/10
Z	=	$1/3 \times 20/100$	= 1/15
K	=	$1/3 \times 10/100$	= 1/30

Question 32 : Nov – 2022 – Paper

PG Limited furnishes the following Balance Sheet as at 31st March, 2022:

	Particulars	Notes	Rs. (in
(I)	**Equity and Liabilities**		
1	**Shareholders' funds**		
	(a) Share Capital	1	12,000
	(b) Reserves and Surplus	2	8,100
2	**Current liabilities**		
	(a) Trade Payables		7,450
	(b) Other Current Liabilities		1,950
	Total		**29,500**
(II)	**Assets**		
1	**Non-current assets**		
	(a) Property, Plant and Equipment		12,760
	(b) Non-current Investments		740
2	**Current assets**		
	(a) Inventories		6,000
	(b) Trade receivables		2,600
	(c) Cash and cash equivalents		7,400
	Total		**29,500**

Notes to accounts :

	Particulars	Rs. (in Lakhs)
1	**Share Capital**	
	Authorized, issued and subscribed capital	
	Equity share capital (fully paid up shares of Rs.10 each)	12,000
2	**Reserves and Surplus**	
	Securities premium	1,750
	General reserve	2,650

	Capital redemption reserve	2,000
	Profit and Loss account	1,700
	Total	8,100

On 1st April, 2022, the company announced the buy-back of 25% of its Equity Shares @ Rs.15 per share. For this purpose, it sold all of its investments for Rs.750 lakhs.

On 5th April, 2022, the company achieved the target of buy-back.

You are required to pass necessary journal entries for the above transactions.

Thanks ....

CHAPTER 17

AS 14 AMALGAMATION OF COMPANIES

Question 1 : May – 2018 – Paper / Nov – 2020 – RTP

X Ltd. and Y Ltd. give the following information of assets, equity and liabilities as on 31st March, 2018:

Particulars	X Ltd. (Rs.)	Y Ltd. (Rs.)
Equity and Liabilities		
Equity Shares of Rs.10 each	30,00,000	9,00,000
9% Preference Shares of Rs.100 each	3,00,000	-
10% Preference Shares of Rs.100 each	-	3,00,000
General Reserve	2,10,000	2,10,000
Retirement Gratuity Fund (long term)	1,50,000	60,000
Trade Payables	3,90,000	2,40,000
Total	**40,50,000**	**17,10,000**
Assets		
Goodwill	1,50,000	75,000
Land & Buildings	9,00,000	3,00,000
Plant & Machinery	15,00,000	4,50,000
Inventories	7,50,000	5,25,000
Trade Receivables	6,00,000	3,00,000
Cash and Bank	1,50,000	60,000
Total	**40,50,000**	**17,10,000**

X Ltd. absorbs Y Ltd. on the following terms:

(i) 10% Preference Shareholders are to be paid at 10% premium by issue of 9% Preference Shares of X Ltd.

(ii) Goodwill of Y Ltd. on absorption is to be computed based on two times of average profits of preceding three financial years (2016-17 : Rs. 90,000; 2015-16 : Rs. 78,000 and 2014-15: Rs. 72,000). The profits of 2014 -15 included credit of an insurance claim of Rs. 25,000 (fire occurred in 2013-14 and loss by fire Rs. 30,000 was booked in Profit and Loss Account of that year). In the year 2015 -16, there was an embezzlement of cash by an employee amounting to Rs. 10,000.

(iii) Land & Buildings are valued at Rs. 5,00,000 and the Plant & Machinery at Rs. 4,00,000.

(iv) Inventories are to be taken over at 10% less value and Provision for Doubtful Debts is to be created @ 2.5%.

(v) There was an unrecorded current asset in the books of Y Ltd. whose fair value amounted to Rs. 15,000 and such asset was also taken over by X Ltd.

(vi) The trade payables of Y Ltd. included Rs. 20,000 payable to X Ltd.

(vii) Equity Shareholders of Y Ltd. will be issued Equity Shares @ 5% premium.

You are required to:

(i) Prepare Realisation A/c in the books of Y Ltd.

(ii) Show journal entries in the books of X Ltd.

(iii) Prepare the Balance Sheet of X Ltd. after absorption as at 31st March,2018.

Solution :

In the Books of Y Ltd.

Realisation Account

		Rs.		Rs.
To Sundry Assets:			By Retirement Gratuity Fund	60,000
Goodwill	75,000		By Trade payables	2,40,000
Land & Building	3,00,000		By X Ltd. (Purchase Consideration)	15,90,000
Plant & Machinery	4,50,000			
Inventory	5,25,000			
Trade receivables	3,00,000			
Bank	60,000	17,10,000		
To Preference Shareholders (Premium on Redemption)		30,000		
To Equity Shareholders (Profit on Realisation)		1,50,000		
		18,90,000		**18,90,000**

In the Books of X Ltd.

Journal Entries

		Dr. Rs.	Cr. Rs.
Business Purchase A/c	Dr.	15,90,000	
To Liquidators of Y Ltd. Account			15,90,000
(Being business of Y Ltd. taken over)			
Goodwill Account	Dr.	1,50,000	
Land & Building Account	Dr.	5,00,000	
Plant & Machinery Account	Dr.	4,00,000	
Inventory Account	Dr.	4,72,500	
Trade receivables Account	Dr.	3,00,000	
Bank Account	Dr.	60,000	
Unrecorded assets Account	Dr.	15,000	
To Retirement Gratuity Fund Account			60,000

Particulars		Dr.	Cr.
To Trade payables Account			2,40,000
To Provision for Doubtful Debts Account			7,500
To Business Purchase A/c			15,90,000
(Being Assets and Liabilities taken over as per agreed valuation).			
Liquidators of Y Ltd. A/c	Dr.	15,90,000	
To 9% Preference Share Capital A/c			3,30,000
To Equity Share Capital A/c			12,00,000
To Securities Premium A/c			60,000
(Being Purchase Consideration satisfied as above)			

Balance Sheet of X Ltd. (after absorption)
as at 31st March, 2018

		Particulars	Notes	Rs.
I.		**Equity and Liabilities**		
1		**Shareholders' funds**		
	a	Share capital	1	48,30,000
	b	Reserves and Surplus	2	2,70,000
2		**Non-current liabilities**		
	a	Long-term provisions	3	2,10,000
3		**Current liabilities**		
	a	Trade Payables	4	6,10,000
	b	Short term provision	5	7,500
		Total		**59,27,500**
II.		**Assets**		
1		**Non-current assets**		
		Property, Plant and Equipment	6	33,00,000
		Intangible assets	7	3,00,000
2		**Current assets**		
	a	Inventories	8	12,22,500
	b	Trade receivables	9	8,80,000
	c	Other current Assets	10	15,000
	d	Cash and cash equivalents	11	2,10,000
		Total		**59,27,500**

Notes to Accounts :

		Rs.
1	Share Capital	
	Equity share capital	
	4,20,000 Equity Shares of Rs. 10 each fully paid (Out of above 1,20,000 Equity Shares were issued at 5% premium in consideration other than for cash)	42,00,000

	Preference share capital 6,300 9% Preference Shares of Rs. 100 each (Out of above 3,300 Preference Shares were issued in consideration other than for cash)	6,30,000
	Total	48,30,000
2	Reserves and Surplus	
	Securities Premium	60,000
	General Reserve	2,10,000
	Total	2,70,000
3	Long-term provisions	
	Retirement Gratuity fund	2,10,000
4	Trade payables (3,90,000 + 2,40,000 - 20,000*) * Mutual Owings eliminated.	6,10,000
5	Short term Provisions	
	Provision for Doubtful Debts	7,500
6	Property, Plant and Equipment	
	Land & Buildings	14,00,000
	Plant & Machinery	19,00,000
	Total	33,00,000
7	Intangible assets	
	Goodwill (1,50,000 +1,50,000)	3,00,000
8	Inventories (7,50,000 + 4,72,500)	12,22,500
9	Trade receivables (6,00,000 + 3,00,000 - 20,000)	8,80,000
10	Other current Assets	15,000
11	Cash and cash equivalents (1,50,000 +60,000)	2,10,000

Working Notes :

1. Computation of goodwill

	Rs.
Profit of 2016-17	90,000
Profit of 2015-16 adjusted (Rs. 78,000 + 10,000)	88,000
Profit of 2014-15 adjusted (Rs. 72,000 – 25,000)	47,000
	2,25,000
Average profit	75,000

Goodwill to be valued at 2 times of average profits = Rs. 75,000 x 2 = Rs. 1,50,000

2.

Purchase Consideration:	**Rs.**
Goodwill	1,50,000
Land & Building	5,00,000

Particulars		Rs.
Plant & Machinery		4,00,000
Inventory		4,72,500
Trade receivables		3,00,000
Unrecorded assets		15,000
Cash at Bank		60,000
		18,97,500
Less: Liabilities:		
Retirement Gratuity	60,000	
Trade payables	2,40,000	
Provision for doubtful debts	7,500	(3,07,500)
Net Assets/ Purchase Consideration		15,90,000
To be satisfied as under:		
10% Preference Shareholders of Y Ltd.		3,00,000
Add: 10% Premium		30,000
9% Preference Shares of X Ltd.		3,30,000
Equity Shareholders of Y Ltd. to be satisfied by issue of 1,20,000 equity Shares of X Ltd. at 5% Premium		12,60,000
		15,90,000

Question 2 : Nov – 2018 – Paper

On 1st April, 2018, Tina Ltd. take over the business of Rina Ltd. and discharged purchase consideration as follows:

(i) Issued 50,000 fully paid Equity shares of Rs. 10 each at a premium of Rs. 5 per share to the equity shareholders of Rina Ltd.

(ii) Cash payment of Rs. 50,000 was made to equity shareholders of Rina Ltd.

(iii) Issued 2,000 fully paid 12% Preference shares of Rs. 100 each at par to discharge the preference shareholders of Rina Ltd.

(iv) Debentures of Rina Ltd. (Rs. 1,20,000) will be converted into equal number and amount of 10% debentures of Tina Ltd.

Calculate the amount of Purchase consideration as per AS-14 and pass Journal Entry relating to discharge of purchase consideration in the books of Tina Ltd.

Solution :

Particulars	**Rs.**
Equity Shares (50,000 x 15)	7,50,000
Cash payment	50,000
12% Preference Share Capital	2,00,000
Purchase Consideration	10,00,000

As per AS 14, consideration for the amalgamation means the aggregate of the shares and other securities issued and the payment made in the form of cash or other assets by the transferee

company to the shareholders of the transferor company. Thus, payment to debenture holders are not covered by the term 'consideration'.

Journal entry relating to discharge of consideration in the books of Tina Ltd.

Liquidation of Rina Ltd.A/c	10,00,000	
To Equity share capital A/c		5,00,000
To 12% Preference share capital A/c		2,00,000
To Securities premium A/c		2,50,000
To Bank/Cash A/c		50,000
(Discharge of purchase consideration)		

Question 3 : May – 2019 – RTP

P Ltd. and Q Ltd. decided to amalgamate as on 01.04.2018 Their summarized Balance Sheets as on 31.03.2018 were as follows:

(Rs.in '000)

Particulars	**P Ltd.**	**Q Ltd.**
Source of Funds:		
Equity share capital (Rs.10 each)	300	280
9% preference share Capital (Rs.100 each)	60	40
Investment allowance Reserve	10	4
Profit and Loss Account	68	68
10 % Debentures	100	60
Trade Payables	50	30
Tax provision	14	8
Total	**602**	**490**
Application of Funds:		
Building	120	100
Plant and Machinery	160	140
Investments	80	50
Trade receivables	90	70
Inventories	72	80
Cash and Bank	80	50
Total	**602**	**490**

From the following information, you are required to prepare the Balance Sheet as on 01.04.2018 of a new company, R Ltd., which was formed to take over the business of both the companies and took over all the assets and liabilities:

(i) 50 % Debenture are to be converted into Equity Shares of the New Company.

(ii) Investments are non- current in nature.

(iii) Fixed Assets of P Ltd. were valued at 10% above cost and that of Q Ltd. at 5% above cost.

(iv) 10 % of trade receivables were doubtful for both the companies. Inventories to be carried at cost.

(v) Preference shareholders were discharged by issuing equal number of 9% preference shares at par.

(vi) Equity shareholders of both the transferor companies are to be discharged by issuing Equity shares of Rs.10 each of the new company at a premium of Rs.5 per share.

Give your answer on the basis that amalgamation is in the nature of purchase.

Solution :

M/s R Ltd.

Balance Sheet as at 1.4.2018

		Particulars	Notes	Rs. in '000
		Equity and Liabilities		
1		**Shareholders' funds**		
	a	Share capital	1	6,55,980
	b	Reserves and Surplus	2	2,77,990
2		**Non-current liabilities**		
	a	Long-term borrowings	3	80,000
3		**Current liabilities**		
	a	Trade Payables	4	80,000
	b	Short term provision	5	22,000
		Total		**11,15,970**
		Assets		
1		**Non-current assets**		
	a	Property, Plant & Equipment		
		Tangible assets	6	5,60,000
	b	Non-current investments	7	1,30,000
2		**Current assets**		
	a	Inventory	8	1,52,000
	b	Trade receivables	9	1,44,000
	c	Cash and cash equivalents	10	1,29,970
		Total		**11,15,970**

Notes to accounts :

		Rs. in '000
1	**Share Capital**	
	Equity share capital	
	55,598 Equity shares of Rs.10 each, fully paid up (W.N.2)	5,55,980
	Preference share capital	
	9% Preference share capital (Share of Rs.100 each) (W.N.2)	1,00,000
		6,55,980
2	**Reserves and Surplus**	

	Securities premium (W.N.2)	2,77,990
	Investment allowance reserve (Rs.10,000+ Rs.4,000)	14,000
	Amalgamation adjustment reserve	14,000)
		2,77,990
3	**Long-term borrowings**	
	Secured	
	10% Debentures (50% of Rs.1,60,000)	80,000
4	**Trade Payables** (Rs.50,000+ Rs.30,000)	80,000
5	**Short term provisions**	
	Provision for tax (Rs.14,000+ Rs.8,000)	22,000
6	**Tangible assets**	
	Building (Rs.1,32,000+Rs.1,05,000)	2,37,000
	Plant and machinery (Rs.1,76,000+Rs.1,47,000)	3,23,000
		5,60,000
7	**Non – current Investments** (Rs.80,000+ Rs.50,000)	1,30,000
8	**Inventory**	
	Stock (Rs. 72,000+ Rs. 80,000)	1,52,000
9	**Trade receivables**	
	Trade receivables (90% of (Rs.90,000+ Rs.70,000)	1,44,000
10	**Cash and cash equivalents**	
	Cash and Bank (Rs. 80,000+ Rs. 50,000 – Rs. 30)	1,29,970

Working Notes:

1. Calculation of value of equity shares issued to transferor companies

		P. Ltd. Rs.		Q. Ltd. Rs.
Assets taken over:				
Building		1,32,000		1,05,000
Plant and machinery		1,76,000		1,47,000
Investments		80,000		50,000
Inventories		72,000		80,000
Trade receivables		81,000		63,000
Cash & Bank		80,000		50,000
		6,21,000		4,95,000
Less: Liabilities:				
10% Debentures	1,00,000		60,000	
Trade payables	50,000		30,000	
Tax Provision	14,000	1,64,000	8,000	98,000
		4,57,000		3,97,000
Less: Preference Share Capital		60,000		40,000
		3,97,000		3,57,000

2. Number of shares issued to equity shareholders, debenture holders and preference shareholders

	P Ltd.	Q Ltd.	Total
Equity shares issued @ Rs. 15 per share (including Rs. 5 premium)			
Rs.3,97,000/15	26,466 shares		
Rs.3,57,000/15		23,800 shares	50,266 shares
Equity share capital @ Rs.10	Rs.2,64,660	Rs.2,38,000	Rs.5,02,660
Securities premium @ Rs.5	Rs.1,32,330	Rs.1,19,000	Rs.2,51,330
	Rs.3,96,990	Rs.3,57,000	Rs.7,53,990
50% of Debentures are converted into equity shares @ Rs. 15 per share			
1,00,000/2 = 50,000/15	3,332 shares		
60,000/2 = 30,000/15		2,000 shares	5,332 shares
Equity share capital @ Rs.10	Rs.33,320	Rs.20,000	Rs.53,320
Security premium@ Rs.5	Rs.16,660	Rs.10,000	Rs.26,660
	Rs.49,980	Rs.30,000	Rs. 79,980
9% Preference share capital issued	Rs.60,000	Rs.40,000	Rs.1,00,000

Question 4 : May – 2019 – Paper

The following are the summarized Balance Sheet of VT Ltd. and MG Ltd. as on 31st March, 2018:

	VT Ltd. (Rs.)	MG Ltd. (Rs.)
Equity and Liabilities		
Equity Shares of Rs.10 each	12,00,000	6,00,000
10% Pref. Shares of Rs.100 each	4,00,000	2,00,000
Reserve and Surplus	6,00,000	4,00,000
12% Debentures	4,00,000	3,00,000
Trade Payables	5,00,000	3,00,000
Total	**31,00,000**	**18,00,000**
Assets		
Fixed Assets	14,00,000	5,00,000
Investment	1,60,000	1,60,000
Inventory	4,80,000	6,40,000
Trade Receivables	8,40,000	4,20,000
Cash at Bank	2,20,000	80,000
Total	**31,00,000**	**18,00,000**

Details of Trade receivables and trade payables are as under:

	VT Ltd. (Rs.)	MG Ltd. (Rs.)
Trade Receivable		
Debtors	7,20,000	3,80,000
Bills Receivable	1,20,000	40,000
	8,40,000	4,20,000
Trade Payables		
Sundry Creditors	4,40,000	2,50,000
Bills Payable	60,000	50,000
	5,00,000	3,00,000

Fixed Assets of both the companies are to be revalued at 15% above book value.
Inventory in Trade and Debtors are taken over at 5% lesser than their book value.
Both the companies are to pay 10% equity dividend, Preference dividend having been already paid.
After the above transactions are given effect to, VT Ltd. will absorb MG Ltd. on the following terms :

(i) VT Ltd. will issue 16 Equity Shares of Rs.10 each at par against 12 Shares of MG Ltd.
(ii) 10% Preference Shareholders of MG Ltd. will be paid at 10% discount by issue of 10% Preference Shares of Rs.100 each, at par, in VT. Ltd.
(iii) 12% Debenture holders of MG Ltd. are to be paid at 8% premium, by 12% Debentures in VT Ltd., issued at a discount of 10%.
(iv) Rs.60,000 is to be paid by VT Ltd. to MG Ltd. for Liquidation expenses.
(v) Sundry Debtors of MG Ltd. includes Rs.20,000 due from VT Ltd.

You are required to prepare :

(1) Journal entries in the books of VT Ltd.
(2) Statement of consideration payable by VT Ltd.

Solution :

(i) Journal Entries in the Books of VT Ltd.

		Dr. Rs.	Cr. Rs.
Fixed Assets	Dr.	2,10,000	
To Revaluation Reserve			2,10,000
(Revaluation of fixed assets at 15% above book value)			
Reserve and Surplus	Dr.	1,20,000	
To Equity Dividend			1,20,000
(Declaration of equity dividend @ 10%)			
Equity Dividend	Dr.	1,20,000	
To Bank Account			1,20,000
(Payment of equity dividend)			

Particulars		Dr. (Rs.)	Cr. (Rs.)
Business Purchase Account	Dr.	9,80,000	
To Liquidator of MG Ltd.			9,80,000
(Consideration payable for the business taken over from MG Ltd.)			
Fixed Assets (115% of Rs. 5,00,000)	Dr.	5,75,000	
Inventory (95% of Rs. 6,40,000)	Dr.	6,08,000	
Debtors	Dr.	3,80,000	
Bills Receivable	Dr.	40,000	
Investment	Dr.	1,60,000	
Cash at Bank (Rs. 80,000 –Rs. 60,000 dividend paid)	Dr.	20,000	
To Provision for Bad Debts (5% of Rs. 3,60,000)			18,000
To Sundry Creditors			2,50,000
To 12% Debentures in MG Ltd.			3,24,000
To Bills Payable			50,000
To Business Purchase Account			9,80,000
To Capital Reserve (Balancing figure)			1,61,000
(Incorporation of various assets and liabilities taken over from MG Ltd. at agreed values and difference of net assets and purchase consideration being credited to capital reserve)			
Liquidator of MG Ltd.	Dr.	9,80,000	
To Equity Share Capital			8,00,000
To 10% Preference Share Capital			1,80,000
(Discharge of consideration for MG Ltd.'s business)			
12% Debentures in MG Ltd. (Rs. 3,00,000 × 108%)	Dr.	3,24,000	
Discount on Issue of Debentures	Dr.	36,000	
To 12% Debentures			3,60,000
(Allotment of 12% Debentures to debenture holders of MG Ltd. at a discount of 10%)			
Sundry Creditors	Dr.	20,000	
To Sundry Debtors			20,000
(Cancellation of mutual owing)			
Goodwill	Dr.	60,000	
To Bank			60,000
(Being liquidation expenses reimbursed to MG Ltd.)			
Capital Reserve/P&L A/c	Dr.	60,000	
To Goodwill			60,000
(Being goodwill set off)			

(ii) Statement of Consideration payable by VT Ltd. for 60,000 shares (payment method)

Shares to be allotted 60,000/12 × 16 = 80,000 shares of VT Ltd.

Issued 80,000 shares of Rs. 10 each i.e.	Rs. 8,00,000	(i)
For 10% preference shares, to be paid at 10% discount		
Rs. 2,00,000x 90/100	Rs. 1,80,000	(ii)
Consideration amount [(i) + (ii)]	Rs. 9,80,000	

Question 5 : Nov – 2019 – RTP

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

Liabilities	Rs.	Assets	Rs.
8,000 Equity shares of Rs.100 each	8,00,000	Building	3,40,000
10% Debentures	4,00,000	Machinery	6,40,000
Loans	1,60,000	Inventory	2,20,000
Trade payables	3,20,000	Trade receivables	2,60,000
General Reserve	80,000	Bank	1,36,000
		Patent	1,30,000
		Share issue Expenses	34,000
	17,60,000		**17,60,000**

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

(1) B Ltd. would take over all assets, except bank balance and Patent at their book values less 10%. Goodwill is to be valued at 4 year's purchase of super profits, assuming that the normal rate of return be 8% on the combined amount of share capital and general reserve.

(2) B Ltd. is to take over trade payables at book value.

(3) The purchase consideration is to be paid in cash to the extent of Rs.6,00,000 and the balance in fully paid equity shares of Rs.100 each at Rs.125 per share.

The average profit is Rs. 1,24,400. The liquidation expenses amounted to Rs. 16,000. B Ltd. sold prior to 31st March, 2018 goods costing Rs. 1,20,000 to A Ltd. for Rs. 1,60,000. Rs. 1,00,000 worth of goods are still in Inventory of A Ltd. on 31st March, 2018. Trade payables of A Ltd. include Rs. 40,000 still due to B Ltd.

Show the necessary Ledger Accounts to close the books of A Ltd. and prepare the Balance Sheet of B Ltd. as at 1st April, 2019 after the takeover.

Solution :

Books of A Limited

Realization Account

	Rs.		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

	Rs.		Rs.
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**

10% Debentures Account

	Rs.		Rs.
To Bank	4,00,000	By Balance b/d	4,00,000
	4,00,000		**4,00,000**

Loan Account

	Rs.		Rs.
To Bank	1,60,000	By Balance b/d	1,60,000
	1,60,000		**1,60,000**

Share Issue Expenses Account

	Rs.		Rs.
To Balance b/d	34,000	By Equity shareholders	34,000
	34,000		**34,000**

General Reserve Account

	Rs.		Rs.
To Equity shareholders	80,000	By Balance b/d	80,000
	80,000		**80,000**

B Ltd. Account

	Rs.		Rs.
To Realisation A/c	12,10,000	By Bank	6,00,000
		By Equity share in B Ltd. (4,880 shares at Rs.125 each)	6,10,000
	12,10,000		**12,10,000**

Equity Shares in B Ltd. Account

	Rs.		Rs.
To B Ltd.	6,10,000	By Equity shareholders	6,10,000
	6,10,000		**6,10,000**

Equity Share Holders Account

	Rs.		Rs.
To Realization Account	76,000	By Equity share capital	8,00,000
To Share issue Expenses	34,000	By 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
		Total		**14,75,000**
		Assets		
1		**Non-current assets**		
	a	Property, Plant and Equipment		
		Tangible assets	4	8,82,000
		Intangible assets	5	2,16,000
2		**Current assets**		
	a	Inventories	6	1,83,000
	b	Trade receivables	7	1,94,000
		Total		**14,75,000**

Notes to Accounts

	Particulars		Rs.
1	**Share Capital**		
	Equity share capital		
	4,880 Equity shares of Rs. 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
	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
2	**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 Rs. 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	
	$\frac{40,000}{1,60,000} \times 1,00,000$	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 6 : May – 2020 – RTP

P Ltd. and Q Ltd. agreed to amalgamate and form a new company called PQ Ltd. The summarized balance sheets of both the companies on the date of amalgamation stood as below :

Liabilities	P Ltd. Rs.	Q Ltd. Rs.	Assets	P Ltd. Rs.	Q Ltd. Rs.
Equity Shares (Rs.100 each)	8,20,000	3,20,000	Land & Building	4,50,000	3,40,000
9% Pref. Shares (Rs.100 each)	3,80,000	2,80,000	Furniture & Fittings	1,00,000	50,000
8% Debentures	2,00,000	1,00,000	Plant & Machinery	6,20,000	4,50,000
General Reserve	1,50,000	50,000	Trade receivables	3,25,000	1,50,000
Profit & Loss A/c	3,52,000	2,05,000	Inventory	2,33,000	1,05,000
Unsecured Loan	-	1,75,000	Cash at bank	2,08,000	1,75,000
Trade payables	88,000	1,60,000	Cash in hand	54,000	20,000
	19,90,000	**12,90,000**		**19,90,000**	**12,90,000**

PQ Ltd. took over the assets and liabilities of both the companies at book value after creating provision @ 5% on inventory and trade receivables respectively and depreciating Furniture & Fittings by @ 10%, Plant and Machinery by @ 10%. The trade receivables of P Ltd. include Rs. 25,000 due from Q Ltd.

PQ Ltd. will issue:

(i) 5 Preference shares of Rs. 20 each @ Rs. 18 paid up at a premium of Rs. 4 per share for each pref. share held in both the companies.

(ii) 6 Equity shares of Rs. 20 each @ Rs. 18 paid up a premium of Rs. 4 per share for each equity share held in both the companies.

(iii) 6% Debentures to discharge the 8% debentures of both the companies.

(iv) 20,000 new equity shares of Rs. 20 each for cash @ Rs. 18 paid up at a premium of Rs. 4 per share.

PQ Ltd. will pay cash to equity shareholders of both the companies in order to adjust their rights as per the intrinsic value of the shares of both the companies.

You are required to prepare ledger accounts in the books of P Ltd. and Q Ltd. to close their books.

Solution :

In the Books of P Ltd.
Realization Account

	Rs.		Rs.
To Land & Building	4,50,000	By 8% Debentures	2,00,000
To Plant & Machinery	6,20,000	By Trade Payables	88,000
To Furniture & Fitting	1,00,000	By PQ Ltd. (Purchase consideration)	16,02,100
To Trade receivables	3,25,000	Equity Shareholders A/c (loss)	1,37,900
To Inventory/Stock	2,33,000		
To Cash at Bank	2,08,000		
To Cash in Hand	54,000		
To Preference shareholders (excess payment)	38,000		
	20,28,000		**20,28,000**

Equity Shareholders Account

	Rs.		Rs.
To Realization A/c (loss)	1,37,900	By Share capital	
To Equity Shares in PQ Ltd.	10,82,400	By Profit & Loss A/c	
To Cash	1,01,700	By General Reserve	
	13,22,000		**13,22,000**

9% Preference Shareholders Account

	Rs.		Rs.
To Preference Shares in PQ Ltd.	4,18,000	By Pref. Share capital	3,80,000
		By Realization A/c	38,000
	4,18,000		**4,18,000**

PQ Ltd. Account

	Rs.			Rs.
To Realization A/c	16,02,100	By Shares in PQ Ltd.		
		For Equity	10,82,400	
		For Pref.	4,18,000	15,00,400
		By Cash		1,01,700
	16,02,100			**16,02,100**

8% Debentures holders Account

	Rs.		Rs.
To 6% Debentures	2,00,000	By 8% Debentures	2,00,000

Books of Q Ltd.

Realization Account

	Rs.		Rs.
To Land & Building	3,40,000	8% Debentures	1,00,000
To Plant & Machinery	4,50,000	Trade payables	1,60,000
To Furniture & Fittings	50,000	Unsecured loan	1,75,000
To Trade receivables	1,50,000	PQ Ltd. (Purchase consideration)	7,92,250
To Inventory	1,05,000	Equity Shareholders A/c Loss	90,750
To Cash at bank	1,75,000		
To Cash in hand	20,000		
To Pref. shareholders	28,000		
	13,18,000		**13,18,000**

Equity Shareholders Account

	Rs.		Rs.
To Equity shares in PQ Ltd.	4,22,400	By Share Capital	3,20,000
To Realization	90,750	By Profit & Loss A/c	2,05,000
To Cash	61,850	By General Reserve	50,000
	5,75,000		**5,75,000**

9% Preference Shareholders Account

	Rs.		Rs.
To Preference Shares in PQ Ltd.	3,08,000	By Share capital	2,80,000
		By Realization A/c	28,000
	3,08,000		**3,08,000**

PQ Ltd. Account

	Rs.		Rs.	Rs.
To Realization A/c	7,92,250	By Equity shares in PQ Ltd.		
		For Equity	4,22,400	
		Preference	3,08,000	7,30,400
		By Cash		61,850
	7,92,250			**7,92,250**

8% Debenture holders Account

	Rs.		Rs.
To 6% Debentures	1,00,000	By 8% Debentures	1,00,000

Working Notes :

(i) Purchase consideration :

	P Ltd. Rs.	Q Ltd. Rs.
Payable to preference shareholders:		
Preference shares at Rs. 22 per share	4,18,000	3,08,000
Equity Shares at Rs. 22 per share	10,82,400	4,22,400
Cash [See W.N. (ii)]	1,01,700	61,850
	16,02,100	**7,92,250**

(ii) Value of Net Assets :

		P Ltd. Rs.		Q Ltd. Rs.
Land & Building		4,50,000		3,40,000
Plant & Machinery less 10% Depreciation		5,58,000		4,05,000
Furniture & Fittings less 10% Depreciation		90,000		45,000
Trade receivables less 5%		3,08,750		1,42,500
Inventory less 5%		2,21,350		99,750
Cash at Bank		2,08,000		1,75,000
Cash in hand		54,000		20,000
		18,90,100		12,27,250
Less: Debentures	2,00,000		1,00,000	
Trade payables	88,000		1,60,000	
Secured Loans	–	(2,88,000)	1,75,000	(4,35,000)
		16,02,100		7,92,250
Payable in shares		15,00,400		7,30,400
Payable in cash*		1,01,700		(61,850)

(iii)

	P Ltd. Rs.	Q Ltd. Rs.
Plant &Machinery	6,20,000	4,50,000
Less: Depreciation 10%	62,000	45,000
	5,58,000	4,05,000
Furniture & Fixtures	1,00,000	50,000
Less: Depreciation 10%	10,000	5,000
	90,000	45,000

*This cash is paid to equity shareholders of both the companies for adjustment of their rights as per intrinsic value of both companies.

Question 7 : Nov – 2020 – RTP

Som Ltd. agreed to takeover Dove Ltd. on 1st April, 2020. The terms and conditions of takeover were as follows:

(i) Som Ltd. issued 56,000 equity shares of Rs.100 each at a premium of Rs.10 per share to the equity shareholders of Dove Ltd.

(ii) Cash payment of Rs.1,00,000 was made to equity shareholders of Dove Ltd.

(iii) 20,000 fully paid preference shares of Rs.70 each issued at par to discharge the preference shareholders of Dove Ltd.

You are required to calculate the amount of purchase consideration as per the provisions of AS 14.

Solution :

As per AS 14, 'Accounting for Amalgamations' consideration for the amalgamation means the aggregate of shares and other securities issued and payment made in form of cash or other assets by the transferee company to the shareholders of the transferor company.

Computation of Purchase Consideration :

		Rs.
(a)	Preference Shares:	
	20,000 Preference shares in Som Ltd. @ Rs. 70 per share	14,00,000
(b)	Cash	1,00,000
(c)	Equity shares: 56,000 equity shares in Som Ltd. @ Rs. 110 per share	61,60,000
		76,60,000

Question 8 : Nov – 2020 – Paper

High Ltd and Low Ltd were amalgamated on and from 1st April 2020. A new company Little Ltd was formed to take over the business of the existing Companies. The Balance sheet of High Ltd and Low Ltd as on 31st March 2020 are as under:

(Rs. In lakhs)

Liabilities	**High Ltd**	**Low Ltd**	**Assets**	**High Ltd**	**Low Ltd**
Share Capital			**Plant, Property and Equipment:**		
Equity Shares of Rs. 100 each	1000	850	Land & Building	670	385
14% Pref Shares of Rs. 100 each	320	175	Plant & Machinery	475	355
Reserves & Surplus			Investments	95	80
Revaluation Reserve	225	110	**Current Assets:**		
General Reserve	360	240	Stock	415	389
Investment Allowance Reserve	80	40	Sundry Debtors	322	213

P & L Account	85	82	Sundry Debtors	322	213
Non-Current Liabilities			Bills Receivables	35	-
Secured Loans:			Cash & Bank	303	166
13% Debentures (Rs. 100 each)	100	56			
Unsecured Loans (Public Deposits)	50	-			
Current Liabilities & Provisions					
Sundry Creditors	65	35			
Bills Payable	30	-			
Total	**2315**	**1588**	**Total**	**2315**	**1588**

Other Information:

1. 13% Debenture holders of High Ltd & Low Ltd are discharged by Little Ltd by issuing such number of its 15 % Debentures of Rs. 100 each so as to maintain the same amount of interest.
2. Preference Shareholders of the two companies are issued equivalent number of 15% Preference shares of Little Ltd. At a price of Rs. 125 Per share (Face Value Rs. 100)
3. Little Ltd will issue 4 equity shares for each Equity shares of High Ltd & 3 equity share for each Equity share of Low Ltd. The shares are to be issued at Rs. 35 each having a face value of Rs. 10 Per share
4. Investment Allowance Reserve is to be maintained for two more years

Prepare the Balance Sheet of Little Ltd as on 01st April 2020 after the amalgamation has been carried out in basis of in the nature of Purchase.

Solution :

Balance Sheet of Little Ltd. as at 1st April, 2020

Particulars	Note No.	(Rs.in lakhs)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	1,150.0
(b) Reserves and Surplus	2	2,437.8
(2) Non-Current Liabilities		
Long-term borrowings	3	135.2
Other Borrowings- Unsecured Loans		50
(3) Current Liabilities		
Trade payables	4	130.0
Total		**3,903**
II. Assets		
(1) Non-current assets		
(a) Property, Plant and Equipment	5	1,885

	(b) Non-current investment (95 + 80)		175
(2)	Current assets		
	(a) Inventory (415+389)		804
	(b) Trade receivables	6	570
	(c) Cash and bank balances (303 + 166)		469
	Total		**3,903**

Notes to Accounts

			(Rs. in lakhs)	**(Rs. in lakhs)**
1	Share Capital			
	Equity share capital (W.N.1)			
	65,50,0001 Equity shares of 10 each		655	
	4,95,0002 Preference shares of Rs. 100 each		495	
	(all the above shares are allotted as fully paid-up pursuant to contracts without payment being received in cash)			1,150
2	Reserves and surplus			
	Securities Premium Account (W.N.3)			
	(1080+ 681.25)		1,761.25	
	Capital Reserve (W.N. 2)(283.33 + 393.22)		676.55	
	Investment Allowance Reserve (80 + 40)		120	
	Amalgamation Adjustment Reserve (80 + 40)		(120)	2,437.8
3	Long-term borrowings			
	15% Debentures			135.2
4	Trade payables			
	Sundry Creditors: High Ltd.		65	
	Low Ltd.		35	
	Bills Payable: High Ltd.		30	130
5	Property, Plant and Equipment			
	Land and Building : High Ltd	670		
	Low Ltd	385	1055	
	Plant and Machinery: High Ltd.	475		
	Low Ltd.	355	830	1,885
6	Trade receivables			
	Sundry Debtors: High Ltd.		322	
	Low Ltd.		213	
	Bills Receivables: High Ltd.		35	570

Working Notes :

			(Rs. in lakhs)	
			High Ltd.	**Low Ltd.**
(1)	Computation of Purchase consideration			
	(a) Preference shareholders:			
	$\left(\frac{3,20,000}{100} \text{ i.e. } 3,20,000 \text{ shares}\right) \times$ Rs.125 each		400	
	$\left(\frac{1,75,000}{100} \text{ i.e. } 1,75,000 \text{ shares}\right) \times$ Rs.125 each			218.75
	(b) Equity shareholders:			
	$\left(\frac{10,00,00,000 \times 4}{100} \text{ i.e. } 40,00,000 \text{ shares}\right) \times$ Rs.35 each		1,400	
	$\left(\frac{8,50,00,000 \times 3}{100} \text{ i.e. } 25,50,000 \text{ shares}\right) \times$ Rs.35 each		____	892.50
	Amount of Purchase Consideration		1,800	1,111.25
(2)	Computation of Capital Reserve			
	Assets taken over:			
	Land and Building		670	385
	Plant and Machinery		475	355
	Investments		95	80
	Inventory		415	389
	Trade receivables		322	213
	Bills Receivables		35	
	Cash and bank		303	166
			2,315	1,588
	Less: Liabilities taken over:			
	Debentures	86.67		48.53
	Unsecured Loan	50		
	Creditors	65		35
	Bills Payable	30		
			231.67	85.53
	Net assets taken over		2083.33	1,504.47
	Purchase consideration		1,800	1,111.25
	Capital reserve		283.33	393.22
(3)	Computation of securities premium			
	On preference share capital			
	High Ltd.- 3,20,000 x 25		80	

	Low Ltd.- 1,75,000 x 25		43.75
	On equity share capital		
	High Ltd.- 40,00,000 x 25	100	
	Low Ltd.- 25,50,000 x 25		637.5
	Total	1080	681.25
(4)	Issue of Debentures (Rs. In Lakhs) High Ltd.- 15% fresh issue of debenture for 13% old debentures = 100 X 13% /15% = 86.67(rounded off) Low Ltd.- 15% fresh issue of debenture for 13% old debentures = 56 X 13% /15% = 48.53 (rounded off) Total number of debentures issued = 86.67 + 48.53 = 135.20 Lakhs		

Question 9 : Jan – 2021 – Paper

Galaxy Ltd. and Glory Ltd. are two companies engaged in the same business of chemicals. To mitigate competition, a new company glorious Ltd., is to be formed to which the assets and liabilities of the existing companies, with certain exception, are to be transferred. The summarised Balance Sheet of Galaxy Ltd. and Glory Ltd. as at 31st March, 2020 are as follows :

	Galaxy Ltd. Rs.	Glory Ltd. Rs.
(1) Equity & Liabilities		
(1) Shareholder's fund		
Share Capital		
Equity shares of Rs.10 each	8,40,000	4,55,000
Reserve & surplus		
General Reserve	4,48,000	40,000
Profit & Loss A/c	1,12,000	72,000
(2) Non-current Liabilities		
Secured Loan		
6% Debentures	-	3,30,000
(3) Current Liabilities		
Trade Payables	4,20,000	1,83,000
Total	**18,20,000**	**10,80,000**
(II) Assets		
(1) Non-current assets		
Property, Plant & Equipment		
Freehold property, at cost	5,88,000	3,36,000
Plant & Machinery, at cost less depreciation	1,40,000	84,000
Motor vehicles, at cost less depreciation	56,000	-

(2) Current Assets		
Inventories	3,36,000	4,38,000
Trade Receivables	4,62,000	1,18,000
Cash at Bank	2,38,000	1,04,000
Total	**18,20,000**	**10,80,000**

Assets and Liabilities are to be taken at book value, with the following exceptions :

(i) The Debentures of Glory Ltd are to be discharged by the issue of 8% Debentures of Glorious Ltd. at a premium of 10%

(ii) Plant & Machinery of Galaxy Ltd. are to be valued at Rs.2,52,000.

(iii) Goodwill is to be valued at
Galaxy Ltd. Rs.4,48,000
Glory Ltd. Rs.1,68,000

(iv) Liquidator of Glory Ltd., is appointed for collection from trade debtors and payment to trade creditors. He retained the cash balance and collected Rs.1,10,000 from debtors and paid Rs.1,80,000 to trade creditors. Liquidator is entitled to receive 5% commission for collection and 2.5% for payments. The balance cash will be taken over by new company.

You are required to :

(1) Compute the number of shares to be issued to the shareholders of Galaxy Ltd. and Gory Ltd. assuming the nominal value of each share in Glorious Ltd. is Rs.10.

(2) Prepare Balance Sheet of Glorious Ltd. as on 1st April, 202 and also prepare notes to the accounts as per Schedule III of the Companies Act, 2013.

Solution :

(i) Calculation of Purchase consideration (or basis for issue of shares of Glorious Ltd.

Purchase Consideration:	**Galaxy Ltd. Rs.**	**Glory Ltd. Rs.**
Goodwill	4,48,000	1,68,000
Freehold property	5,88,000	3,36,000
Plant and Machinery	2,52,000	84,000
Motor vehicles	56,000	-
Inventory	3,36,000	4,38,000
Trade receivables	4,62,000	-
Cash at Bank	2,38,000	24,000
	23,80,000	10,50,000
Less: Liabilities:		
6% Debentures (3,00,000 x 110%)	-	(3,30,000)
Trade payables	(4,20,000)	-
Net Assets taken over	19,60,000	7,20,000
To be satisfied by issue of shares of Glorious. Ltd. @ Rs.10 each	1,96,000	72,000

(ii) Balance Sheet of Glorious Ltd. as at 1st April, 2020

			Particulars	Note No	Amount Rs.
			EQUITY AND LIABILITIES		
1			Shareholders' funds		
	(a)		Share capital	1	26,80,000
	(b)		Reserves and surplus	2	30,000
2			Non-current liabilities		
	(a)		Long-term borrowings	3	3,00,000
3			Current liabilities		
	(b)		Trade payables		4,20,000
			Total		34,30,000
			ASSETS		
1			Non-current assets		
	(a)				
		i.	Property, plant and equipment	4	13,16,000
		ii.	Intangible assets	5	6,16,000
2			Current assets		
	(a)		Inventories	6	7,74,000
	(b)		Trade receivables		4,62,000
	(c)		Cash and cash equivalents	7	2,62,000
			Total		34,30,000

Notes to accounts :

		Rs.	Rs.
1	Share Capital		
	Equity share capital		
	2,68,000 shares of Rs. 10 each		26,80,000
	All the above shares are issued for consideration other than cash)		
2	Reserves and surplus		
	Securities Premium		
	(10% premium on debentures of Rs.3,00,000)		30,000
3	Long-term borrowings		
	Secured		
	8% 3,000 Debentures of Rs.100 each		3,00,000
4	Property Plant and Equipment		

	Freehold property		
	Galaxy Ltd.	5,88,000	
	Glory Ltd.	3,36,000	9,24,000
	Plant and Machinery		
	Galaxy Ltd.	2,52,000	
	Glory Ltd.	84,000	3,36,000
	Motor vehicles - Galaxy Ltd.		56,000
			13,16,000
5	Intangible assets		
	Goodwill		
	Galaxy Ltd.	4,48,000	
	Glory Ltd.	1,68,000	6,16,000
6	Inventories		
	Galaxy Ltd.	3,36,000	
	Glory Ltd.	4,38,000	7,74,000
7	Cash and cash equivalents		
	Galaxy Ltd.	2,38,000	
	Glory Ltd.(As per working note)	24,000	2,62,000

Working note:

Calculation of cash balance of Glory Limited to be taken over by Glorious Limited

		Rs.
Cash balance as at 31st March,2020		1,04,000
Add: Received from debtors		1,10,000
		2,14,000
Less: paid to creditors		(1,80,000)
		34,000
Less: Commission to liquidators		
On Debtors @ 5%	5,500	
On Creditors @ 2.5%	4,500	(10,000)
		24,000

Note:

1. It is assumed that the nominal value of debentures of Glory Ltd. is Rs. 100 each.
2. As per the information given in the question, debentures of Glory Ltd. are to be discharged by the issue of debentures of Glorious Ltd. at premium of 10%. It is assumed in the above solution that the debentures are issued at premium of Rs. 10 for discharge of debentures of Rs. 3,30,000. Alternative answer considering other reasonable assumption is also possible.

Question 10 : Jan – 2021 – Paper

List the conditions to fulfilled as per AS-14 (Revised) for an amalgamation to be in the nature of merger.

Solution :

Amalgamation in the nature of merger is an amalgamation which satisfies all the following conditions:

(i) All the assets and liabilities of the transferor company become, after amalgamation, the assets and liabilities of the transferee company.

(ii) Shareholders holding not less than 90% of the face value of the equity shares of the transferor company (other than the equity shares already held therein, immediately before the amalgamation, by the transferee company or its subsidiaries or their nominees) become equity shareholders of the transferee company by virtue of the amalgamation.

(iii) The consideration for the amalgamation receivable by those equity shareholders of the transferor company who agree to become equity shareholders of the transferee company is discharged by the transferee company wholly by the issue of equity shares in the transferee company, except that cash may be paid in respect of any fractional shares.

(iv) The business of the transferor company is intended to be carried on, after the amalgamation, by the transferee company.

(v) No adjustment is intended to be made to the book values of the assets and liabilities of the transferor company when they are incorporated in the financial statements of the transferee company except to ensure uniformity of accounting policies.

Question 11 : May – 2021 – RTP

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) (a) 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.

(b) The trade payables are paid by issue of 12,000 equity shares at par in full and final settlement of their claims.

(c) 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.

(d) 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 debentures	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 share holders 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 To Equity shares application & allotment A/c (W.N. 3)	15,000 94,600	By Balance c/d (Bal. fig.)	1,09,600
	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	2,00,000
Total		**6,00,000**
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		1,09,600
Total		**6,00,000**

Notes to Accounts

		Rs.
1	**Share Capital**	
	Authorised share capital	
	40,000 equity shares of Rs. 10 each	4,00,000
	Issued and Subscribed	
	40,000 shares of Rs. 10 each fully paid up	4,00,000
	(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)	
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	1,00,000
Total purchase consideration	1,65,400

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.	10,000	(30,540)
Number of equity shares issued to public at par for cash		9,460

Question 12 : May – 2021 – RTP

Astha Ltd. is absorbed by Nistha Ltd.; the consideration being the takeover of liabilities, the payment of cost of absorption not exceeding Rs. 10,000 (actual cost Rs. 9,000); the payment of the 9% debentures of Rs. 50,000 at a premium of 20% through 8% debentures issued at a premium of 25% of face value and the payment of Rs.15 per share in cash and allotment of three 11% preference shares of Rs. 10 each and four equity shares of Rs.10 each at a premium of 20% fully paid for every five shares in Astha Ltd.

The number of shares of the vendor company are 1,50,000 of Rs. 10 each fully paid. Calculate purchase consideration as per AS 14.

Solution :

As per AS 14 'Accounting for Amalgamations', the term 'consideration' has been defined as the aggregate of the shares and other securities issued and the payment made in the form of cash or other assets by the transferee company to the shareholders of the transferor company.

The payment made by transferee company to discharge the Debenture holders and outside liabilities and cost of winding up of transferor company shall not be considered as part of purchase consideration.

Computation of Purchase Consideration

	Rs.
Cash payment Rs.15 x 1,50,000	22,50,000
11% Preference Shares of Rs. 10 each [(1,50,000 x 3/5) x Rs. 10]	9,00,000
Equity shares of Rs. 10 each @ 20% premium	
[(1,50,000 x 4/5) x Rs. 12]	14,40,000
Total Purchase consideration	45,90,000

Question 13 : July – 2021 – Paper

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

Particulars	Notes	Black Limited	White Limited
		(Rs. in 000)	(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	Particulars	Black Limited	White Limited
No.		(Rs. in 000)	(Rs. in 000)
1.	Share Capital		
	Equity Shares of Rs.100 each	6,000	3,600
	Reserve and Surplus		

2.	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 depreciation 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 :

(i) Compute no. of share to be issued by Black Limited to White Limited against purchase consideration.

(ii) Calculate the balance of Net Current Assets of Black Limited and White Limited as on 1st July, 2020.

(iii) 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 × 10 % × 3/12]		(60,000)	
		23,40,000	
Add: Appreciation		1,20,000	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)	60,000	3,00,000	
Less: Dividend [36,00,000 × 10%]		(3,60,000)	3,60,000
			48,60,000
Less: Trade payables			(3,60,000)
Purchase Consideration			45,00,000
Number of shares to be issued by Black Ltd. @ ` 100 each			45,000 shares

(ii) Calculation of Net Current Assets as on 01.07.2020

	Rs.	Black Ltd. Rs.	Rs.	White Ltd. 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	90,000	14,10,000	60,000	3,60,000
		40,50,000		21,60,000
Less: Trade payables		(6,00,000)		(3,60,000)
		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	(6,00,000)
	1,20,000
Add: Estimated profit for 3 months after charging depreciation	4,80,000
	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 x 10% x 3/12]		(90,000)
		35,10,000
Property, plant and equipment of White Ltd.		
Taken over as on 31.03.2020	24,00,000	
Less: Proportionate depreciation for 3 months on fixed assets	(60,000)	
	23,40,000	
Add: Appreciation above the estimated book value	1,20,000	24,60,000
Total Property, plant and equipment as on 1.7.2020		59,70,000

Question 14 : Nov – 2021 – RTP

Heera Ltd. and Rita Ltd. agreed to amalgamate their business. The scheme envisaged a share capital, equal to the combined capital of Heera Ltd. and Rita Ltd. for the purpose of acquiring the assets, liabilities and undertakings of the two companies in exchange for share in HR Ltd.

Heera Ltd. and Rita Ltd. make available the following information as on 31st March, 2021 (the date of amalgamation):

	Heera Ltd. Rs.	Rita Ltd. Rs.
Property, plant and Equipment	7,20,000	10,80,000
Inventories	3,60,000	6,60,000
Trade receivables	4,80,000	7,80,000
Cash at Bank	3,00,000	-
Share Capital	6,00,000	8,40,000
Reserves	10,20,000	6,00,000
Bank Overdraft	-	5,40,000
Trade payables	2,40,000	5,40,000

The consideration was to be based on the net assets of the companies as shown above but subject to an additional payment to Heera Ltd. for its goodwill to be calculated as its weighted average of net profits for the three years ended 31st March, 2021. The weights for this purpose for the years 2018-19, 2019-20 and 2020-21 were agreed as 1, 2 and 3 respectively.

The profit had been:

2018-19 Rs. 3,00,000; 2019-20 Rs. 5,25,000 and 2020-21 Rs. 6,30,000.

The shares of HR Ltd. were to be issued to Heera Ltd. and Rita Ltd.at a premium and in proportion to the agreed net assets value of these companies.

In order to raise working capital, HR Ltd. proceeded to issue 72,000 shares of Rs. 10 each at the same rate of premium as issued for discharging purchase consideration to Heera Ltd. and Rita Ltd.

You are required to calculate the number of shares issued to Heera Ltd. and Rita Ltd. and prepare necessary journal entries in the books of HR Ltd.

Solution :

Calculation of number of shares issued to Heera Ltd. and Rita Ltd.

Amount of Share Capital as per balance sheet	Rs.
Heera Ltd.	6,00,000
Rita Ltd.	8,40,000
	14,40,000

Share of Heera Ltd. = Rs. 14,40,000 x [21,60,000/ (21,60,000 + 14,40,000)]

= Rs. 8,64,000 or 86,400 shares

Securities premium = Rs. 21,60,000 – Rs. 8,64,000 = Rs. 12,96,000

Premium per share = Rs. 12,96,000 / Rs. 86,400 = Rs. 15

Issued 86,400 shares @ Rs. 10 each at a premium of Rs. 15 per share

Share of Rita Ltd. = Rs. 14,40,000 x [14,40,000/ (21,60,000 + 14,40,000)]

= Rs. 5,76,000 or 57,600 shares

Securities premium = Rs. 14,40,000 – Rs. 5,76,000 = Rs. 8,64,000

Premium per share = Rs. 8,64,000 / Rs. 57,600 = Rs. 15

Issued 57,600 shares @ Rs. 10 each at a premium of Rs. 15 per share

Journal Entries in the books of HR Ltd.

Particulars		Dr. Amounts (Rs.)	Cr. Amounts (Rs.)
Business purchase account	Dr.	36,00,000	
To Liquidator of Heera Ltd. account			21,60,000
To Liquidator of Rita Ltd. account			14,40,000
(Being the amount of purchase consideration payable to liquidator of Heera Ltd. and Rita ltd. for assets taken over)			
Goodwill	Dr.	5,40,000	
PPE account	Dr.	7,20,000	
Inventory account	Dr.	3,60,000	
Trade receivables account	Dr.	4,80,000	
Cash at bank	Dr.	3,00,000	
To Trade payables account			2,40,000
To Business purchase account			21,60,000
(Being assets and liabilities of Heera Ltd. taken over)			
PPE account	Dr.	10,80,000	
Inventory account	Dr.	6,60,000	
Trade receivables account	Dr.	7,80,000	
To bank overdraft account			5,40,000
To Trade payables account			5,40,000
To Business purchase account			14,40,000
(Being assets and liabilities of Rita Ltd. taken over)			
Liquidator of Heera Ltd. Account	Dr.	21,60,000	
To Equity share capital account (86,400 x Rs. 10)			8,64,000
To Securities premium (86,400 x Rs. 15)			12,96,000
(Being the allotment of shares as per agreement for discharge of purchase consideration)			
Liquidator of Rita Ltd. account	Dr.	14,40,000	
To Equity share capital account (57,600 x Rs. 10)			5,76,000
To Securities premium (57,600 x Rs. 15)			8,64,000
(Being the allotment of shares as per agreement for discharge of purchase consideration)			
Bank A/c	Dr.	18,00,000	
To Equity share capital account (72,000 x Rs.10)			7,20,000
To Securities premium (72,000 x Rs. 15)			10,80,000
(Equity share capital issued to raise working capital)			

Working Notes:

1. Calculation of goodwill of Heera Ltd.

Particulars	Amount Rs.	Weight	Weighted amount Rs.
2018-19	3,00,000	1	3,00,000
2019-20	5,25,000	2	10,50,000
2020-21	6,30,000	3	18,90,000
Total (a + b + c)	14,55,000	6	32,40,000
weighted Average = [Total weighted amount/Total of weight] [Rs. 32,40,000/6]			
Goodwill			5,40,000

2. Calculation of Net assets

Particulars	Heera Ltd. Rs.	Rita Ltd. Rs.
Assets		
Goodwill	5,40,000	
PPE	7,20,000	10,80,000
Inventory	3,60,000	6,60,000
Trade receivable	4,80,000	7,80,000
Cash at bank	3,00,000	
Less: Liabilities		
Bank overdraft		5,40,000
Trade payables	2,40,000	5,40,000
Net assets or Purchase consideration	21,60,000	14,40,000

Question 15 : Dec – 2021 – Paper

Moon Limited is absorbed by the Sun Limited; the consideration, being the takeover of liabilities, the payment of cost of absorption not exceeding Rs.10,000 (actual cost Rs.9,000); the payment of 9% Debentures of Rs.50,000 at a premium of 20% through 8% debentures issued at a premium of 25% of face value; the payment of Rs.18 per share in cash; allotment of two 11% preference shares of Rs.10/- each and one equity shares of Rs.10/- each an a premium of 30% full paid for every three shares in Moon Limited respectively.

The number of shares of the vendor company is 1,50,000 of Rs.10/- cash fully paid. Calculate purchase consideration as per AS-14.

Solution :

As per AS 14 “Accounting for Amalgamations”, the term consideration has been defined as the aggregate of the shares and other securities issued and the payment made in the form of cash or other assets by the transferee company to the shareholders of the transferor company

	Rs.	Form
Equity shareholders:		
1,50,000 × Rs. 18	27,00,000	Cash
1,50,000 × 2/3 × Rs. 10	10,00,000	11% Pref. shares
1,50,000 × 1/3 × Rs. 13	6,50,000	Equity shares
	43,50,000	

Note:

1. According to AS 14, 'consideration' excludes the any amount payable to debenture-holders. The liability in respect of debentures of vendor company will be taken by transferee company, which will then be settled by issuing new debentures.
2. Liquidation expenses will also not form part of purchase consideration

Question 16 : Dec – 2021 – Paper

Dark Ltd. and Fair Ltd. were amalgamated on and from 1st April, 2021. A new company Bright Ltd. was formed to take over the business of the existing companies. The Balance Sheets of Dark Ltd. and Fair Ltd. as at 31st March, 2021 are given below :

	Particulars	Note No.	Dark Ltd.	Fair Ltd.
I	Equity and Liabilities			
	(1) Shareholder's Funds			
	(a) Share Capital	1	1,650	1,425
	(b) Reserves and Surplus	2	630	495
	(2) Non-current Liabilities			
	Long Term Borrowings			
	10% Debentures of Rs.100 each		90	45
	(3) Current Liabilities			
	Trade Payables		630	285
	Total		**3,000**	**2,250**
II	Assets			
	(1) Non Current Assets			
	(a) Property, Plant and Equipment		1,350	975
	(b) Non current Investments		225	75
	(2) Current Assets			
	(a) Inventories		525	375
	(b) Trade Receivables		450	525
	(c) Cash and Cash Equivalents		450	300
	Total		**3,000**	**2,250**

Notes to Accounts :

	Particulars	Dark Ltd.	Fair Ltd.
1	Share Capital		
	Equity Shares of Rs.100 each	1,200	1,125
	14% Preference Shares of Rs.100 each	450	300
		1,650	1,425
2	Reserves and Surplus		
	Revaluation Reserve	225	150
	General Reserve	255	225
	Investment Allowance Reserve	75	75
	Profit and Loss Account	75	45
		630	495

Additional Information :

(i) Bright Limited will issue 5 equity shares for each equity share of Dark Limited and 4 equity shares for each equity share of Fair Limited. The shares are to be issued @ Rs.35 each having a face value of Rs.10 per share.

(ii) 10% Debenture holders of Dark Limited and Fair Limited are discharged by Bright Limited, issuing such number of its 16% Debentures of Rs.100 each so as to maintain the same amount of interest.

(iv) Investment allowance reserve is to be maintained for 4 more years.

(v) Liquidation expenses are for Dark Limited Rs.6,00,000 and for Fair Limited Rs.3,00,000. It is decided that these expenses would be borne by Bright Limited.

(vi) All the assets and liabilities of Dark Limited and Fair Limited are taken over at book value.

(vii) Authorised equity share capital of Bright Limited is Rs.15,00,00,000 divided into equity shares of Rs.10 each. After issuing required number of shares to the liquidators of Dark Limited and Fair Limited, Bright Limited issued balance shares to public. The issue was full subscribed.

You are required to prepare Balance Sheet of Bright Limited as at 1st April, 2021 after amalgamation has been carried out on the basis of Amalgamation in the nature of purchase.

Solution :

Balance Sheet of Bright Ltd. as at 1st April, 2021

Particulars	Note No.	(Rs. in lakhs)
I Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	2,250
(b) Reserves and Surplus	2	4,200
(2) Non-Current Liabilities		
Long-term borrowings	3	84.375
(3) Current Liabilities		
Trade payables	4	915
Total		**7449.375**

II	**Assets**			
	(1) Non-current assets			
	(a)	i. Property, plant and equipment	5	2,325
		ii. Intangible assets	6	633.375
	(b)	Non-current investments	7	300
	(2)	**Current assets**		
	(a)	Inventories	8	900
	(b)	Trade receivables	9	975
	(c)	Cash and cash equivalents	10	2316
	Total			**7449.375**

Notes to Accounts

			(Rs. in lakhs)	(Rs. in lakhs)
1.	Share Capital			
	Authorized Share Capital			
	1,50,00,000 Equity shares of Rs.10 each		1500	
	7,50,000 16% Preference Share of 100 each		750	
	Issued: 1,50,00,000 Equity shares of Rs. 10 each		1500	
	(Out of which 1,05,00,000 Shares were Issued for consideration other than cash)			
	7,50,000 16% Preference Shares of 100 each (Issued for consideration other than cash)		750	2,250
2.	Reserves and surplus			
	Securities Premium Account			
	(1,50,00,000 shares × Rs. 25)	3,750		
	(7,50,000 shares × Rs. 60)	450	4,200	
	Investment Allowance Reserve		150	
	Amalgamation Adjustment Reserve		(150)	4,200
3.	Long-term borrowings			
	16% Debentures (56,25,000 + 28,12,500) (W.N. 3)			84.375
4.	Trade payables			
	Dark Ltd.		630	
	Fair Ltd.		285	915
5.	Property, plant & equipment			
	Land and Building		1350	

	Plant and Machinery		975	2,325
3.	Intangible assets			
	Goodwill [W.N. 2]	624.375		
	Add: liquidation exp. (6+3)	9.00		633.375
7.	Non-current Investments			
	Investments (225+75)			300
8.	Inventories			
	Dark Ltd.		525	
	Fair Ltd.		375	900
9.	Trade receivables			
	Dark Ltd.		450	
	Fair Ltd.		525	975
10.	Cash & cash equivalents			
	Dark Ltd.		450	
	Fair Ltd.		300	
	Liquidation Expenses (6+3)		(9)	
	Shares issued for cash (45 lakh shares x Rs.35)		1575	2316

Working Notes :

		(Rs. in lakhs)	
		Dark Ltd.	Fair Ltd.
(1)	Computation of Purchase consideration		
	(a) Preference shareholders:		
	$\left(\frac{4,50,00,000}{100}\right)$	720	
	i.e. 4,50,000 shares × Rs. 160 each		
	$\left(\frac{3,00,00,000}{100}\right)$		480
	i.e. 3,00,000 shares × Rs. 160 each		
	(b) Equity shareholders:		
	$\left(\frac{12,00,00,000 \times 5}{100}\right)$	2,100	
	i.e. 60,00,000 shares x Rs. 35 each		
	$\left(\frac{11,25,00,000 \times 4}{100}\right)$	______	1,575
	i.e. 45,00,000 shares × Rs. 35 each		
	Amount of Purchase Consideration	2,820	2,055
(2)	Net Assets Taken Over		
	Assets taken over:		
	Property Plant & Equity	1,350	975

	Non-Current Investments		225		75
	Inventory		525		375
	Trade receivables		450		525
	Cash and bank		450		300
			3,000		2,250
	Less: Liabilities taken over:				
	10% Debentures	56.25		28.125	
	Trade payables	630	(686.25)	285	(313.125)
	Net assets taken over		2,313.75		1936.88
	Purchase consideration		2,820		2055
	Goodwill		506.25		118.125
	Total goodwill				624.375

(3) Issue of Debentures

Debentures	Rs.90,00,000	Rs.45,00,000
Interest 10%	Rs.9,00,000	Rs.4,50,000
	$\left(\frac{9,00,000 \times 100}{16}\right)$ = 56,25,000	$\left(\frac{4,50,000 \times 100}{16}\right)$ = 28,12,500

NOTE: In the above solution Rs. 35 has been considered as the issue price of Equity shares for public issue also. Alternative considering this as Rs. 10 also possible. In that case, the balance of cash and cash equivalents will be Rs. 1,191 lakhs and securities premium will be Rs. 3,075 lakhs in place of the balances given in the balance sheet in the above solution.

Question 17 : May – 2022 – RTP

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 'AakashGanga 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 accured 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 AakashGanga 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 AakashGanga Ltd. **(Rs.)**

	Aakash Limited Rs.	Ganga Limited 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)	(1,25,60,000)	(2,70,40,000)
B	1,95,80,000	(41,60,000)
A-B	Goodwill	Capital Reserve
Net Goodwill (1,95,80,000- 41,60,000)	1,54,20,000	

4. Equity shares issued by AakashGanga 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 18 : May – 2022 – Paper

The summarized Balance Sheet of A Ltd. and B Ltd. as at 31st March, 2022 are as under:

	A Ltd. (in Rs.)	B Ltd. (in Rs.)
Equity shares of Rs.10 each, fully paid up	30,00,000	24,00,000
Share Premium Account	4,00,000	—
General Reserve	6,20,000	5,00,000
Profit and Loss Account	3,60,000	3,20,000
Retirement Gratuity Fund Account	1,00,000	—
10% Debentures	20,00,000	—
Unsecured Loan (including loan from A Ltd.)	6,00,000	8,20,000
Trade Payables	1,00,000	3,40,000
	71,80,000	**43,80,000**
Land and Buildings	28,00,000	21,00,000
Plant and Machinery	20,00,000	7,60,000

Long term advance to B Ltd.	2,20,000	—
Inventories	10,40,000	7,00,000
Trade Receivables	8,20,000	5,20,000
Cash and Bank	3,00,000	3,00,000
	71,80,000	**43,80,000**

B Ltd. is to declare and pay Rs.1 per equity share as dividend, before the following amalgamation takes place with Z Ltd.

Z Ltd. was incorporated to take over the business of both A Ltd. and B Ltd.

(a) The authorized share capital of Z Ltd. is Rs.60 lakhs divided into 6 lakhs equity shares of Rs.10 each.

(b) As per Registered Valuer the value of equity shares of A Ltd. is Rs.18 per share and of B Ltd. is 12 per share respectively and agreed by respective shareholders of the companies.

(c) 10% Debentures of A Ltd. to be issued 12% Debentures of Z Ltd. at par in consideration of their holdings.

(d) A contingent liability of A Ltd. of Rs.2,00,000 is to be treated as actual liability

(e) Liquidation expenses including Registered Valuer fees of A Ltd. Rs.50,000 and B Ltd. Rs.30,000 respectively to be borne by Z Ltd.

(f) The shareholders of A Ltd. and B Ltd. is to be paid by issuing sufficient number of fully paid up equity shares of Rs.10 each at a premium of Rs.10 per share.

Assuming amalgamation in the nature of purchase, you are required to pass the necessary journal entries (narrations not required) in the books of Z Ltd. and Prepare Balance Sheet of Z Ltd. immediately after amalgamation of both the companies.

Solution :

Journal Entries in the books of Z Ltd.

		Rs.	Rs.
Business Purchase A/c	Dr.	54,00,000	
To Liquidator of A Ltd. A/c			54,00,000
Land & Building A/c	Dr.	28,00,000	
Plant & Machinery A/c	Dr.	20,00,000	
Long term advance to B Ltd. A/c	Dr.	2,20,000	
Inventories A/c	Dr.	10,40,000	
Trade Receivables A/c	Dr.	8,20,000	
Cash and Bank A/c	Dr.	3,00,000	
Goodwill A/c	Dr.	12,20,000	
To Retirement Gratuity Fund A/c			1,00,000
To 10% Debentures A/c			20,00,000
To Unsecured Loan A/c			6,00,000
To Trade Payables A/c			1,00,000
To Other liabilities A/c			2,00,000
To Business Purchase A/c			54,00,000

10% Debentures A/c	Dr.	20,00,000	
To 12% Debentures A/c			20,00,000
Liquidator of A Ltd. A/c	Dr.	54,00,000	
To Equity Share Capital A/c			27,00,000
To Securities Premium A/c			27,00,000
Business Purchase A/c	Dr.	28,80,000	
To Liquidator of B Ltd. A/c			28,80,000
Land and Building A/c	Dr.	21,00,000	
Plant & Machinery A/c	Dr.	7,60,000	
Inventories A/c	Dr.	7,00,000	
Trade Receivables A/c	Dr.	5,20,000	
Cash and Bank (less dividend) A/c	Dr.	60,000	
To Unsecured Loan A/c			8,20,000
To Trade Payables A/c			3,40,000
To Business Purchase A/c			28,80,000
To Capital Reserve A/c			1,00,000
Liquidators of B Ltd. A/c	Dr.	28,80,000	
To Equity Share Capital A/c			14,40,000
To Securities Premium A/c			14,40,000
Unsecured Loans A/c	Dr.	2,20,000	
To Long term Advance to B Ltd. A/c			2,20,000
*Capital Reserve A/c	Dr.	1,00,000	
To Cash and Bank A/c (Liquidation expenses)			80,000
To Goodwill A/c			20,000

Note:

1. The journal entries for A Ltd. and B Ltd. have been given separately in the above solution. Alternatively, the entries may be given as combined for both companies.
2. *Alternatively, following set of entries may be given in place of the last entry given in the above solution:

		Rs.	Rs.
Goodwill A/c	Dr.	50,000	
To Cash & Bank A/c (Liquidation expenses of A Ltd.)			50,000
Capital Reserve A/c	Dr.	30,000	
To Cash and Bank A/c (Liquidation expenses of B Ltd.)			30,000
Capital Reserve A/c	Dr.	70,000	
To Goodwill A/c			70,000

Balance Sheet of Z Ltd. as at 31st March, 2022

Particulars	Note No.	(Rs.)
I. Equity and Liabilities		

	(1)	**Shareholder's Funds**		
		(a) Share Capital	1	41,40,000
		(b) Reserves and Surplus	2	41,40,000
	(2)	**Non-Current Liabilities**		
		(a) Long-term borrowings	3	20,00,000
		(b) Long term provisions	4	1,00,000
	(3)	**Current Liabilities**		
		(a) Short-term borrowings[1]	5	12,00,000
		(b) Trade payables	6	4,40,000
		(c) Other liability		2,00,000
		Total		1,22,20,000
II.	**Assets**			
	(1)	**Non-current assets**		
		(a) i. Property, plant and equipment	7	76,60,000
		ii. Intangible assets (Goodwill 12,20,000-20,000)		12,00,000
	(2)	**Current assets**		
		(a) Inventories	8	17,40,000
		(b) Trade receivables	9	13,40,000
		(c) Cash and cash equivalents	10	2,80,000
Total				1,22,20,000

Notes to Accounts

			(Rs.)	(Rs.)
1	Share Capital			
	Authorized Share Capital			
	6,00,000 Equity shares of Rs. 10 each			60,00,000
	Issued: 4,14,000 Equity shares of Rs. 10 each (all these shares were Issued for consideration other than cash)			41,40,000
2	Reserves and surplus			
	Securities Premium Account (4,14,000 shares × Rs. 10)			41,40,000
3	Long-term borrowings			
	12% Debentures			20,00,000
4	Long term Provisions			
	Retirement gratuity fund			1,00,000
5	Short-term borrowings			
	Unsecured loans			
	A Ltd.	6,00,000		

	B Ltd.	8,20,000	14,20,000	
	Less: Mutual		(2,20,000)	12,00,000
6	Trade payables			
	A Ltd.		1,00,000	
	B Ltd.		3,40,000	4,40,000
7	Property, plant & equipment			
	Land and Building			
	A Ltd.		28,00,000	
	B Ltd.		21,00,000	49,00,000
	Plant and Machinery			
	A Ltd.		20,00,000	
	B Ltd.		7,60,000	27,60,000
				76,60,000
8	Inventories			
	A Ltd.		10,40,000	
	B Ltd.		7,00,000	17,40,000
9	Trade receivables			
	A Ltd.		8,20,000	
	B Ltd.		5,20,000	13,40,000
10	Cash & cash equivalents			
	A Ltd.		3,00,000	
	B Ltd. [3,00,000-2,40,000(dividend)]		60,000	
			3,60,000	
	Less: Liquidation Expenses		(80,000)	2,80,000

Working Note:

Calculation of amount of Purchase Consideration

	A Ltd.	B Ltd.
Existing shares	3,00,000	2,40,000
Agreed value per share	Rs. 18	Rs. 12
Purchase consideration	54,00,000	28,80,000
No. of shares to be issued of Rs. 20 each (including Rs. 10 premium)	2,70,000	1,44,000
Face value of shares at Rs. 10	27,00,000	14,40,000
Premium of shares at Rs. 10	27,00,000	14,40,000

Question 19 : Nov – 2022 – RTP

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

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 amalgamated 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.	25,000	2,10,000	
	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)
		21,25,000		10,65,000
Less: Liabilities:				
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				
Capitalised value of average profit	[(6,93,000 / 18) x 100]	38,50,000	[(2,16,000 / 18) x 100]	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 x 80% x 20% = 30,000; and
Myth Ltd. = 1,00,000 x 80% x 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]		4000000 / 100000 = Rs. 40		12,55,000 / 40000 = Rs. 31.375

$**1,50,000 \times \frac{14\%}{12\%} = 1,75,000$

(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 20 : Nov – 2022 – Paper

Star Limited agreed to take over Moon Limited on 1st April, 2022. The terms and conditions of takeover were as follows :

(i) Star Limited issued 70,000 Equity shares of Rs.100 each at a premium of Rs.10 per share to the equity shareholders of Moon Limited.

(ii) Cash payment of Rs.1,25,000 was made to the equity shareholders of Moon Limited.

(iii) 25,000 fully paid Preference shares of Rs.70 each issued at par to discharge the preference shareholders of Moon Limited.

You are required :

(i) to give the meaning of 'consideration for the amalgamation' as per AS -14, and

(ii) Calculate the amount of purchase consideration.

Thanks ....

Rahul Malkan

CHAPTER 18

INTERNAL RECONSTRUCTION OF A COMPANY

Question 1 : Nov – 2018 – Paper

The summarized Balance Sheet of SK Ltd. as on 31st March, 2018 is given below.

(Rs. in '000)

	Amount
Liabilities	
Equity Shares of Rs.10 each	35,000
8%, Cumulative Preference Shares of Rs.100 each	17,500
6% Debentures of Rs.100 each	14,000
Sundry Creditors	17,500
Provision for taxation	350
Total	**84,350**
Assets	
Fixed Assets	43,750
Investments (Market value Rs.3325 thousand)	3,500
Current Assets (Including Bank Balance)	35,000
Profit and Loss Account	2,100
Total	**84,350**

The following Scheme of Internal Reconstruction is approved and put into effect on 31st March, 2018.

(i) Investments are to be brought to their market value.

(ii) The Taxation Liability is settled at Rs. 5,25,000 out of current Assets.

(iii) The balance of Profit and Loss Account to be written off.

(iv) All the existing equity shares are reduced to Rs. 4 each.

(v) All preference shares are reduced to Rs. 60 each.

(vi) The rate of interest on debentures is increased to 9%. The Debenture holders surrender their existing debentures of Rs. 100 each and exchange them for fresh debentures of Rs. 80 each. Each old debenture is exchanged for one new debenture.

(vii) Balance of Current Assets left after settlement of taxation liability are revalued at Rs.1,57,50,000.

(viii) Fixed Assets are written down to 80%.

(ix) One of the creditors of the Company for Rs. 70,00,000 gives up 50% of his claim. He is allotted 8,75,000 equity shares of Rs. 4 each in full and final settlement of his claim.

Pass journal entries for the above transactions.

Solution :

Journal Entries in the books of SK Ltd.

	Particulars		Dr. Rs. '000	Cr. Rs. '000
(i)	Equity share capital (Rs. 10) A/c	Dr.	35,000	
	To Equity Share Capital (Rs. 4) A/c			14,000
	To Capital Reduction A/c			21,000
	(Being conversion of equity share capital of Rs. 10 each into Rs. 4 each as per reconstruction scheme)			
(ii)	8% Cumulative Preference Share capital (Rs. 100) A/c	Dr.	17,500	
	To 8% Cumulative Preference Share Capital (Rs. 60) A/c			10,500
	To Capital Reduction A/c			7,000
	(Being conversion of 6% cumulative preference shares capital of Rs. 100 each into Rs. 60 each as per reconstruction scheme)			
(iii)	6% Debentures (Rs. 100) A/c	Dr.	14,000	
	To 9% Debentures (Rs. 80) A/c			11,200
	To Capital Reduction A/c			2,800
	(Being 9% debentures of Rs. 80 each issued to existing 6% debenture holders. The balance transferred to capital reduction account as per reconstruction scheme)			
(iv)	Sundry Creditors A/c	Dr.	7,000	
	To Equity Share Capital (Rs. 4) A/c			3,500
	To Capital Reduction A/c			3,500
	(Being a creditor of Rs. 70,00,000 agreed to surrender his claim by 50% and was allotted 8,75,000 equity shares of Rs. 4 each in full settlement of his dues as per reconstruction scheme)			
(v)	Provision for Taxation A/c	Dr.	350	
	Capital Reduction A/c	Dr.	175	
	To Liability for Taxation A/c			525
	(Being conversion of the provision for taxation into liability for taxation for settlement of the amount due)			
(vi)	Liability for Taxation A/c	Dr.	525	
	To Current Assets (Bank A/c)			525
	(Being the payment of tax liability)			
(vii)	Capital Reduction A/c	Dr.	34,125	
	To P & L A/c			2,100
	To Fixed Assets A/c			8,750
	To Current Assets A/c			18,725

	To Investments A/c		175
	To Capital Reserve A/c (Bal. fig.)		4,375
	(Being amount of Capital Reduction utilized in writing off P & L A/c (Dr.) Balance, Fixed Assets, Current Assets, Investments and the Balance transferred to Capital Reserve)		

Working Note:

Capital Reduction Account

	Rs.		Rs.
To Liability for taxation A/c	175	By Equity share capital	21,000
To P & L A/c	2,100	By 8% Cumulative preferences Share capital	7,000
To Fixed Assets	8,750	By 6% Debentures	2,800
To Current assets	18,725	By Sundry creditors	3,500
To Investment	175		
To Capital Reserve (Bal. fig.)	4,375		
	34,300		**34,300**

Question 2 : May – 2019 – RTP

The Balance Sheet of Lion Limited as on 31-03-2018 is given below:

Particulars	Note No.	Amount (Rs. in lakh)
Equity & Liabilities		
Shareholders' Funds		
Shares' Capital	1	1,400
Reserves & Surplus	2	-522
Non-Current Liabilities		
Long term Borrowings	3	700
Current Liabilities		
Trade Payables	4	102
Other Liabilities	5	24
Total		**1704**
Assets		
Non-Current Assets		
Property, Plant & Equipment		
Tangible Assets	6	750
Current Assets		
Current Investments	7	200
Inventories	8	300
Trade Receivables	9	450
Cash & Cash Equivalents	10	4
Total		**1704**

Notes to Account :

		(Rs. in lakhs)
(1)	Share Capital	
	Authorised :	
	200 lakh shares of Rs.10 each	2,000
	8 lakh, 8% Preference Shares of Rs.100 each	800
		2,800
	Issued, Subscribed and paid up:	
	100 lakh Equity Shares of Rs.10 each, full paid up	1,000
	4 lakh 8% Preference Shares of Rs.100 each, fully paid	400
	Total	1400
(2)	Reserves and Surplus	
	Debit balance of Profit & Loss A/c	(522)
(3)	Long Term Borrowings	
	6% Debentures (Secured by Freehold Property)	400
	Directors' Loan	300
		700
(4)	Trade Payables	
	Trade payables for Goods	102
(5)	Other Current Liabilities	
	Interest Accrued and Due on 6% Debentures	24
(6)	Tangible Assets	
	Freehold Property	550
	Plant & Machinery	200
		750
(7)	Current Investment	
	Investment in Equity Instruments	200
(8)	Inventories	
	Finished Goods	300
(9)	Trade Receivables	
	Trade receivables for Goods	450
(10)	Cash and Cash Equivalents	
	Balance with Bank	4

The Board of Directors of the company decided upon the following scheme of reconstruction with the consent of respective shareholders:

(1) Preference Shares are to be written down to Rs.80 each and Equity Shares to Rs.2 each.

(2) Preference Shares Dividend in arrears for 3 years to be waived by 2/3rd and for balance 1/3rd, Equity Shares of Rs.2 each to be allotted.

(3) Debenture holders agreed to take one Freehold Property at its book value of Rs.300 lakh in part payment of their holding. Balance Debentures to remain as liability of the company.

(4) Interest accrued and due on Debentures to be paid in cash.

(5) Remaining Freehold Property to be valued at Rs.400 lakh.
(6) All investments sold out for Rs.250 lakh.
(7) 70% of Directors' loan to be waived and for the balance, Equity Shares of Rs.2 each to be allowed.
(8) 40% of Trade receivables and 80% of Inventories to be written off.
(9) Company's contractual commitments amounting to Rs.600 lakh have been settled by paying 5% penalty of contract value.

You are required to:
(a) Pass Journal Entries for all the transactions related to internal reconstruction;
(b) Prepare Reconstruction Account; and
(c) Prepare notes on Share Capital and Tangible Assets to Balance Sheet, immediately after the implementation of scheme of internal reconstruction.

Solution :

(a) Journal Entries in the books of Lion Ltd.

	Particulars		Dr. Rs.	Cr. Rs.
			(Rs. in lakhs)	
(i)	8% Preference share capital A/c (Rs.100 each)	Dr.	400	
	To 8% Preference share capital A/c (Rs. 80 each)			320
	To Capital Reduction A/c			80
	(Being the preference shares of Rs.100 each reduced to Rs.80 each as per the approved scheme)			
(ii)	Equity share capital A/c (Rs.10 each)	Dr.	1,000	
	To Equity share capital A/c (Rs. 2 each)			200
	To Capital Reduction A/c			800
	(Being the equity shares of Rs.10 each reduced to Rs.2 each)			
(iii)	Capital Reduction A/c	Dr.	32	
	To Equity share capital A/c (Rs. 2 each)			32
	(Being 1/3rd arrears of preference share dividend of 3 years to be satisfied by issue of 16 lakhs equity shares of Rs.2 each)			
(iv)	6% Debentures A/c	Dr.	300	
	To Freehold property A/c			300
	(Being claim of Debenture holders settled in part by transfer of freehold property)			
(v)	Accrued debenture interest A/c	Dr.	24	
	To Bank A/c			24
	(Being accrued debenture interest paid)			

(vi)	Freehold property A/c	Dr.	150	
	To Capital Reduction A/c			150
	(Being appreciation in the value of freehold property)			
(vii)	Bank A/c	Dr.	250	
	To Investments A/c			200
	To Capital Reduction A/c			50
	(Being investment sold at profit)			
(viii)	Director's loan A/c	Dr.	300	
	To Equity share capital A/c (Rs. 2 each)			90
	To Capital Reduction A/c			210
	(Being director's loan waived by 70% and balance being discharged by issue of 45 lakhs equity shares of Rs.2 each)			
(ix)	Capital Reduction A/c	Dr.	972	
	To Profit and loss A/c			522
	To Trade receivables A/c (450 x 40%)			180
	To Inventories-in-trade A/c (300x 80%)			240
	To Bank A/c (600 x 5%)			30
	(Being certain value of various assets, penalty on cancellation of contract, profit and loss account debit balance written off through Capital Reduction Account)			
(x)	Capital Reduction A/c	Dr.	286	
	To Capital reserve A/c			286
	(Being balance transferred to capital reserve account as per the scheme)			

(b) Capital Reduction Account

	(Rs. in lakhs)		(Rs. in lakhs)
To Equity Share Capital	32	By Preference Share Capital	80
To Trade receivables	180	By Equity Share Capital	800
To Finished Goods	240	By Freehold Property	150
To Profit & Loss A/c	522	By Bank	50
To Bank A/c	30	By Director's Loan	210
To Capital Reserve	286		
	1,290		**1,290**

(c) Notes to Balance Sheet

		(Rs. in lakhs)	(Rs. in lakhs)
1	Share Capital		
	Authorised:		
	200 lakhs Equity shares of Rs. 2 each		400
	8 lakhs 8% Preference shares of Rs. 80 each		640
			1,040
	Issued:		
	161 lakhs equity shares of Rs.2 each		322
	4 lakhs Preference Shares of Rs.80 each		320
			642
2	Tangible Assets		
	Freehold Property	550	
	Less: Utilized to pay Debenture holders	(300)	
		250	
	Add: Appreciation	150	400
	Plant and Machinery		200
			600

Question 3 : Nov – 2019 – RTP

Platinum Limited has decided to reconstruct the Balance Sheet since it has accumulated huge losses. The following is the draft Balance Sheet of the company as on 31st March, 2019 before reconstruction:

Liabilities	Rs.	Assets	Rs.
Share Capital		Goodwill	22,00,000
50,000 shares of Rs.50 each fully paid up	25,00,000	Land & Building	42,70,000
1,00,000 shares of Rs.50 each Rs.40 paid up	40,00,000	Machinery	8,50,000
Capital Reserve	5,00,000	Computers	5,20,000
8% Debentures of Rs.100 each	4,00,000	Inventories	3,20,000
12% Debentures of Rs.100 each	6,00,000	Trade receivables	10,90,000
Trade payables	12,40,000	Cash at Bank	2,68,000
Outstanding Expenses	10,60,000	Profit & Loss Account	7,82,000
Total	**1,03,00,000**		**1,03,00,000**

Following is the interest of Mr. Shiv and Mr. Ganesh in Platinum Limited:

	Mr. Shiv	Mr. Ganesh
8% Debentures	3,00,000	1,00,000
12% Debentures	4,00,000	2,00,000
Total	7,00,000	3,00,000

The following scheme of internal reconstruction was framed and implemented, as approved by the court and concerned parties:

(1) Uncalled capital is to be called up in full and then all the shares to be converted into Equity Shares of Rs. 40 each.

(2) The existing shareholders agree to subscribe in cash, fully paid up equity shares of 40 each for Rs. 12,50,000.

(3) Trade payables are given option of either to accept fully paid equity shares of Rs. 40 each for the amount due to them or to accept 70% of the amount due to them in cash in full settlement of their claim. Trade payables for Rs. 7,50,000 accept equity shares and rest of them opted for cash towards full and final settlement of their claim.

(4) Mr. Shiv agrees to cancel debentures amounting to Rs. 2,00,000 out of total debentures due to him and agree to accept 15% Debentures for the balance amount due. He also agrees to subscribe further 15% Debentures in cash amounting to Rs. 1,00,000.

(5) Mr. Ganesh agrees to cancel debentures amounting to Rs. 50,000 out of total debentures due to him and agree to accept 15% Debentures for the balance amount due.

(6) Land & Building to be revalued at Rs. 51,84,000, Machinery at Rs. 7,20,000, Computers at Rs. 4,00,000, Inventories at Rs. 3,50,000 and Trade receivables at 10% less to as they are appearing in Balance Sheet as above.

(7) Outstanding Expenses are fully paid in cash.

(8) Goodwill and Profit & Loss A/c will be written off and balance, if any, of Capital Reduction A/c will be adjusted against Capital Reserve.

You are required to pass necessary Journal Entries for all the above transactions and draft the company's Balance Sheet immediately after the reconstruction.

Solution :

Journal Entries in the books of Platinum Ltd.

	Particulars		Dr. Rs. '000	Cr. Rs. '000
	Bank A/c (1,00,000 x Rs. 10)	Dr.	10,00,000	
	To Equity share capital A/c			10,00,000
	(Being money on final call received)			
	Equity share capital (Rs. 50) A/c	Dr.	75,00,000	
	To Equity share capital (Rs. 40) A/c			60,00,000
	To Capital Reduction A/c			15,00,000
	(Being conversion of equity share capital of Rs. 50 each into Rs. 40 each as per reconstruction scheme)			
	Bank A/c	Dr.	12,50,000	

	Particulars		Dr.	Cr.
	To Equity Share Capital A/c (Being new shares allotted at Rs. 40 each)			12,50,000
	Trade payables A/c To Equity share capital A/c To Bank A/c (4,90,000 x 70%) To Capital Reduction A/c (Being payment made to trade payables in shares or cash to the extent of 70% as per reconstruction scheme)	Dr.	12,40,000	 7,50,000 3,43,000 1,47,000
	8% Debentures A/c 12% Debentures A/c To Shiv A/c (Being cancellation of 8% and 12% debentures of Shiv)	Dr. Dr.	3,00,000 4,00,000	 7,00,000
	Bank A/c To Shiv A/c (Being new debentures subscribed by Shiv)	Dr.	1,00,000	 1,00,000
	Shiv A/c To 15% Debentures A/c To Capital Reduction A/c (Being issuance of new 15% debentures and balance transferred to capital reduction account as per reconstruction scheme)	Dr.	8,00,000	 6,00,000 2,00,000
	8% Debentures A/c 12% Debentures A/c To Ganesh A/c (Being cancellation of 8% and 12% debentures of Ganesh)	Dr. Dr.	1,00,000 2,00,000	 3,00,000
	Ganesh A/c To 15% Debentures A/c To Capital Reduction A/c Being issuance of new 15% debentures and balance transferred to capital reduction account as per reconstruction scheme)	Dr.	3,00,000	 2,50,000 50,000
	Land and Building 51,84,000 – 42,70,000) Inventories To Capital Reduction A/c Being value of assets appreciated)	Dr. Dr.	9,14,000 30,000	 9,44,000
	Outstanding expenses A/c To Bank A/c Being outstanding expenses paid in cash)	Dr.	10,60,000	 10,60,000
	Capital Reduction A/c To Machinery A/c	Dr.	33,41,000	 1,30,000

	To Computers A/c			1,20,000
	To Trade receivables A/c			1,09,000
	To Goodwill A/c			22,00,000
	To Profit and Loss A/c			7,82,000
	Being amount of Capital Reduction utilized in writing off P & L A/c (Dr.) balance, goodwill and downfall in value of other assets)			
	Capital Reserve A/c	Dr.	5,00,000	
	To Capital Reduction A/c			5,00,000
	Being debit balance of capital reduction account adjusted against capital reserve)			

Balance Sheet (as reduced) as on 31.3.2019

		Particulars	Notes	Rs.
		Equity and Liabilities		
1		**Shareholders' funds**		
	a	Share capital	1	80,00,000
2		**Non-current liabilities**		
	a	Long-term borrowings	2	8,50,000
		Total		**88,50,000**
		Assets		
1		**Non-current assets**		
	a	Property, Plant and Equipment		
		Tangible assets	3	63,04,000
2		**Current assets**		
	a	Inventories		3,50,000
	b	Trade receivables		9,81,000
	c	Cash and cash equivalents		12,15,000
		Total		**88,50,000**

Notes to accounts :

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

Working Notes :

1. Cash at Bank Account

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

Question 4 : Nov – 2019 – Paper

Following is the summarized Balance Sheet of Fortunate Ltd. as on 31st March, 2019.

Particulars	Amount (Rs.)
Liabilities	
Authorized and Issued Share Capital	
(a) 15,000 8% Preference shares of Rs.50 each	7,50,000
(b) 18,750 Equity shares of Rs.50 each	9,37,500
Profit and Loss Account	5,63,750)
Loan	7,16,250
Trade Payables	2,58,750
Other Liabilities	43,750
Total	**21,42,500**
Assets	
Building at cost less depreciation	5,00,000
Plant at cost less depreciation	3,35,000
Trademarks and goodwill at cost	3,97,500
Inventory	5,00,000
Trade Receivables	4,10,000
Total	**21,42,500**

(Note: Preference shares dividend is in arrear for last five years).

The Company is running with the shortage of working capital and not earnings profits. A scheme of reconstruction has been approved by both the classes of shareholders. The summarized scheme of reconstruction is as follows:

(i) The equity shareholders have agreed that their Rs. 50 shares should be reduced to Rs. 5 by cancellation of Rs. 45.00 per share. They have also agreed to subscribe for three new equity shares of Rs. 5.00 each for each equity share held.

(ii) The preference shareholders have agreed to forego the arrears of dividends and to accept for each Rs. 50 preference share, 4 new 6% preference shares of Rs. 10 each, plus 3 new equity shares of Rs. 5.00 each, all credited as fully paid.

(iii) Lenders to the company for Rs. 1,87,500 have agreed to convert their loan into shares and for this purpose they will be allotted 15,000 new preference shares of Rs. 10 each and 7,500 new equity shares of Rs. 5.00 each.

(iv) The directors have agreed to subscribe in cash for 25,000 new equity shares of Rs. 5.00 each in addition to any shares to be subscribed by them under (i) above.

(v) Of the cash received by the issue of new shares, Rs. 2,50,000 is to be used to reduce the loan due by the company.

(vi) The equity share capital cancelled is to be applied:

(a) To write off the debit balance in the Profit and Loss A/c, and

(b) To write off Rs. 43,750 from the value of plant.

Any balance remaining is to be used to write down the value of trademarks and goodwill. The nominal capital, as reduced, is to be increased to Rs. 8,12,500 for preference share capital and Rs. 9,37,500 for equity share capital.

You are required to pass journal entries to show the effect of above scheme and prepare the Balance Sheet of the Company after reconstruction.

Solution :

In the books of Fortunate Ltd.

Journal Entries

	Particulars		**Dr. Rs.**	**Cr. Rs.**
1	Equity share capital A/c (Rs. 50)	Dr.	9,37,500	
	To Equity share capital A/c (Rs. 5)			93,750
	To Capital reduction A/c*			8,43,750
	(Being equity capital reduced to nominal value of 5 each)			
2	Bank A/c	Dr.	2,81,250	
	To Equity share capital			2,81,250
	(Being 3 right shares against each share was issued and subscribed)			
3	8% Preference share capital A/c (Rs. 50)	Dr.	7,50,000	
	Capital reduction A/c	Dr.	75,000	
	To 6% Preference share capital (Rs. 10)			6,00,000
	To equity share capital (Rs. 50)			2,25,000
	(Being 8% preference shares of Rs. 50 each converted to 6% preference shares of Rs. 10 each and also given to them 3 equity shares for every share held)			
4	Loan A/c	Dr.	1,87,500	
	To 6% Preference share capital A/c (15,000 x Rs. 10)			1,50,000
	To Equity share capital A/c (7,500 x Rs.5)			37,500
	(Being loan to the extent of Rs. 1,50,000 converted into share capital)			
5	Bank A/c (25,000 x Rs.5)	Dr.	1,25,000	
	To Equity share application A/c			1,25,000
	(Being shares subscribed by the directors)			
6	Equity share application A/c	Dr.	1,25,000	

	To Equity share capital A/c (Being application money transferred to capital A/c)		1,25,000
7	Loan A/c Dr. To Bank A/c (Being loan repaid)	2,50,000	2,50,000
8	Capital reduction A/c Dr. To Profit and loss A/c To Plant A/c To Trademarks and Goodwill A/c (Bal. fig.) (Being losses and assets written off to the extent required)	7,68,750	5,63,750 43,750 1,61,250

Balance sheet of Fortunate Ltd. (and reduced)
as on 31.3.2019

		Particulars	Notes	Rs.
		Equity and Liabilities		
1		**Shareholders' funds**		
	a	Share capital	1	15,12,500
2		**Non-current liabilities**		
	a	Long-term borrowings (7,16,250 – 1,87,500 – 2,50,000)		2,78,750
3		**Current liabilities**		
	a	Trade Payables		2,58,750
	b	Other current liabilities		43,750
		Total		**20,93,750**
		Assets		
1		**Non-current assets**		
	a	Property, Plant and Equipment	2	7,91,250
	b	Intangible assets	3	2,36,250
2		**Current assets**		
	a	Inventories		5,00,000
	b	Trade receivables		4,10,000
	c	Cash and cash equivalents	4	1,56,250
		Total		**20,93,750**

Notes to accounts :

			Rs.
1	**Share Capital**		
	Authorized capital:		
	81,250 Preference shares of Rs. 10 each	8,12,500	
	1,87,500 Equity shares of Rs. 5 each	9,37,500	17,50,000
	Issued, subscribed and paid up:		

	1,52,500 equity shares of Rs. 5 each	7,62,500	
	75,000, 6% Preference shares of Rs. 10	7,50,000	15,12,500
2	**Property, Plant and Equipment**		
	Building at cost less depreciation	5,00,000	
	Plant at cost less depreciation	2,91,250	7,91,250
3	**Intangible assets**		
	Trademarks and goodwill		2,36,250
4	**Cash and cash equivalents**		
	Bank (2,81,250+1,25,000-2,50,000)		1,56,250

Note : *In place of Capital Reduction Account, Reconstruction Account or Internal Reconstruction Account may also be used.

Question 5 : May – 2020 – RTP

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

		Particulars	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	1,25,000
		Total	**24,90,000**
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
			24,90,000

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

(i) Paid up value of 7% Preference Share to be reduced to Rs.80, but the rate of dividend being raised to 9%.
(ii) Paid up value of Equity Shares to be reduced to Rs.10.
(iii) The directors to refund Rs.50,000 of the fees previously received by them.
(iv) Debenture holders forego their interest of Rs.26,000 which is included among the trade payables.
(v) The preference shareholders agreed to waive their claims for preference share dividend, which is in arrears for the last three years.
(vi) "B" 6% Debenture holders agreed to take over the Chennai Works at 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.
(vii) The Chennai Worksmen'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.
(viii) 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.
(ix) Chennai works completely written off.
(x) 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.	9,00,000	
		To 9% Preference share capital (Rs. 80)			7,20,000
		To Capital reduction A/c			1,80,000
		(Being preference shares reduced to Rs. 80 and also rate of dividend raised from 7% to 9%)			
(ii)		Equity share capital A/c (Rs. 100 each)	Dr.	10,00,000	
		To Equity share capital A/c (Rs. 10 each)			1,00,000
		To Capital reduction A/c			9,00,000
		(Being reduction of nominal value of one share of Rs. 100 each to Rs. 10 each)			
(iii)		Bank A/c	Dr.	50,000	

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

Question 6 : Nov – 2020 – RTP

The following information pertains to Z Limited as on 31st March, 2019:

	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	(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:	
(a)Property, Plant and Equipment:	
Land & Buildings	30,00,000
Plant & Machinery	12,50,000
Furniture & Fixtures	2,50,000
(b) 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 pass journal entries for all the above-mentioned transactions including amounts of Goodwill, Patents, Loss in Profit and Loss account to be written off. Also prepare Bank Account and Reconstruction A/c.

Solution :

Journal Entries in books of Z Ltd.

	Particulars		**Dr. Rs.**	**Cr. Rs.**
(i)	Equity Share Capital (Rs. 10 each) A/c	Dr.	50,00,000	
	To Equity Share Capital (Rs. 5 each) A/c			25,00,000
	To Reconstruction A/c			25,00,000
	(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.)			
(ii)	9% Preference Share Capital (Rs. 100 each) A/c	Dr.	20,00,000	
	To 10% Preference Share Capital (Rs. 50 each) A/c			10,00,000
	To Reconstruction A/c			10,00,000
	(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.)			
(iii)	10% Secured Debentures A/c	Dr.	9,60,000	
	Trade payables A/c	Dr.	1,00,000	
	Interest on Debentures Outstanding A/c	Dr.	96,000	
	Bank A/c	Dr.	1,00,000	

	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 outstanding 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 12,000 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	
	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	1,00,000
To Reconstruction(Z)	60,000	By Reconstruction A/c (capital commitment penalty paid)	15,000
To Reconstruction A/c (refund of earlier fees by directors)	1,00,000	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		**2,60,000**

Reconstruction Account

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

To Capital Reserve (bal. fig.)	7,75,000		
	50,15,000		**50,15,000**

Question 7 : May – 2021 – RTP

Recover Ltd decided to reorganize its capital structure owing to accumulated losses and adverse market condition. The Balance Sheet of the company as on 31st March 2020 is as follows-

		Particulars	Notes	Rs.
		Equity and Liabilities		
1		**Shareholders' funds**		
	A	Share capital	1	3,50,000
	B	Reserves and surplus	2	(70,000)
2		**Non-current liabilities**		
	A	Long-term borrowings	3	55,000
3		**Current liabilities**		
	A	Trade Payables		80,000
	B	Short term Borrowings – Bank overdraft		90,000
				5,05,000
		Assets		
1		**Non-current assets**		
	A	Property, Plant Equipment	4	3,35,000
	B	Intangible assets	5	50,000
	C	Non-current investments	6	40,000
2		**Current assets**		
	A	Inventories		30,000
	B	Trade receivables		50,000
				5,05,000

Notes to accounts:

			Rs.
1	**Share Capital**		
	Equity share capital:		
	20,000 Equity Shares of Rs. 10 each		2,00,000
	Preference share capital:		
	15,000 8% Cumulative Preference Shares of Rs. 10 each (preference dividend has been in arrears for 4 years)		1,50,000
			3,50,000
2	**Reserves and surplus**		
	Securities premium		10,000
	Profit and loss account (debit balance)		(80,000)
			(70,000)
3	**Long-term borrowings**		
	<u>Secured</u>		

	9% Debentures (secured on the freehold property		50,000
	Accrued interest on 9% debentures		5,000
			55,000
4	**Property, Plant and Equipment**		
	Freehold property		1,20,000
	Leasehold property		85,000
	Plant and machinery		1,30,000
			3,35,000
5	**Intangible assets**		
	Goodwill		50,000
			50,000
6	**Non-current investments**		
	Non-Trade investments at cost		40,000
			40,000

Subsequent to approval by court of a scheme for the reduction of capital, the following steps were taken:

i. The preference shares were reduced to Rs. 2.5 per share, and the equity shares to Rs. 1 per share.

ii. One new equity share of Rs. 1 was issued for the arrears of preferred dividend for past 4 years.

iii. The balance on Securities Premium Account was utilized and was transferred to capital reduction account.

iv. The debenture holders took over the freehold property at an agreed figure of Rs. 75,000 and paid the balance to the company after deducting the amount due to them.

v. Plant and Machinery was written down to Rs. 1,00,000.

vi. Non-trade Investments were sold for Rs. 32,000.

vii. Goodwill and obsolete stock (included in the value of inventories) of Rs. 10,000 were written off.

viii. A contingent liability of which no provision had been made was settled at Rs. 7,000 and of this amount, Rs. 6,300 was recovered from the insurance.

You are required (a) to show the Journal Entries, necessary to record the above transactions in the company's books and (b) to prepare the Balance Sheet, after completion of the scheme.

Solution :

In the books of Recover Ltd

Journal entries

Particulars	**Dr. Rs.**	**Cr. Rs.**
8% Cumulative Preference share capital (Rs. 10) A/c Dr.	1,50,000	
To 8% Cumulative Preference share capital (Rs.2.5) A/c		37,500

Particulars		Dr.	Cr.
To Capital reduction (Rs. 7.5) A/c			1,12,500
(Preference shares being reduced to shares of Rs. 2.5 per share and remaining transferred to capital reduction account as per capital reduction scheme)			
Equity share capital A/c (Rs.10)	Dr.	2,00,000	
To Equity Share capital A/c (Rs. 1)			20,000
To Capital reduction A/c (Rs. 9)			1,80,000
(Equity shares reduced to Rs. 1 per share with the remaining amount transferred to capital reduction ac as a part of the internal reconstruction scheme.)			
Capital reduction A/c	Dr.	48,000	
To Equity share capital A/c			48,000
(Equity shares of Rs. 1 issued in lieu of the arrears of preference dividend for 4 years as a part of the internal reconstruction scheme)			
Securities Premium A/c	Dr.	10,000	
To Capital reduction A/c			10,000
(Amount from the securities premium utilized towards the capital reduction a/c as a part of the internal reconstruction scheme)			
9% Debentures A/c	Dr.	50,000	
Accrued interest on debentures A/c	Dr.	5,000	
Bank A/c	Dr.	20,000	
Capital reduction A/c	Dr.	45,000	
To Freehold property A/c			1,20,000
(Debenture holders being paid by the sale of property, which is sold at a loss debited to the capital reduction account. Amount received in excess being refunded to company by debenture holders as a part of the internal reconstruction scheme.)			
Capital reduction A/c	Dr.	90,000	
To Plant and Machinery Ac			30,000
To Goodwill A/c			50,000
To Inventory A/c			10,000
(The assets written off as a part of the internal reconstruction scheme)			
Bank A/c	Dr.	32,000	
Capital reduction A/c	Dr.	8,000	
To Investments A/c			40,000

Particulars		Dr. (Rs.)	Cr. (Rs.)
(Investments sold at a loss debited to capital reduction account as a part of the internal reconstruction scheme)			
Contingent Liability A/c	Dr.	7,000	
To Bank A/c			7,000
(Contingent liability paid as a part of the internal reconstruction scheme)			
Bank A/c	Dr.	6,300	
Capital reduction A/c	Dr.	700	
To Contingent Liability A/c			7,000
(The insurance company remitting part of the contingency payment amount)			
Capital reduction A/c	Dr.	80,000	
To Profit and loss A/c			80,000
(Accumulated losses written off to capital reduction account as a part of the internal reconstruction scheme).			
Capital reduction A/c	Dr.	30,800	
To Capital reserve A/c			30,800
(The balance in capital reduction account transferred to capital reserve as a part of the internal reconstruction scheme)			

Balance sheet of Recover Ltd. as at 31st March 2020 (and reduced)

		Particulars	Notes	Rs.
		Equity and Liabilities		
1		**Shareholders' funds**		
	A	Share capital	1	1,05,500
	B	Reserves and surplus	2	30,800
2		**Non-current liabilities**		
	A	Long-term borrowings		-
3		**Current liabilities**		
	A	Trade Payables		80,000
	B	Bank Overdraft		90,000
		Total		**3,06,300**
		Assets		
1		**Non-current assets**		
	A	Property, Plant and Equipment	3	1,85,000
2		**Current assets**		
	A	Inventories		20,000
	B	Trade receivables		50,000

	C	Cash and cash equivalents	4	51,300
		Total		**3,06,300**

Notes to accounts:

1	**Share Capital**	**Rs.**
	Equity share capital	
	68,000 Equity Shares of Rs. 1 each	68,000
	Preference share capital	
	15,000 8% Cumulative Preference Shares of Rs. 2.5 each	37,500
		1,05,500
2	**Reserves and surplus**	
	Capital reserve	30,800
3	**Property, Plant and Equipment**	
	Leasehold property	85,000
	Plant and machinery	1,00,000
		1,85,000
4	**Cash and cash equivalents**	
	Bank A/c (20,000+32,000-7000+6,300)	51,300

Question 8 : July – 2021 – Paper

Sapra Limited has laid down the following terms upon the sanction of the reconstruction scheme by the court.

(i) The shareholders to receive in lieu of their present holding at 7,50,000 shares of Rs.10 each, the following :

- New fully paid Rs.10 Equity Shares equal to 3/5th of their holding.
- Fully paid Rs.10.6% Preference Shares to the extent of 2/5th of the above new equity shares.
- 7% Debentures of Rs.2,50,000.

(ii) Goodwill which stood at Rs.2,70,000 is to be completely written off.

(iii) Plant and machinery to be reduced by Rs.1,00,000, Furniture to be reduced by Rs.88,000 and Building to be appreciated by Rs.1,50,000.

(iv) Investment of Rs.6,00,000 to be brought down to its existing market price of Rs.1,80,000.

(v) Write off Profit and Loss Account debit balance of Rs.2,25,000.

In case of any shortfall, the balance of General Reserve of Rs.42,000 can be utilized to write off the losses under reconstruction scheme.

You are required to show the necessary Journal Entries in the books of Spara Limited of the above reconstruction scheme considering that balance in General Reserve is utilized to write off the losses.

Solution :

Journal Entries

		Rs.	**Rs.**
Equity Share Capital (old) A/c	Dr.	75,00,000	
To Equity Share Capital (` 10) A/c			45,00,000
To 6% Preference Share Capital (` 10) A/c			18,00,000
To 7% Debentures A/c			2,50,000
To Capital Reduction A/c			9,50,000
(Being new equity shares, 6% Preference Shares, 7% Debentures issued and the balance transferred to Reconstruction account as per the Scheme)			
Building A/c	Dr.	1,50,000	
Capital Reduction A/c	Dr.	9,53,000	
To Goodwill Account			2,70,000
To Plant and Machinery Account			1,00,000
To Furniture Account			88,000
To Investment A/c			4,20,000
To Profit & Loss A/c			2,25,000
(Being Capital Reduction Account utilized for writing off of Goodwill, Plant and Machinery, furniture, investment and Profit & Loss as per the scheme)			
General reserve A/c	Dr.	3,000	
To Capital Reduction A/c			3,000
(Being general reserve utilized to write off the balance in Capital reduction A/c)			

Note: In place of Capital Reduction Account, Reconstruction Account or Internal Reconstruction Account may also be used in the above journal entries.

Question 9 : Nov – 2021 – RTP

Shine Ltd. provides the following information as on 31st March, 2021:

(Rs. in '000)

	Amount
Equity Shares of Rs. 10 each	35,000
8%, Cumulative Preference Shares of Rs. 100 each	17,500
6% Debentures of Rs. 100 each	14,000
Sundry Creditors	17,500
Provision for taxation	350
Property, Plant and Equipment	43,750
Investments (Market value Rs. 3325 thousand)	3,500
Current Assets (Including Bank Balance)	35,000
Profit and Loss Account (Dr. balance)	2,100

The following Scheme of Internal Reconstruction is approved and put into effect on 31st March, 2021.

(i) All the existing equity shares are reduced to Rs. 4 each.

(ii) All preference shares are reduced to Rs. 60 each.

(iii) The rate of interest on debentures is increased to 9%. The Debenture holders surrender their existing debentures of Rs. 100 each and exchange them for fresh debentures of Rs. 80 each. Each old debenture is exchanged for one new debenture.

(iv) Investments are to be brought to their market value.

(v) The Taxation Liability is settled at Rs. 5,25,000 out of current Assets.

(vi) The balance of Profit and Loss Account to be written off and balance of Current Assets left after settlement of taxation liability are revalued at Rs.1,57,50,000.

(vii) One of the creditors of the Company for Rs. 70,00,000 gives up 50% of his claim. He is allotted 8,75,000 equity shares of Rs. 4 each in full and final settlement of his claim.

(viii) Property, plant and equipment to be written down to 80%.

You are required to give journal entries for the above transactions and prepare capital reduction account.

Solution :

Journal Entries in the books of Shine Ltd.

			Rs.' 000	**Rs.' 000**
(i)	Equity share capital (Rs. 10) A/c	Dr.	35,000	
	To Equity Share Capital (Rs. 4) A/c			14,000
	To Capital Reduction A/c			21,000
	(Being conversion of equity share capital of Rs. 10 each into Rs. 4 each as per reconstruction scheme)			
(ii)	8% Cumulative Preference Share capital (Rs. 100) A/c	Dr.	17,500	
	To 8% Cumulative Preference Share Capital (Rs. 60) A/c			10,500
	To Capital Reduction A/c			7,000
	(Being conversion of 6% cumulative preference shares capital of Rs. 100 each into Rs. 60 each as per reconstruction scheme)			
(iii)	6% Debentures (Rs. 100) A/c	Dr.	14,000	
	To 9% Debentures (Rs. 80) A/c			11,200
	To Capital Reduction A/c			2,800
	(Being 9% debentures of Rs. 80 each issued to existing 6% debenture holders. The balance transferred to capital reduction account as per reconstruction scheme)			
(iv)	Sundry Creditors A/c	Dr.	7,000	
	To Equity Share Capital (Rs. 4) A/c			3,500
	To Capital Reduction A/c			3,500
	(Being a creditor of Rs. 70,00,000 agreed to surrender his claim by 50% and was allotted 8,75,000 equity shares of			

	Rs. 4 each in full settlement of his dues as per reconstruction scheme)			
(v)	Provision for Taxation A/c	Dr.	350	
	Capital Reduction A/c	Dr.	175	
	To Liability for Taxation A/c			525
	(Being conversion of the provision for taxation into liability for taxation for settlement of the amount due)			
(vi)	Liability for Taxation A/c	Dr.	525	
	To Current Assets (Bank A/c)			525
	(Being the payment of tax liability)			
(vii)	Capital Reduction A/c	Dr.	34,125	
	To P & L A/c			2,100
	To PPE A/c			8,750
	To Current Assets A/c			18,725
	To Investments A/c			175
	To Capital Reserve A/c (Bal. fig.)			4,375
	(Being amount of Capital Reduction utilized in writing off P & L A/c (Dr.) Balance, Fixed Assets, Current Assets, Investments and the Balance transferred to Capital Reserve)			

Capital Reduction Account

	Rs.		Rs.
To Liability for taxation A/c	175	By Equity share capital	21,000
To P & L A/c	2,100	By 8% Cumulative preferences Share capital	7,000
To Fixed Assets	8,750	By 6% Debentures	2,800
To Current assets	18,725	By Sundry creditors	3,500
To Investment	175		
To Capital Reserve (Bal. fig.)	4,375		
	34,300		**34,300**

Question 10 : May – 2022 – RTP

Z Limited provides the following information as on 31st March, 2021:

Particulars	Amount in Rs.
<u>Share Capital:</u>	
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
<u>Reserves and Surplus:</u>	
Profit and Loss Account (Dr. balance)	14,60,000
<u>Non-Current Liabilities:</u>	
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 pass journal entries for all the above-mentioned transactions including amounts to be written off for Goodwill, Patents and Loss in Profit and Loss account. Also prepare Bank Account and Reconstruction A/c.

Solution :

Journal Entries in the Books of Z Ltd.

			Rs.	Rs.
(i)	Equity Share Capital (Rs. 10 each) A/c	Dr.	50,00,000	
	To Equity Share Capital (Rs. 5 each) A/c			25,00,000
	To Reconstruction A/c			25,00,000
	(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.)			
(ii)	9% Preference Share Capital (Rs. 100 each) A/c	Dr.	20,00,000	
	To 10% Preference Share Capital (Rs. 50 each) A/c			10,00,000
	To Reconstruction A/c			10,00,000
	(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.)			
(iii)	10% Secured Debentures A/c	Dr.	9,60,000	
	Trade payables A/c	Dr.	1,00,000	
	Interest on Debentures payable A/c	Dr.	96,000	
	Bank A/c	Dr.	1,00,000	
	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.)			

			Dr. (Rs.)	Cr. (Rs.)
(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	
	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.)		

Reconstruction Account

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

Question 11 : Nov – 2022 – RTP

Planet Limited has decided to reconstruct the Balance Sheet since it has accumulated huge losses. The following is the balance sheet of the company as on 31st March, 2022 before reconstruction:

Particulars	Note No.	Amount (Rs. In lakh)
Equity & Liabilities		
Shareholders' Funds		
Share Capital	1	2,100
Reserves & Surplus	2	(783)
Non-Current Liabilities		
Long term Borrowings	3	1,050
Current Liabilities		
Trade Payables	4	153
Other Liabilities	5	36
Total		2,556
Assets		
Non-Current Assets:		
PPE	6	1,125
Current Investments	7	300
Inventories	8	450
Trade Receivables	9	675
Cash & Cash Equivalents	10	6

Total			2,556

Notes to Accounts:

		Rs. In lakh
(1)	Share capital	
	Authorised:	
	300 lakh Equity shares of Rs. 10 each	3,000
	12 lakh, 8% preference Shares of Rs. 100 each	1,200
		4,200
	Issued, Subscribed and Paid up:	
	150 Lakh Equity Shares of Rs. 10 each, fully paid up	1,500
	6 lakh 8% Preference Shares of Rs. 100 each, fully paid up	600
		2,100
(2)	Reserves and Surplus	
	Debit balance of Profit & Loss A/c	(783)
(3)	Long term borrowings	
	6% Debentures (Secured by freehold property)	600
	Director's Loan	450
		1,050
(4)	Trade payables	
	Trade payables for Goods	153
(5)	Other Liabilities	
	Interest Accrued and Due on 6% Debentures	36
(6)	PPE	
	Freehold Property	825
	Plant & machinery	300
		1,125
(7)	Current Investment	
	Investment in Equity Instruments	300
(8)	Inventories	
	Finished Goods	450
(9)	Trade Receivables	
	Trade receivables for Goods	675
(10)	Cash and Cash equivalents	
	Balance with bank	6

The Board of Directors of the company decided upon the following scheme of reconstruction with the consent of respective shareholders:

(1) Preference Shares are to be written down to Rs. 75 each and Equity Shares to Rs. 2 each.

(2) Preference Shares Dividend in arrears for 3 years to be waived by 2/3rd and for balance 1/3rd, Equity Shares of Rs. 2 each to be allotted.

(3) Debenture holders agreed to take one Freehold Property at its book value of Rs. 450 lakh in part payment of their holding. Balance Debentures to remain as liability of the company.

(4) Interest accrued and due on Debentures to be paid in cash.
(5) Remaining Freehold Property to be valued at Rs. 550 lakh.
(6) All investments sold out for Rs. 425 lakh.
(7) 70% of Directors' loan to be waived and for the balance, Equity Shares of Rs. 2 each to be alloted.
(8) 40% of Trade receivables and 80% of Inventories to be written off.
(9) Company's contractual commitments amounting to Rs. 900 lakh have been settled by paying penalty of Rs. 72 lakhs.

You are required to:
(a) Pass Journal Entries for all the transactions related to internal reconstruction;
(b) Prepare Capital Reduction Account, Bank Account; and
(c) Prepare Notes to Accounts on Share Capital and PPE, immediately after the implementation of internal reconstruction.

Solution :

(a) Journal Entries related to internal reconstruction in the books of Planet Ltd.

	Particulars		Debit Rs.	Credit Rs.
i	8% Preference share capital A/c (Rs. 100 each)	Dr.	600	
	To 8% Preference share capital A/c (Rs. 75 each)			450
	To Capital reduction A/c			150
	(Being the preference shares of Rs. 100 each reduced to Rs. 75 each as per the approved scheme)			
ii	Equity share capital A/c (Rs. 10 each)	Dr.	1,500	
	To Equity share capital A/c (Rs. 2 each)			300
	To Capital reduction A/c			1,200
	(Being the equity shares of Rs. 10 each reduced to Rs. 2 each)			
iii	Capital reduction A/c	Dr.	48	
	To Equity share capital A/c (Rs. 2 each)			48
	(Being 1/3rd of arrears of preference share dividend of three years to be satisfied by issue of 24 lakh equity shares of each)			
iv	6% Debentures A/c	Dr.	450	
	To Freehold property A/c			450
	(Being claim settled in part by transfer of freehold property)			
v	Accrued debenture interest A/c	Dr.	36	
	To Bank A/c			36
	(Being accrued debenture interest paid)			

vi	Freehold property A/c	Dr.	175	
	To Capital reduction A/c		175	
	(Being appreciation (550-375) in the value of freehold property)			
vii	Bank A/c	Dr.	425	
	To Investment A/c			300
	To Capital reduction A/c			125
	(Being investment sold on profit)			
viii	Director's loan A/c	Dr.	450	
	To Equity share capital A/c (Rs. 2 each)			135
	To Capital reduction A/c			315
	(Being director's loan waived by 70% and balance being discharged by issue of 67.5 lakh equity shares of Rs. 2 each)			
ix	Capital Reduction A/c	Dr.	1,485	
	To Profit and loss A/c			783
	To Trade receivables A/c (675 x 40%)			270
	To Inventories-in-trade A/c (450 x 80%)			360
	To Bank A/c			72
	(Being various assets, penalty on cancellation of contract, profit and loss account debit balance written off through capital reduction account)			
x	Capital Reduction A/c	Dr.	432	
	To Capital reserve A/c			432
	(Being balance transferred to capital reserve account as per the scheme)			

(b) **Capital Reduction Account** **(Rs.in lakhs)**

	Rs.		Rs.
To Equity Share Capital	48	By 8% Pref. Share Capital	150
To P & L A/c	783	By Equity Share Capital	1,200
To Trade Receivables	270	By Freehold property	175
To Inventories	360	By Bank (profit on sale of investment)	125
To Bank	72	By Director's loan	315
To Capital Reserve	432		
	1,965		**1,965**

Bank Account **(Rs.in lakhs)**

	Rs.		Rs.
To Balance b/d	6	By Accrued debenture interest	36

To Investments	300	By Capital Reduction Account (Penalty on cancellation of contract)	72
To Capital reduction	125	By Balance c/d	323
	431		**431**

(c) **Note to Accounts on Share Capital and PPE after implementation of internal reconstruction**

Share Capital		(Rs. in lakhs)
Authorised:		
300 lakh shares of Rs. 2 each		600
12 lakh, 8% Preference shares of Rs. 75 each		900
		1,500
Issued, subscribed and paid up:		
241.5 lakh Equity shares of Rs. 2 each		483
(out of which 91.5 lakh shares have been issued for consideration other than cash)		
6 lakh, 8% Preference shares of Rs.75 each fully paid up		450
Total		933
PPE		
Freehold property	825	
Less: Utilised to pay Debenture holders	(450)	
Add: Appreciation	175	550
Plant and machinery		300
Total		850

Working Note:

Calculation of number of equity shares issued

To equity shareholders	150 Lakh
To Preference shareholders (in lieu of arrear of preference dividend)	24 Lakh
To Directors	67.5 Lakh
	241.5 Lakh

Question 12 : Nov – 2022 – Paper

The following is the Balance Sheet of Purple Limited as at 31st March, 2022 :

Balance Sheet of Purple Limited as at 31st March, 2022

	Particulars	Notes	Amount in Rs.
I.	**Equity and Liabilities**		
	(1) Shareholder's Funds		
	(a) Share Capital	1	15,00,000
	(b) Reserves & Surplus	2	(3,00,000)

	(2) Current Liabilities		
	(a) Trade Payables		2,20,000
	(b) Short Term Borrowings - Bank Overdraft		2,00,000
	Total		**16,20,000**
II.	**Assets**		
	(1) Non-Current Assets		
	(a) Property, Plant and Equipment	3	10,20,000
	(b) Intangible Assets	4	1,20,600
	(2) Current Assets		
	(a) Inventories		1,70,000
	(b) Trade Receivables		3,01,800
	(c) Cash and cash equivalents		7,600
	Total		**16,20,000**

Note to Accounts

		Rs.	**Rs.**
(1)	**Share Capital**		
	90,000 Equity Shares of Rs.10 each fully paid	9,00,000	
	6% Preference Share Capital	6,00,000	15,00,000
(2)	**Reserves & Surplus**		
	Profit & Loss account		-3,00,000
(3)	**Property, Plant and Equipment**		
	Land and Building	5,40,000	
	Plant and Machinery	4,80,000	10,20,000
(4)	**Intangible Assets**		
	Goodwill	84,600	
	Patents	36,000	1,20,600

Dividends on preference shares are in arrears for 3 years.

On the above date, the company adopted the following scheme of reconstruction:

(i) The preference shares are converted from 6% to 8% but revalued in a manner in which the total return on them remains unaffected.

(ii) The value of equity shares is brought down to Rs.8 per share.

(iii) The arrears of dividend on preference shares are cancelled.

(iv) The debit balance of Goodwill account is written off entirely.

(v) Land and Building and Plant and Machinery are revalued at 85% and 80% of their respective book values.

(vi) Book debts amounting to Rs.14,400 are to be treated as bad and hence to be written off.

(vii) The company expects to earn a profit at the rate of Rs.90,000 per annum from the current year which would be utilized entirely for reducing the debit balance of Profit and loss

accounts for 3 years. The remaining balance of the said account would be written off at the time of capital reduction process.

(viii) The balance of total capital reduction is to be utilized in writing down Patents.

(ix) A secured loan of Rs.4,80,000 bearing interest at 12% per annum is to be obtained by mortgaging tangible fixed assets for repayment of bank overdraft and for providing additional funds for working capital.

You are required to give journal entries incorporating the above scheme of reconstruction, capital reduction account and prepare the reconstructed Balance Sheet.

Thanks ....

CHAPTER 19

LIQUIDATION OF COMPANY

Question 1 : May – 2018 – Paper

In a liquidation which commenced on 11th November, 2017 certain creditors could not receive payments out of the realization of assets and out of the contributions from "A" list contributories. The following are the details of certain transfer, which took place in 2016 and 2017:

Share holders	Number of shares transferred at the date of ceasing to be member	Date of ceasing to be member	Creditors remaining unpaid and outstanding Rs.
C	2,500	1st September, 2016	5,000
P	1,500	1st January, 2017	9,000
D	2,000	1st April, 2017	12,000
B	700	1st August, 2017	13,500
S	300	15th September, 2017	14,500

All the shares were Rs.10 each, Rs.5 paid up.

Ignoring expenses of and remuneration to liquidators show the amount to be realised from various persons listed above.

Solution :

Statement of Liabilities of B list contributors (showing the amount realized)

	Creditors Outstanding on the date of ceasing to be member	P 1,500 Shares Rs.	D 2,000 Shares Rs.	B 700 Shares Rs.	S 300 Shares Rs.	Amount to be paid to the Creditors Rs.
(1)	9,000	3,000	4,000	1,400	600	9,000
(2)	3,000	-	2,000	700	300	3,000
(3)	1,500	-	-	1,050	450	1,500
(4)	1,000	-	-	-	1,000	150
	Total (a)	3,000	6,000	3,150	2,350	
(b)	maximum liability on shares held	7,500	10,000	3,500	1,500	
(c)	Amount to be realized (a) or (b) whichever is lower	3,000	6,000	3,150	1,500	

Working Notes:

1. C will not be liable since he transferred his shares prior to one year preceding the date of winding up.
2. P will not be responsible for further debts incurred after 01.01.2017 (from the date when he ceases to be a member). Similarly, D & B will not be liable for the debts incurred after the date of their transfer of shares.
3. The increase between 1st August 2017 and 15th September 2017, is solely the responsibility of S. Liability of S has been restricted to the maximum allowable limit of Rs. 1,500. Therefore, amount payable by S on 15.09.2017 is Rs. 150 only.
4. Ratio of discharge of liability will be in the ratio of no. of shares held by B List Contributories which is as follows:

Calculation of Ratio for discharge of Liabilities :

Date	Cumulative liability Rs.	Increase in liabilities Rs.	Ratio of no. of shares held by L, M, N, O
01.01.2017	9,000	-	15:20:7:3
01.04.2017	12,000	3,000	20:07:03
01.08.2017	13,500	1,500	7:03
15.09.2017	14,500	1,000	Only S

Question 2 : Nov – 2018 – Paper

Virat Ltd. furnishes the following summarized Balance Sheet as at 31st March, 2018:

	Particulars	Rs.	Rs.
	<u>**Equity and Liabilities :**</u>		
1	**Shareholders Funds:**		
	Share Capital 10,000, 12% Pref. Shares of Rs.100 each fully paid up	10,00,000	
	1,00,000 Equity shares of Rs.10 each fully paid up	10,00,000	
	50,000 Equity shares of Rs. 10 each, Rs. 8 paid up	4,00,000	24,00,000
(b)	Reserve and Surplus		
	Profit & Loss A/c. (Dr. Balance)		(3,50,000)
2	**Non-current Liabilities:**		
	12% Debentures	15,00,000	
	Loan on Mortgage	4,50,000	19,50,000
3	**Current Liabilities:**		
	Bank Overdraft	2,75,000	
	Trade Payables	7,30,000	10,05,000
	Total		**50,05,000**
	<u>Assets:</u>		
1	**Non-current Assets:**		
	Fixed Assets - Land & Buildings		6,00,000
2	**Current Assets :** Sundry Current Assets		44,05,000
	Total		**50,05,000**

The mortgage loan was secured against the Land & Buildings. Debentures were secured by a floating charge on all the assets of the company. The debenture holders appointed a Receiver. The company being voluntarily wound up, a liquidator was also appointed. The Receiver was entrusted with the task of realising the Land & Buildings which fetched Rs.7,50,000 . Receiver also took charge of Sundry current assets of value Rs. 30,00,000 and sold them for Rs. 28,75,000. The Bank overdraft was secured by a personal guarantee of the directors who discharged their obligations in full from personal resources. The costs of the Receiver amounted to Rs. 10,000 and his remuneration Rs. 15,000.
The expenses of liquidator was Rs. 17,500 and his remuneration was decided at 2% on the value of the assets realised by him. The remaining assets were realised by liquidator for Rs. 12,50,000. Preference dividend was in arrear for 2 years. Articles of Association of the company provide for payment of preference dividend arrears in priority to return of equity capital.
Prepare the accounts to be submitted by the Receiver and the Liquidator.

Solution :

Receiver's Receipts and Payments Account

Particulars		Rs.	Particulars	Rs.
Sundry Assets realized		28,75,000	Costs of the Receiver	10,000
Surplus received from Mortgage			Remuneration to Receiver	15,000
			Debentures holders Principal*	15,00,000
Sale Proceeds of land and building	7,50,000		Surplus transferred to the Liquidator	16,50,000
Less: Applied to Discharge of mortgage loan	(4,50,000)	3,00,000		
		31,75,000		**31,75,000**

Note : * Assumed that interest on debentures has already been paid before winding up proceedings.

Liquidator's Final Statement of Account

Particulars	Rs.	Particulars	Rs.
Surplus received from Receiver	16,50,000	Cost of Liquidation (legal exp.)	17,500
Assets Realized	12,50,000	Remuneration to Liquidator (12,50,000 x 2%)	25,000
Calls on partly paid Shareholders:		Unsecured Creditors:	
		for Trade	7,30,000
		Directors for payment of Bank O/D	2,75,000
		Preferential Shareholders:	
		Capital	10,00,000
		Arrears of Preference Dividends	2,40,000
		Equity shareholders:	

		Return of money to contributors to holders	
		1,00,000 shares at Rs. 4.75	4,75,000
		50,000 shares at Rs. 2.75	1,37,500
	29,00,000		**29,00,000**

Working Note :

Amount to be paid or received from Equity shareholders	Rs.
Total Equity share capital paid up	14,00,000
Less: Surplus before call from Equity Shares (29,00,000 — 22,87,500)	(6,12,500)
Loss to be borne by 1,50,000 shares	7,87,500
Loss per share = (7,87,500/ 1,50,000 shares)	5.25
Hence, Refund to Equity shareholders of 1,00,000 shares of Rs. 10 fully paid up	4.75

Refund to Equity shareholders of 50,000 shares of Rs. 8 paid up 2.75

Question 3 : May – 2019 – RTP / Nov – 2020 – RTP

The following is the summarized Balance Sheet of Shah Ltd. Co. which is in the hands of the liquidator:

Balance Sheet as at 31.3.2017

Liabilities	Rs.	Assets	Rs.
Share Capital:		Fixed assets	2,00,000
1,000, 6% Preference Shares of Rs.100 each, fully paid	1,00,000	Inventory	1,20,000
2,000 Equity shares of Rs.100 each, fully paid	2,00,000	Book debts	2,40,000
2,000 Equity shares of Rs.100 each Rs.75 paid up	1,50,000	Cash in hand	40,000
Loan from bank (on security of stock)	1,00,000	Profit and loss A/c	3,00,000
Trade Payables	3,50,000		
	9,00,000		**9,00,000**

The assets realized the following amounts (after all costs of realization and liquidator's commission amounting to Rs.5,000 paid out of cash in hand).

	Rs.
Fixed assets	1,68,000
Inventory	1,10,000
Trade Receivables	2,30,000

Calls on partly paid shares were made but the amounts due on 200 shares were found to be irrecoverable.

You are required to prepare Liquidator's Final Statement of Receipts and Payments.

Solution :

Liquidator's Final Statement of Receipts and Payments A/c

	Rs.	Rs.		Rs.
To Cash in hand		40,000	By Liquidator's remuneration and expenses	5,000
To Assets realised:			By Trade Payables	3,50,000
Fixed assets	1,68,000		By Preference shareholders	1,00,000
Inventory			By Equity shareholders @ Rs. 10 on 2,000 shares	20,000
(1,10,000 – 1,00,000)	10,000			
Book debts	2,30,000	4,08,000		
To Cash - proceeds of call on 1,800 equity shares @ Rs. 15*		27,000		
		4,75,000		**4,75,000**

Working Note :

Return per equity share

	Rs.
Cash available before paying preference shareholders	
(Rs. 4,48,000 – Rs. 3,55,000)	93,000
Add: Notional calls 1,800 shares (2,000-200) × Rs. 25	45,000
	1,38,000
Less: Preference share capital	1,00,000)
Available for equity shareholders	38,000
Return per share = $\frac{Rs.38,000}{3,800(4,000-200)}$ = Rs.10	
and Loss per Equity Share Rs. (100-10) = Rs. 90	

Question 4 : May – 2019 – Paper

BT Ltd. went into Voluntary Liquidation on 31st March, 2018, when their detailed Balance Sheet was as follows:

Liabilities	**In Rs.**
Issued & Subscribed Capital	
10,000 12% cumulative preference shares of Rs.100 each, fully paid	10,00,000
10,000 Equity Shares of Rs.100 each 75 per share paid up	7,50,000
20,000 Equity Shares of Rs.100 each 60 per share paid up	12,00,000
Profit & Loss Account	(5,25,000)
12% Debentures (Secured by a floating charge)	10,00,000
Interest outstanding on Debentures	1,20,000
Creditors	8,50,000

	43,95,000
Assets	
Land & Building	17,60,000
Plant & Machinery	12,50,000
Furniture	4,75,000
Patents	1,45,000
Stock	1,80,000
Trade Receivables	5,09,300
Cash at Bank	75,700
	43,95,000

Preference dividends were in arrear for 1 year. Creditors include preferential creditors of Rs.75,000. Balance creditors are discharged subject to 5% discount.

Assets are realised as under:

	In Rs.
Land & Building	24,50,000
Plant & Machinery	9,00,000
Furniture	2,85,000
Patents	90,000
Stock 2,80,000	
Trade Receivables	3,15,000

– Expenses of liquidation amounted to Rs.45,000.
– The liquidator is entitled to a remuneration of 3% on all assets realised (except cash at bank).
– All payments were made on 30th June, 2018.

You are required to prepare the Liquidator's Final Statement of Account as on 30th June, 2018. Working Notes should form part of the answer.

Solution :

BT Limited

Liquidator's Statement of Account

Receipts		Rs.	Particulars		Rs.
To Assets realized:			By Liquidation expenses		45,000
Bank		75,700	By Preferential creditors		75,000
Other assets:			By Liquidator's Remuneration (W.N.1)		1,29,600
Land & building	24,50,000		By Debenture holders:		
Plant & Machinery	9,00,000		Debentures	10,00,000	
Furniture	2,85,000		Interest accrued	1,20,000	
Patents	90,000		Interest 1-4-18 to 30-6-18	30,000	11,50,000
Stock	2,80,000		By Unsecured creditors		7,36,250
Trade receivables	3,15,000	43,20,000	By Preferential shareholders		
			Preference capital	10,00,000	
			Arrear of Dividend	1,20,000	11,20,000

			By Equity shareholders -		32,55,850
			Rs. 32.995 on 20,000 shares		6,59,900
			Rs. 47.995 on 10,000 shares		4,79,950
		43,95,700			**43,95,700**

Working Notes:

(1) Liquidator's remuneration 43,20,000 × 3/100 = Rs. 1,29,600

(2) As the company is solvent, interest on the debentures will have to be paid for the period 1-4-2018 to 30-6-2018
10,00,000 x 12% x 3/12 = Rs. 30,000

(3) Total equity capital - paid up (7,50,000 +12,00,000) Rs. 19,50,000
Less : Balance available after payment to unsecured and preference shares
(43,95,700 — 32,55,850) Rs. (11,39,850)
Rs. 8,10,150

Loss to be born by 30,000 equity shares
Loss per share
Rs. 27.005
Hence, Refund for share on Rs. 60 paid share (60 - 27.005) Rs. 32.995
Refund for share on Rs. 75 paid (75 - 27.005) Rs. 47.995

Question 5 : Nov – 2019 – RTP

Given below is the Balance Sheet of OM Limited as on 31.3.2019:

Liabilities	Rs.	Assets	Rs.
Share Capital:		Fixed Assets:	
14%, 1,60,000 cumulative preference shares of Rs.100 each fully paid up	16,00,000	Land	1,60,000
32,000 equity shares of Rs.100 each, Rs.60 per share paid up	19,20,000	Buildings	6,40,000
Reserves and Surplus	NIL	Plant and Machinery	21,60,000
Secured Loans:		Patents	1,60,000
14% debentures	9,20,000	Investments	NIL
(Having a floating charge on all assets)		Current Assets:	
Interest accrued on above debentures	1,28,800	Inventory at cost	4,00,000
(Also having a floating charge as above)		Trade receivables	9,20,000
Loan on mortgage of land and building	6,00,000	Cash at bank	2,40,000
Unsecured Loan	NIL	Profit and Loss A/c	9,60,000
Current liabilities			
Trade payables	4,71,200		

	56,40,000		56,40,000

On 31.3.2019 the company went into voluntary liquidation. The dividend on 14% preference shares was in arrears for one year. Trade payables include preferential creditors amounting to Rs.1,20,000.

The assets realized the following sums:

Land Rs. 3,20,000; Buildings Rs. 8,00,000; Plant and machinery Rs. 20,00,000; Patent Rs. 2,00,000; Inventory Rs. 6,40,000; Trade receivables Rs. 8,00,000.

The expenses of liquidation amounted to Rs. 1,17,736. The liquidator is entitled to a commission of 2% on all assets realized (except cash at bank) and 2% on amounts among unsecured creditors other than preferential creditors. All payments were made on 30th June, 2019. Interest on mortgage loan shall be ignored at the time of payment.

Prepare the liquidator's final statement of account.

Solution :

OM Ltd.

Liquidator's Final Statement of Account

Receipts	**Value Realised**		**Payments Rs.**	**Payments Rs.**
Assets Realised:		Liquidator's Remuneration (W.N. 1)		1,02,224
Cash at Bank	2,40,000	Liquidation Expenses		1,17,736
Trade receivables	8,00,000	Debentureholders:		
Inventory	6,40,000	14% Debentures	9,20,000	
Plant and Machinery	20,00,000	Interest Accrued (W.N. 2)	1,61,000	10,81,000
Patent	2,00,000	Creditors:		
Surplus from Securities (W.N. 3)	5,20,000	Preferential	1,20,000	
		Unsecured	3,51,200	4,71,200
		Preference Shareholders:		
		Preference Share Capital	16,00,000	
		Arrears of Dividend	2,24,000	18,24,000
		Equity Shareholders (W.N.4)		
		Rs. 25.12 per share on 32,000 shares		8,03,840
	44,00,000			**44,00,000**

Working Notes :

		Rs.
1	Liquidator's remuneration:	
	2% on assets realised (2% of Rs.47,60,000)	95,200
	2% on payments to unsecured creditors (2% on Rs.3,51,200)	7,024

		1,02,224
2	Interest accrued on 14% Debentures:	
	Interest accrued as on 31.3.2019	1,28,800
	Interest accrued upto the date of payment i.e. 30.6.2019	32,200
		1,61,000
3	Surplus from Securities:	
	Amount realised from Land and Buildings (Rs.3,20,000 + Rs.8,00,000)	11,20,000
	Less: Mortgage Loan	(6,00,000)
		5,20,000
4	Amount payable to Equity Shareholders:	
	Equity share capital (paid up)	19,20,000
	Less: Amount available for equity shareholders	(8,03,840)
	Loss to be borne by equity shareholders	11,16,160
	Loss per equity share (Rs.11,16,160/32,000)	34.88
	Amount payable to equity shareholders for each equity share (60-34.88)	25.12

Question 6 : Nov – 2019 – Paper

A liquidator is entitled to receive remuneration at 5% of the assets realized and 8% of the amount distributed among the unsecured creditors. The assets realized Rs.13,75,000. Payment was made from realised amount as follows:

Liquidation expenses	13,000
Preferential creditors (treated as unsecured creditors)	88,500
Secured creditors	1,00,000

You are required to calculate remuneration payable to the liquidator.

Solution :

Calculation of Total Remuneration payable to Liquidator

		Amount in Rs.
5% on Assets realised	(13,75,000 x 5%)	68,750
8% on payment made to Unsecured creditors (Refer W.N)		7,080
Total Remuneration payable to Liquidator		75,830

Working Note:

Liquidator's remuneration on payment to unsecured creditors =

Cash available for unsecured creditors after all payments including liquidation expenses, payment to secured creditors and liquidator's remuneration

	Rs.	Rs.13,75,000
Total amount realized		
Less: Liquidation expenses paid	(13,000)	

Payment to secured creditors	(1,00,000)	
Liquidator's remuneration on assets realized	(68,750)	
		Rs.1,81,750
		Rs.11,93,250

Sufficient amount is available for preference creditors (treated as unsecured creditors) therefore Liquidator's remuneration on payment to unsecured creditors = 8% x Rs. 88,500 = Rs. 7,080

Note: Since the amount of unsecured creditors (other than preferential creditors) is not given in the question, the above solution is based on the assumption that there are no unsecured creditors (other than preferential creditors who are treated as unsecured creditors).

Question 7 : May – 2020 – RTP

Alpha Ltd. is under the process of liquidation. Liquidator is entitled to receive remuneration at 2% on the assets realized, 3% on the amount distributed to Preferential Creditors and 3% on the payment made to Unsecured Creditors. The assets were realized for Rs. 37,50,000 against which payment was made as follows:

Liquidation Expenses	Rs. 37,500
Secured Creditors	Rs. 15,00,000
Preferential Creditors	Rs. 1,12,500

The amount due to Unsecured Creditors was Rs. 22,50,000. You are asked to calculate the total Remuneration payable to Liquidator.

Calculation shall be made to the nearest multiple of a rupee.

Solution :

Calculation of Total Remuneration payable to Liquidator

		Amount in Rs.
2% on Assets realised	37,50,000 x 2%	75,000
3% on payment made to Preferential creditors	1,12,500 x 3%	3,375
3% on payment made to Unsecured creditors (Refer W.N)		58,882
Total Remuneration payable to Liquidator		1,37,257

Working Note:

Liquidator's remuneration on payment to unsecured creditors

Cash available for unsecured creditors after all payments including liquidation expenses, payment to secured creditors, preferential creditors & liquidator's remuneration

= Rs. 37,50,000 – Rs. 37,500 – Rs. 15,00,000 – Rs. 1,12,500 – Rs. 75,000 – Rs. 3,375 = Rs. 20,21,625.

Liquidator's remuneration

= 3/103 x Rs. 20,21,625= Rs. 58,882

Question 8 : Nov – 2020 – Paper / Jan – 2021 - Paper

In a winding up of a company creditors remain unpaid. The following person has transferred then holdings before winding up

Name	Date of Transfer	No of shares transferred	Amount due to creditors on the transfer (Rs.)
D	1st January 2019	1000	8500
E	15Th February 2019	400	13500
H	15Th March 2009	700	19000
J	31St March 2019	900	22000
K	5th April 2019	1000	31000

The Shares were of Rs. 100 each, Rs. 80 being called up and paid up on the date of transfers

1. A member G, who holds 200 shares died on 28th Feb 2019 when the amount due to creditors was Rs. 16000. His shares were transmitted to his Son X.
2. R was the transferee of shares held by J. R paid Rs. 20 per share as calls in advance immediately on becoming a member
3. The liquidation of the company commenced on 1st Feb 2020. When the liquidator made a call on the present and past contributories to pay the amount.

You are required to quantify the maximum liability of the transferors of shares mentioned in the above table.

Solution :

Statement of Liability as Contributories of Former Members

Date	Creditors outstanding	Amount paid to Creditors (Increase in Creditors)	No. of shares	E 400 shares	G/X 200 shares	H 700 shares	K 1,000 shares	Amount to be paid to Creditors
2019	Rs.	Rs.	Ratio	Rs.	Rs.	Rs.	Rs.	Rs.
15-Feb	13,500	13,500	4:2:7:10	2,348	1,174	4,108	5,870	13,500
28-Feb	16,000	2,500	2:7:10	—	263	921	1,316	2,500
15-Mar	19,000	3,000	2:7:10	—	316	1,105	1,579	3,000
5-Apr	31,000	12,000	2:10	—	2,000	—	10,000	12,000
	(a) Maximum amount payable to creditors			2,348	3,753	6,134	18,765	31,000
	(b) Maximum liability at Rs. 20 per share held			8,000	4,000	14,000	20,000	
	Lower of (a) and (b)			2,348	3,753	6,134	18,765	

Working Note:

(1) The transferors are D, E, H, J and K. When the transferees pay the amount due as "present" member contributories, there will not be any liability on the transferors. It is only when the transferees do not pay as "present" member contributories then the liability would arise in the case of "past" members as contributories.

(2) D will not be liable to pay any amount as the winding up proceedings commenced after one year from the date of the transfer.

(3) J also will not be liable as the transferee R has paid the balance Rs. 20 per share as call in advance.

(4) E, G/X, H and K will be liable, as former members, to the maximum extent as indicated, provided the transferees do not pay the calls.

(5) X to whom shares were transmitted on demise of his father G would be liable as an existing member contributory. He steps into the shoes of his deceased father under section 430. His maximum liability would be at Rs. 20 per share on 200 shares received on transmission i.e. for Rs. 4,000.

Question 9 : Nov – 2020 – Paper

Beekey Ltd is being wound up by the tribunal. All the assets of the company have been charged to the company's bankers to whom the company owes Rs. 2.50 crores. The company owns following amounts to others:

Dues to workers	Rs. 62,50,000
Taxes payable to Government	Rs. 15,00,000
Unsecured creditors	Rs. 30,00,000

You are required to compute with reference to the provision pf the companies Act 2013, the amount each kind of creditors is likely to get if the amount realized by the official liquidator from the secured asset and available for distribution amount creditors in only Rs. 2,00,00,000.

Solution :

Section 326 of the Companies Act, 2013 is talks about the overriding preferential payments to be made from the amount realized from the assets to be distributed to various kind of creditors. According to the proviso given in the section 326 the security of every secured creditor should be deemed to be subject to a pari passu change in favour of the workman to the extent of their portion.

$$\text{Workman's Share to Secured Asset} = \frac{\text{Amount Realized} \times \text{Workman's Dues}}{\text{Workman's Dues} + \text{Secured Loan}}$$

$$\text{Workman's Share to Secured Asset} = \frac{2{,}00{,}00{,}000 \times 62{,}50{,}000}{62{,}50{,}000 + 2{,}50{,}00{,}000}$$

$$= 2{,}00{,}00{,}000 \times 1/5$$

Workmen's share to Secured Assets = Rs.40,00,000

Amount available to secured creditor is Rs.200 Lakhs – 40 Lakhs = 160 Lakhs

Hence, no amount is available for payment of government dues and unsecured creditors.

Question 10 : May – 2021 – RTP

From the following Trial Balance of All Rounder Ltd., on 1st January, 2021, prepare liquidator's final statement of account:

Particulars	Debit (Rs.)	Credit (Rs.)
9% Preference Share Capital (2,500 Preference Shares at Rs.100 each, fully paid)		2,50,000
Equity Share Capital: 4,000 Equity Shares at Rs.100 each, fully paid.		4,00,000

4,000 Equity Shares at Rs.100 each, Rs.50 paid up		2,00,000
Plant	6,00,000	
Stock-in-Trade	7,20,000	
Sundry Debtors	1,70,000	
Sundry Creditors		4,42,000
Bank Balance	2,40,000	
Preliminary Expenses	12,000	
6% Mortgage Loan		4,60,000
Outstanding Liabilities for Expenses	-	50,000
Profit and Loss A/c (Trading Loss for the previous accounting year)	60,000	-
	18,02,000	**18,02,000**

Following points should be kept in mind:

1. On 21st January, 2021, the Liquidator sold plant for Rs.5,90,000 and stock-in-trade at 10% less than the Book Value. He realized 80% of Sundry Debtors, and incurred cost of collection of Rs.3,700 (remaining Debtors are to be treated as bad).
2. The Loan Mortgage was discharged as on 31st January, 2021, along with interest for 6 months. Creditors were discharged subject to 5% discount. Outstanding Expenses paid at 20% less.
3. Preference Share Dividend is due for one year and paid with final payment.
4. Liquidation Expenses incurred are Rs.3,600, and Liquidator's Remuneration is settled at 4% on disbursement to shareholders (preference and equity) excluding preference dividend, subject to minimum of Rs.20,000. Liquidator's Remuneration to be rounded off to the multiple of Rs.10.

Solution :

Liquidator's Final Statement of Account

Receipts		Rs.	Payments		Rs.
Sundry Assets realized:			Liquidator's Remuneration (Working note)		25,020
Bank Balance		2,40,000	Liquidation Expenses (given)		3,600
Plant		5,90,000	Secured Creditors:		
Debtors (1,70,000 X 80%)	1,36,000		6% Mortgage Loan	4,60,000	
Less: Realization Expenses	-3,700		Add: Interest (4,60,000 × 6% × 6/12)	13,800	4,73,800
Stock (7,20,000× 90%)			Unsecured Creditors:		
			Creditors (4,42,000 X 95%)	4,19,900	
			Outstanding Expenses	40,000	4,59,900

		Preference Shareholders:		
		Capital	2,50,000	
		Dividend	22,500	2,72,500
		(for 1 year @ 9%)		
		Equity Shareholders:		
		(Working note)		
		Fully Paid Shares	2,87,740	
		(4,000×71.935)		
		Partly Paid Shares	87,740	3,75,480
		(4,000×21.935)		
	16,10,300			**16,10,300**

Working Note:

Computation of Liquidations' Remuneration and Payment to Equity Shareholders

		Rs.
(a)	Total of Receipts (from above account)	16,10,300
(b)	Total Payments before Final Payment to Members (excluding Preference Capital) and Liquidator's Remuneration (3,600 + 4,73,800 + 4,59,900 + Pref Dividend 22,500)	(9,59,800)
(c)	Balance left for Liquidator's Remuneration, Pref. Capital and Equity Shareholders	6,50,500
(d)	Liquidator's Remuneration (6,50,500 × 4/104 = Rs.25,020 or Rs.20,000 whichever is higher)	(25,020)
(e)	Refund of Capital to Preference Shareholders	(2,50,000)
(f)	Balance money before Notional Call	3,75,480
(g)	Notional Call on 4,000 Partly Paid Shares at Rs.50 each (to make all Shares Rs.100 paid up)	2,00,000
(h)	Surplus Cash balance after Notional Call	5,75,480
(i)	Number of Equity Shares deemed fully paid (4,000 + 4,000)	8,000
(j)	Hence, Refund on every Rs.100 paid up Share (h ÷ i) = Rs.5,75,480 ÷ 8,000	Rs.71.935
(k)	Loss per Rs.100 paid up Equity Share = Paid Up Value Rs.100 – Refund as above Rs.71.935	28.065
(l)	Refund per Rs.50 Partly Paid-Up Equity Share = Paid Up Value Rs.50 – Loss as above Rs.28.065	21.935

Question 11 : July – 2021 – Paper

The different categories of shareholders of Earth Limited, who went into liquidation on 1st April, 2021 are as follows :

(i) 32,000 Equity shares of Rs.100 each, Rs.80 paid up

(ii) 48,000 Equity shares of Rs.100 each, Rs.35 paid up

(iii) 12,80,000 Equity shares of Rs.10 each, Rs.7 paid up

You are required to distribute the surplus money among different categories of shareholders, if the surplus available with Liquidator after discharging all the liabilities is Rs.32,00,000.

Solution :

Particulars	I	II	III	Total (Rs.)
No. of shares	32,000	48,000	12,80,000	13,60,000
Equity share capital	32,00,000 (@Rs. 100)	48,00,000 (@Rs. 100)	128,00,000 (@Rs. 10)	208,00,000
Paid up share Capital (A)	25,60,000	16,80,000	89,60,000	132,00,000
Loss due to Liquidation (B) (Rs. 100,00,000 in 2:3:8)	(15,38,462)	23,07,692)	(61,53,846)	(100,00,000)
Surplus/ (deficiency) amount distributed among different categories of shareholders (A) – (B)	10,21,538	(6,27,692)	28,06,154	32,00,000

Loss due to Liquidation Rs. 100,00,000 will be distributed in ratio in 2:3:8

Note: Shareholders of category I and III will get surplus amount, while category II shareholders will pay Rs. 6,27,692.

Alternative Answer

Particulars	I	II	III
No. of shares (A)	32,000	48,000	12,80,000
Nominal value per share	Rs. 100	Rs. 100	Rs. 10
Paid up value per share (B)	80	35	7
Loss per share due to Liquidation (C)	48.08	48.08	4.808
Surplus/ Deficiency amount distributed among different categories of shareholders (A) x [(B) – (C)]	10,21,440	(6,27,840)	28,05,760

Calculation of loss per share

Total Paid up Share Capital = Rs. 1,32,00,000
Surplus = Rs. 32,00,000
Loss to Shareholders = Rs.1,00,00,000
No. Shares = 2,08,000 [32,000 + 48,000 + (12,80,000 x 10/100)]
Loss per Share = Rs. 48.08

Question 12 : Nov – 2021 – RTP

The position of Neha Ltd. on its liquidation is as under:

5,000, 10% Preference Shares of Rs. 100 each Rs. 60 paid up

2,000, Equity shares of Rs. 75 each, Rs. 50 paid up

Unsecured Creditors Rs. 99,000

Liquidation Expenses Rs. 1,000

Liquidator is entitled to a commission of 2% on the amount realized from calls made on contributories

You are required to prepare Liquidator's Final Statement of Account if the total assets realized Rs. 3,80,400.

Solution :

Liquidator's Final Statement of Account

Receipts	**Rs.**	**Payments**	**Rs.**
Receipts	3,80,400	Liquidation Expenses	1,000
Assets realized	20,000	Liquidator's Remuneration	400
Call on contributories: 2,000		Unsecured Creditors	99,000
Equity Shares @ Rs. 10 per share (W.N.)		Preference Shareholders	3,00,000
	4,00,400		**4,00,400**

Working Notes :

(i) Calculation of Shortage of funds	**Rs.**
Total Amount Available	3,80,400
Less: liquidation Expenses	(1,000)
Balance	3,79,400
Less: Unsecured Creditors	(99,000)
Balance	2,80,400
Less: Pref. Shareholders	(3,00,000)
Shortage of Funds	19,600

(ii) Calculation of funds required to meet shortage and commission payable on Calls to be made (to be called from equity shareholders)

Shortage of funds × $\frac{100}{100 - \text{Rate of Commission}}$ = Rs.19,600 × $\frac{100}{100-2}$

= $\frac{\text{Rs.}19{,}600 \times 100}{98}$ = Rs.20,000

(iii) Uncalled Capital @ Rs. 25 on 2,000 shares = Rs. 50,000

(iv) Amount of Calls to be made from equity shareholders (least of funds required and uncalled capital) i.e. Rs. 20,000 i.e. Rs. 10 per Share

(v) Commission on Call = Rs. 20,000 x 2/100 = Rs. 400

Question 13 : Dec – 2021 – Paper

A liquidator is entitled to receive remuneration at 3% on the assets realized and 4% on the payment made to creditors and company's bankers. The assets were realized for Rs.80,00,000. All the assets of the company have been charged to the company's bankers to whom the company owes Rs.1,00,00,000. The company owes following amounts to others :

Due to workers	Rs.25,00,000
Other Preferential creditors	Rs.20,00,000
Unsecured creditors	Rs.10,50,000

With reference to the provision of the Companies Act 2013, you are required to calculate the amount payable to :

1. Workers
2. Other Preferential creditors
3. Unsecured creditors

4. Liquidator for remuneration and
5. Company's banker's

Solution :

Section 326 of the Companies Act, 2013 is talks about the overriding preferential payments to be made from the amount realized from the assets to be distributed to various kind of creditors. According to the proviso given in the section 326 the security of every secured creditor should be deemed to be subject to a pari-passu charge in favour of the workman to the extent of their portion.

Workman's Share to Secured Asset = $\frac{\text{Amount Realized*} \times \text{Workman's Dues}}{\text{Workman's Dues} + \text{Secured Loan}}$

Workmen share to secured assets = Rs. 80,00,000 x (25,00,000/125,00,000) = Rs. 80,00,000 x 1/5 i.e. Rs. 16,00,000

Amount available to secured creditor is Rs. 80,00,000 – Rs. 16,00,000 = Rs. 64,00,000

Amount payable to workers Rs. 16,00,000. Amount payable to Company's bankers = Rs. 64,00,000.

Hence, no amount is available for payment of other preferential creditors and unsecured creditors.

Calculation of Total Remuneration payable to Liquidator

		Amount in Rs.
3% on Assets realized	(80,00,000 x 3%)	2,40,000
4% on payment made to company's Banker (Refer W.N)		2,36,923
Total Remuneration payable to Liquidator		4,76,923

Working Note:

Liquidator's remuneration on payment to Company's banker:

Cash available after liquidator remuneration on assets realized

= Rs. 80,00,000 – Rs. 16,00,000 - 2,40,000= Rs. 61,60,000 X4/104= Rs. 2,36,923

Thus,

1. Amount payable to workers Rs. 16,00,000.
2. No amount is available for payment of other preferential creditors
3. No amount is available for payment of unsecured creditors.
4. Liquidator for remuneration Rs. 4,76,923
5. Amount payable to Company's bankers = Rs. 59,23,077 (Rs. 61,60,000 less Rs. 2,36,923).

Note: The answer given above assumes that the workers are given the full amount due towards them without any deduction for Liquidators' remuneration and amount realized from sale of asset has been considered before Liquidator's remuneration. Accordingly, liquidator's remuneration has been considered for payment to banker only in the given answer. Hence, 4% remuneration has not been provided on the payment to workers as the question states that the liquidator is entitled to receive remuneration at 4% on payment made to banker and creditors. Moreover, workers are not considered as creditors in the given answer.

Alternative answer is possible when Liquidators' remuneration for asset realization is considered for payment to Workmen. In this case, two alternative answers will be possible which can be given as follows:

Alternative 1 -If Workmen are not treated as creditors for the purpose of Liquidator's remuneration (as the question states that the liquidator is entitled to receive remuneration at 4% on payment made to banker and creditors)

Workman's Share to Secured Asset = $\frac{\text{Amount Realized}^* \times \text{Workman's Dues}}{\text{Workman's Dues} + \text{Secured Loan}}$

Workmen share to secured assets = Rs. 80,00,000 x (25,00,000/125,00,000) = Rs. 80,00,000x1/5 i.e. Rs. 16,00,000

Banker's share to secured assets is Rs. 80,00,000 – 16,00,000 = 64,00,000

Thus the ratio of workmen share and bankers share is 1:4. (64,00,000/16,00,000)

Calculation of Total Remuneration payable to Liquidator

		Amount in Rs.
3% on Assets realized	(80,00,000 x 3%)	2,40,000
4% on payment made to company's Banker (Refer W.N)		2,38,769
Total Remuneration payable to Liquidator		4,78,769

Working Note:

Liquidator's remuneration on payment to Company's banker

Cash available after liquidator remuneration on assets realized

= Rs. 80,00,000 – Rs. 2,40,000 = Rs. 77,60,000 which will be paid to workers and Company's banker in ratio of 1:4.

Cash balance is available Company's banker = Rs. 77,60,000 less Rs. 15,52,000 = 62,08,000 x 4/104= Rs. 2,38,769.

Thus,

1. Amount payable to workers Rs. 15,52,000 (77,60,000 x 1/5).
2. No amount is available for payment of other preferential creditors
3. No amount is available for payment of unsecured creditors.
4. Liquidator for remuneration Rs. 4,78,769
5. Amount payable to Company's bankers = Rs. 59,69,231 (62,08,000 less 2,38,769).

Alternative 2 - If Workmen are treated as creditors for the purpose of Liquidator's remuneration

Ratio of workmen share and bankers share is 1:4. (64,00,000/16,00,000) as computed in Alternative 1 above.

Calculation of Total Remuneration payable to Liquidator

		Amount in Rs.
3% on Assets realized	(80,00,000 x 3%)	2,40,000
4% on payment made to company's Banker (Refer W.N)		2,98,462
Total Remuneration payable to Liquidator		5,38,462

Working Note:

Liquidator's remuneration on payment to Company's banker and workmen:

Cash available after liquidator remuneration on assets realized

= Rs. 80,00,000 – Rs. 2,40,000 = Rs. 77,60,000

Liquidator remuneration = Rs. 77,60,000 X 4/104 = Rs. 2,98,462 (rounded off)

Cash balance is available for workers and Company's banker = Rs. 77,60,000 less Rs. 2,98,462 = Rs. 74,61,538.
The amount of Rs. 74,61,538 will be paid to workers and Company's banker in ratio of 1:4. Thus
1. Amount payable to workers Rs. 14,92,308 (rounded off) (74,61,538 x 1/5).
2. No amount is available for payment of other preferential creditors
3. No amount is available for payment of unsecured creditors.
4. Liquidator for remuneration Rs. 5,38,462
5. Amount payable to Company's bankers = Rs. 59,69,230 (rounded off) (74,61,538 x 4/5).

Question 14 : May – 2022 – RTP

The Balance Sheet of Cloud Ltd., as at 31st March, 2021, being the date of voluntary winding up is as under:

		Particulars	Note	Amount (Rs.)
I		**Equity and Liabilities**		
	1	**Shareholders' Funds:**		
		(a) Share Capital	1	21,00,000
		(b) Reserve and Surplus	2	4,00,000
	2	**Non-Current Liabilities:**		
		(a) Long Term Borrowings	3	4,20,000
	3	**Current Liabilities:**		
		(a) Short Term Borrowings	4	9,70,000
		(b) Trade Payables		12,00,000
		(c) Other Current Liabilities	5	2,10,000
		Total		**53,00,000**
II		**Assets**		
	1	**Non-Current Assets:**		
		(a) Property, Plant and Equipment	6	26,00,000
	2	**Current Assets:**		
		(a) Inventories		6,50,000
		(b) Trade Receivables		20,50,000
		(c) Cash and Cash Equivalents		-
		Total		**53,00,000**

Notes to Accounts:

Particulars	Amount (Rs.)
1. Share Capital	
Authorized:	
10,000 Equity Shares of Rs. 100 each	10,00,000
10,000 Equity Shares of Rs. 100 each	10,00,000
10,000, 10% Cumulative Preference Shares of Rs. 100 each	10,00,000
Issued, Subscribed & Paid up:	

			Rs.
		10,000 Equity Shares of Rs. 100 each, Rs. 60 paid up.	6,00,000
		10,000 Equity Shares of Rs. 100 each, Rs. 50 paid up.	5,00,000
		10,000, 10% Cumulative Preference Shares of Rs. 100 each, fully paid up.	10,00,000
		Total	21,00,000
2.	**Reserve and Surplus**		
	(a)	Securities Premium	15,00,000
	(b)	Profit & Loss A/c (Dr. balance)	(11,00,000)
			4,00,000
3.	**Long Term Borrowings**		
		10% Debentures	4,20,000
4.	**Short Term borrowings**		
		Bank Overdraft (unsecured)	9,70,000
5.	**Other Current Liabilities**		
		Preferential Creditors	2,10,000
6.	**Property, Plant and Equipment**		
	(a)	Land and Buildings	10,40,000
	(b)	Plant and Machinery	15,60,000
			26,00,000

Preference Dividend is in arrears for three years (upto 31st March, 2021). The assets realized as follows:

Land & Building	Rs. 12,40,000	Plant & Machinery	Rs. 14,20,000
Inventory	Rs. 6,20,000	Trade receivables	Rs. 13,20,000

Expenses of Liquidation are Rs.1,72,000. The Remuneration of the Liquidator is 2% of the realization of assets. Income Tax Payable is Rs.1,34,000. Interest on debentures for the year ended 31st March, 2021 has not been considered in the given balance sheet and is also to be paid.

Prepare the Liquidator's Final Statement of Account.

Solution :

Liquidator's Final Statement of Account

Receipts		**Rs.**	**Payments**	**Rs.**
To Sundry Assets Realized:			By Liquidator's Remuneration ($46,00,000 \times 2\%$)	92,000
Trade receivable	13,20,000			
Inventory	6,20,000		By Liquidation Expenses	1,72,000
Land & Building	12,40,000		By Preferential Creditors:	
Plant & Machinery	14,20,000	46,00,000	As given in Balance Sheet	2,10,000
To Calls from shareholders:			Income Tax Liability (given)	1,34,000

Call money on 10,000 Equity shares, Rs. 50 paid up at Rs. 2 per Share	20,000	By Debenture holders:	
		Face Value of Debentures	4,20,000
		Debenture Interest (for 1 year at 10%)	42,000
		By Unsecured Creditors:	
		Bank Overdraft	9,70,000
		Trade payables	12,00,000
		By Preference Shareholders:	
		Preference Capital	10,00,000
		Arrears of Dividend (10,00,000 × 10% × 3 years)	3,00,000
		By Equity Shareholders:	
		refund on 10,000 Shares Rs.60 paid up, at Rs.8 per Share	80,000
	46,20,000		**46,20,000**

Working Note:

Calls from Holders of Partly Paid Shares

	Particulars	**Rs.**
(a)	Total of Receipts before considering Call Money (from the above account Dr. Side)	46,00,000
(b)	Total Payments before final payments to Equity Shares (92,000 + 1,72,000 + 4,20,000 + 42,000 + 2,10,000 + 1,34,000 + 9,70,000 + 12,00,000 + 10,00,000 + 3,00,000)	45,40,000
(c)	Surplus from above Calls made on Equity Shares (a-b)	60,000
(d)	Notional Call on 10,000 Partly Paid Shares at Rs. 10 each (to make all Shares Rs. 60 Paid up)	1,00,000
(e)	Surplus Cash Balance after Notional Call (c + d)	1,60,000
(f)	Number of Shares deemed to be paid at Rs. 60 per Share (10,000 + 10,000)	20,000
(g)	Hence, Refund on every Rs. 60 Paid up Share (e ÷ f) = Rs. 1,60,000 ÷ 20,000 Shares	Rs. 8.00
(h)	So, Required Call on Rs. 50 Paid up Share (Rs. 10 Notional Call Rs. 8 Refund)	Rs. 2

Question 15 : May – 2022 – Paper

The position of Bad Luck Limited on its liquidation on 31st March, 2022 is as under :

Issued and paid up capital:

90,000,10% Preference Shares of Rs.100 each, fully paid

90,000 Equity Shares of Rs.100 each, fully paid up

30,000 Equity Shares of Rs.50 each, Rs.40 paid up

10,000 Equity Shares of Rs.10 each, Rs.4 paid up

Calls in arrears are Rs.3,00,000 and calls received in advance Rs.2,55,000. Preference dividends are in arrears for two years. Amount left with the liquidator after discharging of all liabilities is Rs.1,25,15,000. Articles of Association of the company provide for payment of preference dividend arrears in priority to return of equity capital.

You are required to prepare the Liquidator's Final Statement of Account.

Solution :

Liquidator's Final Statement of Account

Receipts	Rs.	Payments	Rs.
Cash with liquidator	1,25,15,000	Return to contributors:	
Realization from:		Arrears of Preference dividend	18,00,000
Calls in arrears	3,00,000	Preference shareholders	90,00,000
Final call of Rs. 4 per equity share on 10,000 shares (Rs. 4 × 10,000) See WN	40,000	Calls in advance	2,55,000
		Equity shareholders (90,000 × Rs. 20)	18,00,000
	1,28,55,000		**1,28,55,000**

Working Notes:

(i) **Calculation of amount available with liquidator after paying pref. shareholders**

		Rs.
Cash account balance		1,25,15,000
Less: Payment for dividend	18,00,000	
Preference shareholders	90,00,000	
Calls in advance	2,55,000	(1,10,55,000)
		14,60,000
Add: Calls in arrears		3,00,000
		17,60,000

(ii) Paid up Share capital = 90,00,000 + 12,00,000 + 40,000=Rs. 1,02,40,000

(iii) Deficiency for equity shareholders:
Rs. 1,02,40,000 - Rs. 17,60,000 = Rs. 84,80,000

(iv) Nominal Value of Share Capital
= Rs. 90,00,000 + 15,00,000+1,00,000 = 1,06,00,000

(v) % of deficiency to be borne by each equity shareholder:
= (Rs. 84,80,000 / Rs. 1,06,00,000) x 100 = 80%

(vi) Amount refunded/recovered from equity shareholders:

	90,000 shares of Rs.100 each	30,000 shares of Rs.50 each	10,000 shares of Rs.10 each
Paid up per share	Rs. 100	Rs. 40	Rs. 4
Deficiency to bear per share (80% of nominal value)	Rs. 80	Rs. 40	Rs. 8
	To refund Rs. 20 per share	NIL	To recover Rs. 4 per share

Note: Alternative presentation of the above working notes may be provided in the answer.

Question 16 : Nov – 2022 – RTP

Debit and credit Balances of Blossam Ltd as on 31.12.2021 were as follows:

Dr. Balances		Cr. Balances	
Land & Building	1,25,000	Share Capital:	
Other Fixed Assets	3,00,000	8,000 Preference Shares of Rs. 10 each	80,000
Inventory	5,25,000	12,000 Equity Shares of Rs. 10 each	1,20,000
Trade receivables	1,00,000	Bank Loan	4,00,000
Surplus a/c (-ve bal.)	58,000	8% Debentures	1,00,000
		Interest Outstanding on Debentures	8,000
		Trade payables	4,00,000
	11,08,000		**11,08,000**

The Company went into Liquidation on that date. Prepare liquidator's account after taking following:

(a) Liquidation Expenses Rs. 3,000.

(b) Liquidation Remuneration Rs. 10,000.

(c) Bank Loan was secured by pledge of Stock.

(d) Debentures & Interest thereon are secured by floating charge on all assets.

(e) Fixed Assets were realized at book values and Current Assets @ 80% of book values.

Solution :

Liquidator's Statement of account

	Rs.	Rs.		Rs	Rs.
Assets Realized			Liquidation Expenses.		3,000
Land & Building		1,25,000	Liquidator's Remuneration		10,000
Other Fixed Assets		3,00,000	Debenture holders		
Inventory	4,20,000		8% Debentures	1,00,000	
(80% x 5,25,000)			Add: Interest Outstanding	8,000	1,08,000

Less: bank loan	(4,00,000)	20,000	Trade payables		4,00,000
Trade receivables		80,000	Pref. Shareholders		
(80% x 1,00,000)			On 8,000 Shares @ 50 Paise per Share		4,000
		5,25,000			**5,25,000**

Working Notes

(a) Value of Debentureholders — Rs.

8% Debentures = 1,00,000

Add Interest Outstanding = 8,000

= 1,08,000

(b) Value of Preference Shareholders to be paid

8000 Shares @ 50 Paise Per Share

8000 x 0.50 = Rs. 4,000

Question 17 : Nov – 2022 – Paper

Proud Limited is being wound up by the tribunal. All the assets of the company have been charged to the company's banker to whom the company owes Rs.10 crores. The company owes the following amounts to others:

(i) Dues to workers – Rs.2,50,00,000

(ii) Taxes payable to Government – Rs.60,00,000

(iii) Unsecured Creditors – Rs.1,20,00,000 '

You are required to compute with the reference to the provisions of the Companies Act, 2013 the amount each kind of creditors is likely to get if the amount realized by the official liquidator from the secured assets and available for distribution among creditors is only Rs.8,00,00,000.

Thanks ....

CHAPTER 20

FINANCIAL STATEMENTS OF BANKING COMPANIES

Question 1 : May – 2018 – Paper / Nov – 2020 – Paper / May – 2022 – Paper

Astha Bank has the following Capital Funds and Assets as at 31st March, 2018:

	Rs. in crores
Capital Funds:	
Equity Share Capital	600.00
Statutory Reserve	470.00
Profit and Loss Account (Dr. Balance)	30.00
Capital Reserve (out of which Rs.025 crores were due to revaluation of assets and balance due to sale of assets)	130.00
Assets:	
Balance with other banks	15.00
Cash balance with RBI	35.50
Claim on Banks	52.50
Other Investments	70.00
Loans and Advances:	
(i) Guaranteed by government	22.50
(ii) Guaranteed by DICGC/ECGC	110.00
(iii) Other	9365.00
Premises, furniture and fixtures	92.50
Leased assets	40.00
Off- Balance Sheet items:	
(i) Acceptances, endorsements and letters of credit	1100.00
(ii) Guarantees and other obligations	6200.00

You are required to:

(i) Segregate the capital funds into Tier I and Tier II capitals.

(ii) Find out the risk-adjusted assets and risk weighted assets ratio.

Solution :

(i) Capital Funds –

	Rs. in crore
Tier I :	
Equity Share Capital	600
Statutory Reserve	470

Capital Reserve (arising out of sale of assets)	105
Less: Profit & Loss (Dr. bal.)	(30)
	1,145
Tier II :	
Capital Reserve (arising out of revaluation of assets)	25
Less: Discount to the extent of 55%	(13.75)
	11.25

(ii) Risk Adjusted Assets

Funded Risk Assets	Rs. in crore	Percentage weight	Amount Rs. in crore
Cash Balance with RBI	35.50	0	-
Balances with other Banks	15	20	3
Claims on banks	52.50	20	10.50
Other Investments	70	100	70
Loans and Advances:			
(i) guaranteed by government	22.50	0	-
(ii) guaranteed by DICGC/ECGC	110	50	55
(iii) Others	9,365	100	9,365
Premises, furniture and fixtures	92.50	100	92.50
Leased Assets	40	100	40
			9,636

Off-Balance Sheet Item	Rs. in Crore	Credit Conversion Factor	Rs. in Crore
(i) Acceptances, Endorsements and Letters of credit	1,100	100	1,100
(ii) Guarantees and other obligations	6,200	100	6,200
			7,300

Risk Weighted Assets Ratio : $\dfrac{\text{Capital Funds (Tier I \& Tier II)}}{\text{Risk Adjusted Assets + Off Balance sheet items}} \times 100$

= (1,145 +11.25)/ (9,636 +7,300)

= (1,156.25 /16,936) x 100 = 6.83% (rounded off)

Question 2 : Nov – 2018 – Paper / May – 2021 – RTP

Forward Bank Ltd furnishes the following information as on 31st March, 2018.

	Amount in Rs.
Bills Discounted	82,23,000
Rebate on bills discounted as on 1st April, 2017	1,32,960
Discount received	6,33,990

Details of bills discounted is as given below:

Value of Bills (Rs.)	Due Date	Rate of Discount
10,95,000	15th June, 2018	14%
30,00,000	25th June, 2018	12%
16,92,000	5th July, 2018	16%
24,36,000	15th July, 2018	16%

(i) Calculate the rebate on bills discounted as on 31st March, 2018.

(ii) Pass necessary Journal Entries.

Solution :

In order to determine the amount to be credited to the Profit and Loss A/c it is necessary to first ascertain the amount attributable to the unexpired portion of the period of the respective bills. The workings are as given below:

Value (Rs.)	Due Date	Days after 31-03-2018	Discount %	Discount Amount Rs.
10,95,000	15-06-2018	(30+31 + 15) = 76	14%	
30,00,000	25-06-2018	(30 + 31 + 25) = 86	12%	31,920
16,92,000	05-07-2018	(30 + 31 + 30 + 5) = 96	16%	84,822
24,36,000	15-07-2018	(30 + 31 + 30 + 15) = 106	16%	71,203
		Rebate on bills discounted as on 31.3.2018		1,13,191*
				3,01,136

The journal entries will be as follows :

Particulars		Dr. Rs.	Cr. Rs.
Rebate on Bills Discounted A/c	Dr.	1,32,960	
To Discount on Bills A/c			1,32,960
(Being the transfer of Rebate on Bills Discounted on 1.4.2017 to Discount on Bills Account)			
Discount on Bills A/c	Dr.	3,01,136	
To Rebate on Bills Discounted A/c			3,01,136
(Being the transfer of rebate on bills discounted required on 1.4.2018 from discount on Bills Account)			
Discount on Bills A/c	Dr.	4,65,814	
To Profit and Loss A/c			4,65,814
(Being the amount of discount on Bills transferred to Profit and Loss Account)			

Working Note:

The amount of discount to be credited to the Profit and Loss Account will be:

	Rs.
Transfer from Rebate on bills discount as on 1.4.17	1,32,960
Add: Discount received during the year ended 31-3-2018	6,33,990
	7,66,950
Less: Rebate on bills discounted as on 31.3.2018	(3,01,136)
	4,65,814

Question 3 : May – 2019 – RTP

From the following information of Wealth Bank Limited, Prepare Profit and Loss Account for the year ended 31st March, 2018:

Particulars	Rs. in lakhs	Particulars	Rs. in lakhs
Interest on Cash Credit	364	Interest paid on Recurring Deposits	17
Interest on Overdraft	150	Interest paid on Savings Bank Deposits	12
Interest on Term Loans	308	Auditor's Fees and Allowances	24
Income on Investments	168	Directors' Fees and Allowance	50
Interest on Balance with RBI	30	Advertisement	36
Commission on remittances and transfer	15	Salaries, allowances and bonus to employees	248
Commission on Letters of Credit	24	Payment to Provident Fund	56
Commission on Government Business	16	Printing & Stationery	28
Profit on Sale of Land & Building	5	Repairs & Maintenance	10
Loss on exchange transactions	10	Postage, courier & telephones	16
Interest paid on Fixed Deposits	25		

Other Information :

		Rs. in lakhs	
		Earned	Collected
(i)	Interest on NPA is as follows:		
	Cash Credit	164	80
	Term Loans	90	20
	Overdraft	150	50
(ii)	Classification of Non-performing Advances:		

	Standard		60
	Sub-standard-fully secured		22
	Doubtful assets-fully unsecured		40
	Doubtful assets covered fully by security:		
	Less than 1 year		6
	More than 1 year upto 3 years		3
	More than 3 years		2
	Loss Assets		38

(iii) Provide 35% of the profits towards provision for taxation.

(iv) Transfer 25% of the profit to Statutory Reserves.

Solution :

Wealth Bank Limited
Profit and Loss Account
For the year ended 31st March, 2018

Rs. in lakhs

	Particulars	**Schedule**	**Year ended 31-3-2018**
I	Income		
	Interest earned	13	766
	Other income	14	50
			816
II	Expenditure		
	Interest expended	15	54
	Operating expenses	16	468
	Provisions and Contingencies (Refer W.N.)		158.96
			680.96
III	Profit/Loss		
	Net Profit/(Loss) for the year		135.04
	Net Profit/(Loss) brought forward		Nil
			135.04
IV	Appropriations:		
	Transfer to Statutory reserve (25% of the profits)		33.76
	Balance carried to the balance sheet		101.28
	Total		135.04

Schedule 13 – Interest Earned

		Year ended 31-3-2018	
			(Rs. in lakhs)
I	Interest/discount on advances/bills		
	Interest on cash credit (364-84)	280	
	Interest on overdraft (150-100)	50	
	Interest on term loans (308-70)	238	568
II	Income on investments		168
III	Interest on Balance with RBI		30
			766

Interest on NPA is recognized on cash basis, hence difference of accrued interest not received have been reduced from the total accrued interest.

Schedule 14 - Other Income

		Year ended 31-3-2018	
			(Rs. in lakhs)
I	Commission, Exchange and Brokerage:		
	Commission on remittances and transfer	15	
	Commission on letter of credit	24	
	Commission on Government business	16	55
II	Profit on sale of Land and Building		5
III	Loss on Exchange Transactions		(10)
			50

Schedule 15 – Interest Expended

		Year ended 31-3-2018	
			(Rs. in lakhs)
I	Interest on Deposits		
	Fixed deposits	25	
	Recurring deposits	17	
	Saving bank deposits	12	54

Schedule 16 – Operating Expenses

		Year ended 31-3-2018	
			(Rs. in lakhs)
I	Payment to and provision for employees		
	Salaries, allowances and bonus	248	
	Provident Fund Contribution	56	304
II	Printing and Stationery		28
III	Advertisement and publicity		36
IV	Directors' fees, allowances and expenses		50
V	Auditors' fees and expenses		24

VI	Postage, telegrams, telephones etc.		16
VII	Repairs and maintenance		10
			468

Working Note :

Provisions and contingencies			**(Rs. in lakhs)**
Provision for Advances:			
Standard	60 × 0.40%		0.24
Sub-standard	22 × 15%		3.3
Doubtful not covered security	40× 100%		40
Doubtful covered by security:			
Less than 1 year	6 x 25%	1.5	4.7
More than 1 year but less than 3 years	3 x 40%	1.2	
More than 3 years	2 x 100%	2.0	
Loss Assets	(38 × 100%)		38
			86.24
Provision for tax	35% of (Total Income – Total Expenditure) 35% of [816-(54 + 468 + 86.24)] 35% of 207.76		72.72
			158.96

Question 4 : May – 2019 – Paper

(i) The following is an extract of Trial Balance of SM Bank, an overseas bank as on 31st March, 2018.

	Dr. Rs.	**Cr. Rs.**
Bill Discounted	15,16,800	
Discount Received		1,26,859
Rebate on Bills discounted not due on 31st March, 17		26,592

An analysis of bill discounted is as follows :

Amount in Rs.	**Due Date**	**Rate of Discount**
1,46,200	4th May, 2018	15
2,30,400	12th May, 2018	15
4,35,900	28th May, 2018	15
4,36,200	18th June, 2018	16
2,68,100	4th July, 2018	16

You are required to calculate Rebate on Bills Discounted as on 31st March, 2018 and show necessary Journal Entries.

(ii) The following information are also given for SM Bank :

Assets	**Rs. in Lakhs**
Standard	75,00
Sub-Standard	60,00

Doubtful:	for 1 Year (fully secured)	12,00
	for 1 to 3 Year (fully secured)	9,00
	for more than 3 Years	9,00
Loss Assets		15,00

Additional Information:

(1) Standard Assets includes Rs.15,00 Lakhs Advances to Commercial Real Estate (CRE).

(2) Out of Rs.60,00 Lakhs of Sub-Standard Asset Rs.20,00 Lakhs are unsecured. Unsecured amount includes Rs.5,00 Lakhs in respect of Infrastructure Loan Accounts with ESCROW safeguard.

(3) Doubtful Asset for more than 3 Years includes Rs.4,00 Lakhs, which is covered by 50% ECGC, value of security of which is Rs.150 Lakhs.

You are required to find out the amount of provision to be shown in the Profit & Loss Account of SM Bank.

Solution :

(i) Statement showing rebate on bills discounted

Value (Rs.)	Due Date	Days after 31-03-2018	Rate of Discount	Discount Amount
1,46,200	4.5.18	(30+ 4) = 34	15%	2,043
2,30,400	12.5.18	(30+12) = 42	15%	3,977
4,35,900	28.5.18	(30+28) = 58	15%	10,390
4,36,200	18.6.18	(30+ 31+ 18) = 79	16%	15,106
2,68,100	4.7.18	(30+ 31+30+4) = 95	16%	11,165
15,16,800		Rebate on bills discounted on 31.3.2018		42,681

In the books of SM Bank Ltd.

Journal Entries

	Particulars		Dr. Rs.	Cr. Rs.
(i)	Rebate on bills discounted Account	Dr.	26,592	
	To Discount on bills Account			26,592
	[Being opening balance of rebate on bills discounted account transferred to discount on bills account]			
(ii)	Bills purchased & discounted Account	Dr.	15,16,800	
	To Discount on bills Account			1,26,859
	To Clients Account			13,89,941
	(Being bills purchased and discounted during the year)			
(iii)	Discount on bills Account	Dr.	42,681	
	To Rebate on bills discounted Account			42,681

	[Being provision made on 31st March, 2018]		
(iv)	Discount on bills Account Dr.	1,10,770	
	To Profit and loss Account		1,10,770
	[Being transfer of discount on bills, of the year, to profit and loss account]		

Credit to Profit and Loss A/c will be as follows:
Rs.(1,26,859 + 26,592 – 42,681) = Rs.1,10,770

(ii) Statement showing the amount of provisions on Assets

			(Rs. in lakhs)
Assets	**Amount**	**% of provision**	**Provision**
Standard:			
Advances to CRE	15,00	1	15
Others	60,00	4	24
Sub-standard:			
Secured	40,00	15	6,00
Unsecured- Others	15,00	25	3,75
Unsecured infrastructure	5,00	20	1,00
Doubtful Secured:			
up to one year	12,00	25	3,00
For more than 1 year up to 3 years	9,00	40	3,60
More than 3 years	4,00	W.N.1	2,75
Doubtful unsecured (more than 3 years)	5,00	100	5,00
Loss	15,00	100	15,00
Total Provision Required			40,49

Working Note :
Provision required where assets are ECGC covered

	Rs. in lakhs
Outstanding balance (ECGC Covered)	4,00
Less: Value of security	1,50
Unrealised balance	2,50
Less: ECGC Cover @ 50%	1,25
Net Unsecured Balance	1,25
Provision for unsecured portion @100%	1,25
Provision for secured portion @100%	1,50
Total Provision to be made	2,75

Question 5 : Nov – 2019 – RTP

The following is an extract from the Trial Balance of Jeevan Bank Ltd. as at 31st March, 2019:

Rebate on bills discounted as on 1-4- 2018	1,36,518 (Cr.)
Discount received	3,40,312 (Cr.)

Analysis of the bills discounted reveals as follows:

Amount (Rs.)	Due date
5,60,000	June 1, 2019
17,44,000	June 8, 2019
11,28,000	June 21, 2019
16,24,000	July 1, 2019
12,00,000	July 5, 2019

You are required to find out the amount of discount to be credited to Profit and Loss account for the year ending 31st March, 2019 and pass Journal Entries. The rate of discount may be taken at 10% per annum.

Solution :

The amount of rebate on bills discounted as on 31st March, 2019 the period which has not been expired upto that day will be calculated as follows:

Discount on Rs.5,60,000 for 62 days @ 10%	9,512
Discount on Rs.17,44,000 for 69 days @ 10%	32,969
Discount on Rs.11,28,000 for 82 days @ 10%	25,341
Discount on Rs.16,24,000 for 92 days @ 10%	40,934
Discount on Rs.12,00,000 for 96 days @ 10%	31,562
Total	1,40,318

Note: The due date of the bills discounted is included in the number of days above.

The amount of discount to be credited to the profit and loss account will be:

	Rs.
Transfer from rebate on bills discounted as on 31.03. 2018	1,36,518
Add: Discount received during the year	3,40,312
	4,76,830
Less: Rebate on bills discounted as on 31.03. 2019 (as above)	(1,40,318)
	3,36,512

Journal Entries

	Dr. Rs.	**Cr. Rs.**
Rebate on bills discounted A/c Dr.	1,36,518	
To Discount on bills A/c		1,36,518
(Transfer of opening unexpired discount on 31.03. 2018)		

Discount on bills A/c Dr. To Rebate on bills discounted A/c (Unexpired discount on 31.03. 2019 taken into account)	1,40,318	 1,40,318
Discount on Bills A/c Dr. To P & L A/c (Discount earned in the year, transferred to P&L A/c)	3,36,512	 3,36,512

Question 6 : Nov – 2019 – Paper

From the following information, you are required to prepare Profit and Loss Account of Simple Bank for the year ended as on 31st March, 2019:

2017-18 (Rs.in '000)	Item	2017-18 (Rs.in '000)
71,35	Interest and Discount	1,02,25
5,70	Income from investment	5,60
7,75	Interest on Balances with RBI	8,85
36,10	Commission, Exchange and Brokerage	35,60
60	Profit on sale of investments	6,10
30,60	Interest on Deposits	41,10
6,35	Interest to RBI	7,35
36,35	Payment to and provision for employees	42,75
7,90	Rent, taxes and lighting	8,95
7,35	Printing and Stationery	10,60
5,60	Advertising and publicity	4,90
4,90	Depreciation	4,90
7,40	Director's fees	10,60
5,50	Auditor's fees	5,50
2,50	Law Charges	7,60
2,40	Postage, telegrams and telephones	3,10
2,10	Insurance	2,60
2,85	Repair and maintenance	3,30

Other Information:

(i) The following items are already adjusted with Interest and Discount (Cr.)

Tax Provision (Rs.'000)	7,40
Provision for Doubtful Debts (Rs.'000)	4,60
Loss on sale of investments (Rs.'000)	60
Rebate on Bills discounted (Rs.'000)	2,75

(ii) Appropriations:

25% of profit is transferred to Statutory Reserves.

5% of profit is transferred to Revenue Reserve.

You are required to give necessary Schedules also.

Solution :

Simple Bank
Profit and Loss Account for the year ended 31-3-2019

		Schedule No.	(Rs. 000's) Year ended 31-3-2019	(Rs. 000's) Year ended 31-3-2018
I.	Income			
	Interest Earned	13	1,29,30	84,80
	Other Income	14	41,10	36,70
	Total		1,70,40	1,21,50
II.	Expenditure			
	Interest Expended	15	48,45	36,95
	Operating Expenses	16	1,04,80	84,85
	Provisions and Contingencies		12,00	
	Total		1,65,25	1,21,80
III.	Profit/Loss			
	Net Profit/Loss for the year		5,15	(30)
	Profit/Loss brought forward		(30)	
	Total		4,85	(30)
IV.	Appropriations			
	Transfer to Statutory Reserve		128.75	
	Transfer to Other Reserve, Proposed Dividend		25.75	
	Balance carried over to Balance Sheet		330.5	
	Total		485.0	

Schedule 13 – Interest Earned

(Rs. 000's)

		Year ended 31-3-2019	Year ended 31-3-2018
I.	Interest/Discount	1,14,85	71,35
II.	Income on Investments	5,60	5,70
III.	Interest on Balances with RBI and other inter-bank fund	8,85	7,75
IV.	Others	------	------
	Total	1,29,30	84,80

Schedule 14 – Other Income

(Rs. 000's)

		Year ended 31-3-2019	Year ended 31-3-2018
I	Commission, Exchange and Brokerage	35,60	36,10
II	Profit on Sale of Investments	6,10	60
	Less: Loss on sale of Investments	(60)	-
	Total	41,10	36,70

Schedule 15 – Interest Expended

(Rs. 000's)

		Year ended 31-3-2019	Year ended 31-3-2018
I	Interest on Deposits	41,10	30,60
II	Interest on RBI/inter-bank borrowings	7,35	6,35
	Total	48,45	36,95

Schedule 16 – Operating Expenses

(Rs. 000's)

		Year ended 31-3-2019	Year ended 31-3-2018
I	Payments to and provision for employees	42,75	36,35
II	Rent, taxes and lighting	8,95	7,90
III	Printing and stationery	10,60	7,35
IV	Advertisement and Publicity	4,90	5,60
V	Depreciation on the Bank's Property	4,90	4,90
VI	Director's fees, allowances and expenses	10,60	7,40
VII	Auditor's fees and expenses (including branch auditors)	5,50	5,50
VIII	Law charges	7,60	2,50
IX	Postage, telegrams, telephones etc.	3,10	2,40
X	Repairs and maintenance	3,30	2,85
XI.	Insurance	2,60	2,10
XII.	Other Expenditure	------	------
	Total	1,04,80	84,85

Question 7 : Nov – 2019 – Paper

The following information is furnished by ALFA Bank Ltd.

	Rs.in Lakhs
Margins held against letter of credit	200
Recurring accounts deposits	100
Current accounts deposits	375

Demand deposits	125
Unclaimed deposits	75
Gold deposits	235
Demand liabilities portion of saving bank deposit	1325
Time liabilities portion of saving bank deposit	722

Explain CRR and you are required to calculate the amount of Cash Reserve Ratio (CRR) as per the directions of Reserve Bank of India.

Solution :

Cash Reserve Ratio (CRR): For smoothly meeting cash payment requirement, banks are required to maintain certain minimum ready cash balances at all times. This is called as Cash Reserve Ratio (CRR).

Cash reserve can be maintained by way of either a cash reserve with itself or as balance in a current account with the Reserve Bank of India or by way of net balance in current accounts or in one or more of the aforesaid ways. Every Scheduled Commercial Bank has to maintain cash reserve ratio (i.e. CRR) as per direction of the RBI. The current Cash Reserve Ratio (CRR) is 4% of their Net Demand and Time Liabilities (NDTL).

Margins held against letters of credit	Demand Liability	200
Recurring Accounts deposits	Time Liability	100
Current deposits	Demand Liability	375
Demand deposits	Demand Liability	125
Unclaimed deposits,	Demand Liability	75
Gold deposits	Time Liability	235
Demand liabilities portion of savings bank deposits	Demand Liability	1325
Time liabilities portion of savings bank deposits	Time Liability	722
	Total	3,157

Cash Reserve Ratio = Net (demand + Time) liabilities x 4/100

CRR= 3,157 x 4/100 = 126.28 Lakhs

Question 8 : May – 2020 – RTP

Anmol Bank Ltd. has a balance of Rs. 40 crores in "Rebate on bills discounted" account as on 31st March, 2018. The Bank provides you the following information:

(i) During the financial year ending 31st March, 2019 Anmol Bank Ltd. discounted bills of exchange of Rs. 5,000 crores charging interest @ 14% and the average period of discount being 146 days.

(ii) Bills of exchange of Rs. 500 crores were due for realization from the acceptors/customers after 31st March, 2019. The average period of outstanding after 31st March, 2019 being 73 days. These bills of exchange of Rs. 500 crores were discounted charging interest @ 14% p.a.

You are requested to give the necessary Journal Entries in the books of Anmol Bank Ltd. for the above transactions.

Solution :

In the books of Anmol bank Ltd.
Journal Entries

Rs. in crores

Particulars		**Dr. Rs.**	**Cr. Rs.**
Rebate on bills discounted A/c	Dr.	40	
To Discount on bills A/c			40
(Being the transfer of opening balance in 'Rebate on bills discounted A/c' to 'Discount on bills A/c')			
Bills purchased and discounted A/c	Dr.	5,000	
To Discount on bills A/c			280
To Clients A/c			4,720
(Being the discounting of bills of exchange during the year)			
Discount on bills A/c	Dr.	14	
To Rebate on bills discounted A/c			14
(Being the unexpired portion of discount in respect of the discounted bills of exchange carried forward)			
Discount on bills A/c	Dr.	306	
To Profit and Loss A/c			306
(Being the amount of income for the year from discounting of bills of exchange transferred to Profit and loss A/c)			

Working Notes:

1. **Discount received on the bills discounted during the year**
   Rs. 5,000 crores x 14/100 x 146/365 = Rs. 280 crores
2. **Calculation of rebate on bill discounted**
   Rs. 500 crores x 14/100 x 73/365 = Rs.14 crores
3. Income from bills discounted transferred to Profit and Loss A/c would be calculated by preparing Discount on bills A/c

Discount on bills A/c

Rs. in crores

Date	**Particulars**	**Amount**	**Date**	**Particulars**	**Amount**
31.3.2019	To Rebate on bills discounted	14	1.4.2018	By Rebate on bills discounted b/d	40
"	To Profit and Loss A/c (Bal. Fig.)	306	2018-19	By Bills purchased and discounted	280
		320			**320**

Question 9 : Nov – 2020 – RTP / May – 2021 – RTP

State with reason whether the following cash credit accounts are NPA or not:

	Case-1	Case-2
Sanctioned limit	60,00,000	45,00,000
Drawing power	56,00,000	42,00,000
Amount outstanding continuously 01-01-19 to 31-03-19	48,00,000	30,00,000
Total interest debited for the above period	3,84,000	2,40,000
Total credits for the above period	Nil	3,20,000

Solution :

	Case 1 Rs.	Case 1 Rs.
Sanctioned limit	60,00,000	45,00,000
Drawing power	56,00,000	42,00,000
Amount outstanding continuously from 1.01.2019 to 31.03.2019	48,00,000	30,00,000
Total interest debited	3,84,000	2,40,000
Total credits	-	320,000
Is credit in the account is sufficient to cover the interest debited during the period or amount is not 'overdue' for a continuous period of 90 days.	No	Yes
	NPA	NOT NPA

Question 10 : Nov – 2020 – RTP

The following is an extract from the trial balance of Novel Bank Limited as on 31st March 2019:

Rebate on bills discounted as on 1st April 2018 Rs.78,566 (Cr. bal)

Discount Received Rs.1,60,572 (Cr. bal)

An analysis of bills discounted is as follows:

Amount Rs.	Due Date
2,90,000	1-Jun-19
8,75,000	8-Jun-19
5,65,000	21-Jun-19
8,12,000	1-Jul-19
6,50,000	5-Jul-19

Find out the amount of discount to be credited to Profit and Loss Account for the year ending on 31st March, 2019 and pass the necessary journal entries. The rate of discount shall be taken at 10% per annum.

Solution :

The amount of rebate on bills discounted as on 31st March, 2019 the period which has not been expired upto that day will be calculated as follows:

Discount on Rs. 2,90,000 for 62 days @ 10%	4,926
Discount on Rs. 8,75,000 for 69 days @ 10%	16,541
Discount on Rs. 5,65,000 for 82 days @ 10%	12,693
Discount on Rs. 8,12,000 for 92 days @ 10%	20,467
Discount on Rs. 6,50,000 for 96 days @ 10%	17,096
Total	71,723

Note: The due date of the bills discounted is included in the number of days above.

The amount of discount to be credited to the profit and loss account will be:

	Rs.
Transfer from rebate on bills discounted as on 1.4. 2018	78,566
Add: Discount received during the year	1,60,572
	2,39,138
Less: Rebate on bills discounted as on 31.03. 2019 (as above)	(71,723)
	1,67,415

Journal Entries

Particulars		**Dr. Rs.**	**Cr. Rs.**
Rebate on bills discounted A/c	Dr.	78,566	
To Discount on bills A/c			78,566
(Transfer of opening unexpired discount on 31.03. 2018)			
Discount on bills A/c	Dr.	71,723	
To Rebate on bills discounted			71,723
(Unexpired discount on 31.03. 2019 taken into account)			
Discount on Bills A/c	Dr.	1,67,415	
To P & L A/c			1,67,415
(Discount earned in the year, transferred to P&L A/c)			

Question 11 : Jan – 2021 – Paper

A commercial bank has the following capital funds and assets. Segregate the capital funds into Tier I and Tier II capitals. Find out the risk-adjusted asset risk weighted assets ratio :

Capital Funds :	**(Rs.in lakhs)**
Equity Shares Capital	29,00
Perpetual Non-cumulative Preference Shares	8,00
Perpetual Cumulative Preference Shares (fully paid up)	5,50
Statutory Reserve	13,50
Capital Reserve (of which Rs.13.5 lakhs were due to revaluation of assets and the balance due to sale of assets)	45
Securities Premium	7,00

Assets :

Cash balance with RBI	3,50
Balances with other banks	4,75
Claims on Banks	10,25
Investments in Bonds issued by other banks	78,00
Investments in venture capital funds	17,00
Other investments	121,00
Loan and Advances :	
(i) Loans guaranteed by Government	16,10
(ii) Loans guaranteed by public sector undertakings	6,20
(iii) Leased assets	4
(iv) Advances against term deposits	15,00
(v) Educations loans	12
Other Assets :	
(i) Premises, Furniture & Fixtures and other assets	150,55
(ii) Intangible assets	18
(iii) Deferred tax asset	0.40
Off Balance sheet Items :	
(i) Acceptances, Endorsements and letter of credit	203,00
(ii) Non funded exposure of real estate	19,00

Solution :

			(in lakhs)
(i)	**Capital Funds - Tier I:**		
	Equity Share Capital		29,00.00
	Securities premium		7,00.00
	Perpetual non-cumulative pref. shares		8,00.00
	Statutory Reserve		13,50.00
	Capital Reserve (arising out of sale of assets)		31.50
			57,81.50
	Less: Intangible assets	(18.00)	
	Deferred tax assets	(0.40)	(18.40)
	Total		57,63.10
	Capital Funds - Tier II:		
	Perpetual cumulative pref. shares		5,50.00
	Capital Reserve (arising out of revaluation of assets)	13.50	
	Less: Discount to the extent of 55%	(7.43)*	6.07
	Total		556.07
	Total Capital Funds		63,19.17

* 7.425 has been rounded off as 7.43.

(ii) Calculation of Risk Adjusted Assets

	Rs. in lakhs	Weight in %	Amount (Rs. in lakhs)
Funded Risk Assets			
Cash Balance with RBI	3,50	0	0
Balances with other Banks	4,75	20	95
Claims on banks	10,25	20	2,05
Investment in bonds issued by other banks	78,00	20	15,60
Investment in venture capital funds	17,00	150	25,50
Other Investments	121,00	100	121,00
Loans and Advances:			
(i) guaranteed by government	16,10	0	0
(ii) guaranteed by public sector undertakings	6,20	0	0
(iii) Leased assets	4	100	4
(iv) Advances against term deposits	15,00	0	0
(v) Educational Loans	12	100	12
Premises, furniture and fixtures	150,55	100	150,55
			315,81

Off-Balance Sheet Item	**Rs. in lakhs**	**Credit Conversion Factor**	**Rs. in lakhs**
Acceptances, Endorsements and Letters of credit	203,00	100	203,00
Non-funded exposure to real estate sector	19,00	150	28,50
			231,50

(iii) Risk Weighted Assets Ratio: $\frac{\text{Capital Funds (Tier I \& Tier II)}}{\text{Risk Adjusted Assets + off Balance sheet items}} \times 100$

Capital Adequacy Ratio = 63,19.17/315,81 + 231,50

= (63,19.17/547,31) x 100=11.55%

Question 12 : July – 2021 – Paper

The following are the figures extracted from the books of New Bank Limited as on 31.03.2021.

	Figure in Rs.
Interest and Discount received	48,11,200
Interest paid on Deposits	22,95,920
Salaries and allowances	8,40,510

Directors fees and allowances	45,000
Issued and subscribed capital	16,00,000
Commission, Exchange and Brokerage received	1,45,000
Postage and Telegrams	60,000
Statutory Reserve Fund	8,00,000
Interest on cash credit	2,65,000
Profit on sale of Investments	1,15,800
Depreciation on Bank's Property	40,000
Interest on Overdraft	1,20,000
Rent Received	65,000
Legal Expenses	21,000
Auditors Fees	5,000
Statutory Expenses	38,000

The following information is also given :

(i) A customer to whom a sum of Rs.5 Lakhs was advanced has become insolvent and it is expected that only 50% can be recovered from his estate.

(ii) Make necessary provisions on Risk Assets :

	Rs.
Standard (excluding above Rs.5,00,00)	10,00,000
Sub-Standard (fully secured)	8,20,000
Doubtful assets covered security for 1 year	40,000
Loss assets	1,00,000

(iii) Provide Rs.6,50,000 for Income Tax.

(iv) The directors desire to declare 10% dividend.

(v) 25% of profit is to be transferred to Reserve fund.

(vi) Rebate on Bills discounted on 31.03.2020 was Rs.20,000 and Rs.15,000 on 31.03.2021.

You are required to prepare Profit and Loss A/c of New Bank Limited for the year ended 31.03.2021.

Solution :

New Bank Limited

Profit and Loss Account for the year ended 31st March, 2021

		Schedule	Year ended 31.03.2021 Rs.
I.	Income:		
	Interest earned	13	52,01,200
	Other income	14	3,25,800
	Total		55,27,000
II.	Expenditure		
	Interest expended	15	22,95,920

	Operating expenses	16	10,49,510
	Provisions and contingencies (6,50,000 + 2,37,000 + 2,50,000)		11,37,000
	Total		44,82,430
III.	Profits/Losses		
	Net profit for the year		10,44,570
	Profit brought forward		Nil
			10,44,570
IV.	Appropriations		
	Transfer to statutory reserve (25% of 10,44,570)		2,61,143
	Proposed dividend		1,60,000
	Balance carried over to balance sheet		6,23,427
			10,44,570

Note: Profit & Loss Account balance of Rs. 6,23,427 will appear under the head 'Reserves and Surplus' in Schedule 2 of the Balance Sheet.

Year ended 31.3.2021 (`)		
	Schedule 13 – Interest Earned	
I.	Interest/discount on advances/bills (Refer W.N.)	48,16,200
	Interest on cash credit*	2,65,000
	Interest on overdraft *	1,20,000
		52,01,200
	Schedule 14 – Other Income	
I.	Commission, exchange and brokerage	1,45,000
II.	Profit on sale of investment	1,15,800
III.	Rent received	65,000
		3,25,800
	Schedule 15 – Interest Expended	
I.	Interests paid on deposits	22,95,920
		22,95,920
	Schedule 16 – Operating Expenses	
I.	Payment to and provisions for employees (salaries & allowances)	8,40,510
II.	Depreciation on assets	40,000
III.	Director's fee, allowances and expenses	45,000
IV	Auditor's fee	5,000
V.	Statutory (law) expenses	38,000
VI.	Postage and telegrams	60,000
VII.	Legal expenses	21,000
		10,49,510

Working Notes:

1.

	Rs.
Interest and discount received	48,11,200
Add: Rebate on bills discounted on 31.3. 2020	20,000
Less: Rebate on bills discounted on 31.3. 2021	-15,000
	48,16,200

2.

Classification of Assets	Amount of Advances	% age of provision	Amount of provision
Standard assets	10,00,000	0.40	4,000
Sub-standard assets	8,20,000	15	1,23,000
Doubtful assets:			
For one year (secured)	40,000	25	10,000
Loss assets	1,00,000	100	1,00,000
Total provision required			2,37,000

Question 13 : Nov – 2021 – RTP

From the following information of Sun Bank Limited, Prepare Profit and Loss Account for the year ended 31st March, 2021 after providing 35% of the profits towards provision for taxation and transferring 25% of the profit to Statutory Reserves:

Particulars	Rs. in lakhs	Particulars	Rs. in lakhs
Interest on Cash Credit	364	Interest paid on Recurring Deposits	17
Interest on Overdraft	150	Interest paid on Savings Bank Deposits	12
Interest on Term Loans	308	Auditor's Fees and Allowances	24
Income on Investments	168	Directors' Fees and Allowance	50
Interest on Balance with RBI	30	Advertisement	36
Commission on remittances and transfer	15	Salaries, allowances and bonus to employees	248
Commission on Letters of Credit	24	Payment to Provident Fund	56
Commission on Government Business	16	Printing & Stationery	28
Profit on Sale of Land & Building	5	Repairs & Maintenance	10
Loss on exchange transactions	10	Postage, courier & telephones	16
Interest paid on Fixed Deposits	25		

Other Information:

	Rs. in lakhs	
	Earned	**Collected**
Interest on NPA is as follows:		
Cash Credit	164	80
Term Loans	90	20
Overdraft	150	50
Classification of Non-performing Advances:		
Standard	60	
Sub-standard-fully secured	22	
Doubtful assets-fully unsecured	40	
Doubtful assets covered fully by security:		
Less than 1 year	6	
More than 1 year upto 3 years	3	
More than 3 years	2	
Loss Assets	38	

Solution :

Sun Bank Limited
Profit and Loss Account
For the year ended 31st March, 2021

Rs. in lakhs

	Particulars	**Schedule**	**Year ended 31-03-2021**
I	Income		
	Interest earned	13	766
	Other income	14	50
			816
II	Expenditure		
	Interest expended	15	54
	Operating expenses	16	468
	Provisions and Contingencies (Refer W.N.)		158.96
			680.96
III	Profit/Loss		
	Net Profit/(Loss) for the year		135.04
	Net Profit/(Loss) brought forward		Nil
			135.04
IV	Appropriations:		
	Transfer to Statutory reserve (25% of the profits)		33.76
	Balance carried to the balance sheet		101.28
	Total		135.04

Schedule 13 - Interest Earned

	Particulars		Year ended 31-3-2021 (Rs. in lakhs)
I	Interest/discount on advances/bills		
	Interest on cash credit (364-84)	280	
	Interest on overdraft (150-100)	50	
	Interest on term loans (308-70)	238	568
II	Income on investments		168
III	Interest on Balance with RBI		30
			766

Interest on NPA is recognized on cash basis, hence difference of accrued interest not received have been reduced from the total accrued interest.

Schedule 14 - Other Income

	Particulars		Year ended 31-3-2021 (Rs. in lakhs)
I	Commission, Exchange and Brokerage:		
	Commission on remittances and transfer	15	
	Commission on letter of credit	24	
	Commission on Government business	16	55
II	Profit on sale of Land and Building		5
III	Loss on Exchange Transactions		(10)
			50

Schedule 15 - Interest Expended

	Particulars		Year ended 31-3-2021 (Rs. in lakhs)
I	Interest on Deposits		
	Fixed deposits	25	
	Recurring deposits	17	
	Saving bank deposits	12	54

Schedule 16 - Operating Expenses

	Particulars		Year ended 31-3-2021 (Rs. in lakhs)
I	Payment to and provision for employees		
	Salaries, allowances and bonus	248	
	Provident Fund Contribution	56	304
II	Printing and Stationery		28

III	Advertisement and publicity		36
IV	Directors' fees, allowances and expenses		50
V	Auditors' fees and expenses		24
VI	Postage, telegrams, telephones etc.		16
VII	Repairs and maintenance		10
			468

Working Note :

Provisions and contingencies			**(Rs. in lakhs)**
Provision for Advances:			
Standard	60 × 0.40%		0.24
Sub-standard	22 × 15%		3.3
Doubtful not covered by security	40× 100%		40
Doubtful covered by security:			
Less than 1 year	6 x 25%	1.5	
More than 1 year but less than 3 years	3 x 40%	1.2	
More than 3 years	2 x 100%	2.0	4.7
Loss Assets	(38 × 100%)		38
			86.24
Provision for tax	35% of (Total Income – Total Expenditure) 35% of [816-(54+468+86.24)] 35% of [816 - 608.24] 35% of 207.76		72.72
			158.96

Question 14 : Dec – 2021 – Paper

From the following information, you are required to prepare Profit and Loss account of Popular Bank for the year ended 31st March, 2021.

Particulars	**(Rs.)**
Interest on cash credit	13,65,000
Interest on overdraft	5,62,500
Interest on term loans	11,55,000
Income on investments	6,30,000
Interest on balance with RBI	1,12,500
Commission on remittances and transfer	56,250
Commission on letters of credit	88,500
Commission on government business	61,500
Profit on sale of land and building	20,250
Loss on exchange transactions	39,000
Interest paid on deposit	20,40,000
Auditor's fees and allowances	90,000

Directors' fees and allowances	1,87,500
Advertisements	1,35,000
Salaries, allowances and bonus to employees	9,30,000
Payment to Provide Fund	2,10,000
Printing and Stationery	1,05,000
Repairs and maintenance	37,500
Postage, telegrams , telephones	60,000

Other information :

(i) Interest on NPA is as follows :

Particulars	**Earned (Rs.)**	**Collected (Rs.)**
Cash credit	6,15,000	3,00,000
Overdraft	3,37,500	75,000
Term loans	5,62,500	1,87,500

(ii) Classification of Non Performing Advances

	(Rs.)
Standard	22,50,000
Sub-standard	8,40,000
Doubtful assets not covered by security	1,50,000
Doubtful assets covered by security for one year	37,500
Loss Assets	1,50,000

(iii) Investment Rs.20,62,500

Bank should not keep more than 25% of its investment as 'Held-to-Maturity'. The market value of its rest 75% investment is Rs.14,81,250 as on 31st March, 2021.

Solution :

Popular Bank
Profit and Loss Account
For the year ended 31st March, 2021

	Particulars	**Schedule**	**Year ended 31-3-2021 (Rs.)**
I	Income		
	Interest earned	13	28,72,500
	Other income	14	1,87,500
			30,60,000
II	Expenditure		
	Interest expended	15	20,40,000
	Operating expenses	16	17,55,000
	Provisions and Contingencies (W.N)		5,10,000

			43,05,000
III	Profit/Loss		(12,45,000)
IV	Appropriations		Nil

Schedule 13 - Interest Earned

		Year ended 31-3-2021 (Rs.)	
I	Interest/discount on advances/bills		
	Interest on cash credit Rs. (13,65,000-3,15,000)	10,50,000	
	Interest on overdraft Rs. (5,62,500-2,62,500)	3,00,000	
	Interest on term loans Rs. (11,55,000-3,75,000)	7,80,000	21,30,000
II	Income on investments		6,30,000
III	Interest on Balance with RBI		1,12,500
			28,72,500

Interest on NPA is recognized on cash basis, hence excess reduced.

Schedule 14 - Other Income

		Year ended 31-3-2021 (Rs.)	
I	Commission, Exchange and Brokerage		
	Commission on remittances and transfer	56,250	
	Commission on letter of credit	88,500	
	Commission on Government business	61,500	2,06,250
II	Profit on sale of Land and Building		20,250
III	Loss on Exchange Transactions		(39,000)
			1,87,500

Schedule 15 - Interest Expended

		Year ended 31-3-2021 (Rs.)
I	Interest on Deposits	20,40,000

Schedule 16 - Operating Expenses

		Year ended 31-3-2021 (Rs.)	
I	Payment and provision for employees		
	Salaries, allowances and bonus	9,30,000	
	Provident Fund Contribution	2,10,000	11,40,000
II	Printing and Stationery		1,05,000
III	Advertisement and publicity		1,35,000
IV	Directors' fees and allowances		1,87,500
V	Auditors' fees and expenses		90,000
VI	Postage, telegrams, telephones etc.		60,000
VII	Repairs and maintenance		37,500
			17,55,000

Working Note:

Provisions and contingencies			**(Rs.)**
Provision for NPA:			
Standard	22,50,000 × 0.40%		9,000
Sub-standard	8,40,000 × 15%*		1,26,000
Doubtful not covered by security	1,50,000 × 100%		1,50,000
Doubtful covered by security for one year	37,500 × 25%		9,375
Loss Assets	1,50,000 × 100%		1,50,000
			4,44,375
Depreciation on current investments			
Cost (75% of 20,62,500)		15,46,875	
Less: Market value		(14,81,250)	65,625
			5,10,000

Note: 25% of the total investments are held to maturity. In the case of Held to Maturity investments the valuation is done at cost and these are not marked to market value generally. Hence, depreciation on investments has been calculated only on other investments which can either be Held for Trading (HFT) or Available for Sale (AFS).

Question 15 : May – 2022 – RTP

The following figures are available from the books of Star Bank Ltd. for the year ended 31st March, 2021.

	Amount in Rs.
Interest and Discounts Received	1,52,00,640
Interest Paid on Deposits	91,81,440
Salaries and Allowances	10,00,000
Directors' Fees and Allowances	1,40,000
Rent and Taxes Paid	4,00,000
Postage	2,61,360
Statutory Reserve Fund	32,00,000
Commission, Exchange and Brokerage Earned	7,60,000
Rent Received	2,88,000
Profit on sale of Investments	9,03,200
Depreciation on Assets	1,60,000
Statutory Expenses	1,52,000
Preliminary Expenses	1,20,000
Auditors' Fees	48,000

The following further information is also available:

(i) Issued and Subscribed Capital of the Bank is Rs. 40,00,000

(ii) Preliminary Expenses to be fully written off during the year.

(iii) Rebate on Bills Discounted was Rs. 60,000 as on 31st March, 2020 and was Rs. 80,000 on 31st March, 2021.

(iv) Transfer 25% of the profits to statutory reserves.

(v) Income Tax of Rs. 8,00,000 is to be provided.

(vi) Mr. G, a customer of the bank, who had taken an advance of Rs. 40,00,000 from the bank became insolvent and only 25% was expected to be recovered from his estate.

(vii) A provision of Rs. 8,00,000 was also necessary on other debts.

(viii) There was no opening balance of Profit and Loss Account.

You are required to prepare the Profit and Loss Account and the Schedules of Profit and Loss Account of Star bank for the year ended 31st March, 2021. Also show how the Profit and Loss Account will appear in the Balance Sheet.

Solution :

Star Bank Limited

Profit and Loss Account for the year ended 31st March, 2021

		Schedule	Year ended 31.03.2021 Rs.
I.	Income:		
	Interest earned	13	1,51,80,640
	Other income	14	19,51,200
	Total		1,71,31,840
II.	Expenditure		
	Interest expended	15	91,81,440
	Operating expenses	16	22,81,360
	Provisions and contingencies (W.N.1)		46,00,000
	Total		1,60,62,800
III.	Profits/Losses		
	Net profit for the year		10,69,040
	Profit brought forward		Nil
			10,69,040
IV.	Appropriations		
	Transfer to statutory reserve (25% of 10,69,040)		2,67,260
	Balance carried over to balance sheet		8,01,780
			10,69,040

Profit & Loss Account balance of Rs. 8,01,780 will appear under the head 'Reserves and Surplus' in Schedule 2 of the Balance Sheet.

		Year ended 31.3.2021 (Rs.)
	Schedule 13 – Interest Earned	
I.	Interest/discount on advances/bills (Refer W.N. 2)	1,51,80,640
		1,51,80,640
	Schedule 14 – Other Income	
I.	Commission, exchange and brokerage	7,60,000
II.	Profit on sale of investment	9,03,200
III.	Rent received	2,88,000
		19,51,200
	Schedule 15 – Interest Expended	
I.	Interests paid on deposits	91,81,440
		91,81,440
	Schedule 16 – Operating Expenses	
I.	Payment to and provisions for employees (salaries & allowances)	10,00,000
II.	Rent, taxes paid	4,00,000
III.	Depreciation on assets	1,60,000
IV.	Director's fee, allowances and expenses	1,40,000
V.	Auditor's fee	48,000
VI.	Statutory expenses	1,52,000
VII.	Postage	2,61,360
VIII.	Preliminary expenses	1,20,000
		22,81,360

Working Notes:

1. Provisions and contingencies

	Rs.
Provision on advance to Mr. G	30,00,000
Provision on other debts	8,00,000
Provision for Income tax	8,00,000
	46,00,000

2. Interest and discount earned

	Rs.
Interest and discount received	1,52,00,640
Add: Rebate on bills discounted on 31.3. 2020	60,000
Less: Rebate on bills discounted on 31.3. 2021	(80,000)
	1,51,80,640

Question 16 : May – 2022 – Paper

(i) Write a short note on Non-performing assets of a banking company.

(ii) Dee Bank provides you the following information relating to their two cash credit accounts:

	Account A Rs.in Lakhs	Account B Rs.in Lakhs
Sanctioned limit	4,500	3,200
Drawing power	4,200	2,500
Amount outstanding continuously from 01.01.2021 to 31.03.2021	3,600	2,000
Total Interest debited for the above period	288	315
Total credits for the above period	120	380

State with reason whether the above cash credit accounts are NPA or not ?

Solution :

(i) Performing assets are also called as Standard Assets. A non-performing asset is a loan or advance for which the principal or interest payment remains overdue for a period of 90 days. The assets other than performing assets are called Non-Performing Assets (NPA). NPAs are classified into three groups: (a) sub-standard Assets (b) doubtful assets & (c) Loss Assets.

(a) **Sub-standard Assets** –A Sub-standard asset is one which has been classified as an NPA for a period not exceeding 12 months.

(b) **Doubtful Assets** - An asset would be classified as doubtful if it has remained in the substandard category for a period of at least12 months.

(c) **Loss Assets** - A loss asset is one where loss has been identified by the bank or internal or external auditors or the RBI inspectors but the amount has not been written off, wholly or partly. In other words, such an asset is considered uncollectible or if collected of such little value that its continuance as a bank asset is not warranted although there may be some salvage or recovery value.

Income from non-performing assets can only be accounted for as and when it is actually received.

(ii)

	Account A Rs. in lakhs	Account B Rs. in lakhs
Sanctioned limit	4,500	3,200
Drawing power	4,200	2,500
Amount outstanding continuously from 1.01.2021 to 31.03.2021	3,600	2,000

Total interest debited	288	315
Total credits	120	380
Is credit in the account is sufficient to cover the interest debited during the period? or	No	Yes
Is amount 'overdue' for a continuous period of 90 days?	Yes	No
	NPA	Not NPA

Question 17: Nov – 2022 – RTP

The following are the figures extracted from the books of TOP Bank Limited as on 31.3.2022.

	Rs.
Interest and discount received	59,29,180
Interest paid on deposits	32,59,920
Issued and subscribed capital	16,00,000
Salaries and allowances	3,20,000
Directors fee and allowances	48,000
Rent and taxes paid	1,44,000
Postage and telegrams	96,460
Statutory reserve fund	12,80,000
Commission, exchange and brokerage	3,04,000
Rent received	1,04,000
Profit on sale of investments	3,20,000
Depreciation on bank's properties	48,000
Statutory expenses	44,000
Preliminary expenses	40,000
Auditor's fee	28,000

The following further information is given:

(i) A customer to whom a sum of Rs. 16 lakhs has been advanced has become insolvent and it is expected only 40% can be recovered from his estate.

(ii) There were also other debts for which a provision of Rs. 2,10,000 was found necessary by the auditors.

(iii) Rebate on bills discounted on 31.3.2021 was Rs. 19,000 and on 31.3.2022 was Rs. 25,000.

(iv) Preliminary expenses are to be fully written off during the year.

(v) Provide Rs. 9,00,000 for Income-tax.

(vi) Profit and Loss account opening balance was Nil as on 31.3.2021.

Prepare the Profit and Loss account of TOP Bank Limited for the year ended 31.3.2022.

Solution :

TOP Bank Limited

Profit and Loss Account for the year ended 31st March, 2022

		Schedule	Year ended 31.03.2022
			(Rs. in '000s)
I.	**Income:**		
	Interest earned	13	5923.18
	Other income	14	728.00
	Total		6,651.18
II.	**Expenditure**		
	Interest expended	15	3259.92
	Operating expenses	16	768.46
	Provisions and contingencies (960+210+900)		2,070.00
	Total		6,098.38
III.	**Profits/Losses**		
	Net profit for the year		552.80
	Profit brought forward		Nil
			552.80
IV.	**Appropriations**		
	Transfer to statutory reserve (25%)		138.20
	Balance carried over to balance sheet		414.60
			552.80

		Year ended 31.03.2022
		(Rs. in '000s)
	Schedule 13 – Interest Earned	
I.	Interest/discount on advances/bills (Refer W.N.)	5,923.18
		5,923.18
	Schedule 14 – Other Income	
I.	Commission, exchange and brokerage	304
II.	Profit on sale of investments	320
III.	Rent received	104
		728
	Schedule 15 – Interest Expended	
I.	Interests paid on deposits	3,259.92
	Schedule 16 – Operating Expenses	

I.	Payment to and provisions for employees	320
II.	Rent and taxes	144
III.	Depreciation on bank's properties	48
IV.	Director's fee, allowances and expenses	48
V.	Auditors' fee	28
VI.	Law (statutory) charges	44
VII.	Postage and telegrams	96.46
VIII.	Preliminary expenses	40
		768.46

Working Note:

	(Rs. in '000s)
Interest/discount	5,929.18
Add: Rebate on bills discounted on 31.3. 2021	19.00
Less: Rebate on bills discounted on 31.3. 2022	(25.00)
	5,923.18

Question 18: Nov – 2022 – Paper

Following information of RJS Bank Limited for the year ended 31st March, 2022 are as under:

Particulars	Rs. in '000
Total interest earned and received on term loans	6375.00
Interest earned on term loans classified as NPA	1827.50
Interest received on term loans classified as NPA	595.00
Total interest earned on cash credits and overdrafts	14157.50
Interest earned but not received on cash credits and overdrafts treated as NPA	2307.50
Interest on Deposits	10300.00
Commission, exchange and brokerage	502.50
Profit on sale of Investments	4690.00
Profit on revaluation of Investments	855.00
Income from Investments	5435.00
Payment to and provision for employees	6862.50
Rent, Taxes and Lighting	962.50
Printing and Stationery	155.00
Director's fees, allowances and expenses	782.50
Repairs and Maintenance	140.00
Depreciation on Bank's property	247.50
Insurance	107.50

Classification of Assets :

Particulars	**? in '000**
Standard [including advances to Commercial Real Estate (CRE) sector Rs.17,50,000]	11,750
Sub-standard (fully secured)	4,750
Doubtful Assets not covered by security	1,000
Doubtful Assets covered by security for 1 year	100
Loss Assets	750

You are required to :

Prepare Profit and Loss account of RJS Bank Limited including Schedules for the year ended 31st March, 2022 and calculate provision required to be made on Risk Assets.

Thanks ....

Rahul Malkan

CHAPTER 21

NON-BANKING FINANCIAL COMPANIES

Question 1 : May – 2018 – Paper

Preeti has invested in three mutual funds. From the details given below, find out effective yield on per annum basis to Preeti in respect of each of the schemes upto 31st March, 2017:

Mutual Fund	**X**	**Y**	**Z**
Date of Investment	1.12.2016	1/1/2017	1/3/2017
Amount of Investment (Rs.)	2,50,000	3,00,000	1,50,000
NAV at the date of investment (Rs.)	10.00	10.50	10.00
Dividend received upto 31st March, 2017 (Rs.)	4,500	5,700	Nil
NAV as at 31st March, 2017 (Rs.)	10.10	10.40	9.80

Solution :

Calculation of effective yield on per annum basis in respect of three mutual fund schemes of Preeti upto 31.03.2017

		X	**Y**	**Z**
1	Amount of Investment (Rs.)	2,50,000	3,00,000	1,50,000
2	Date of investment	1.12.2016	1.1.2017	1.3.2017
3	NAV at the date of investment (Rs.)	10.00	10.50	10.00
4	No. of units on date of investment [1/3]	25,000	28,571.43	15,000
5	NAV per unit on 31.03.2017 (Rs.)	10.10	10.40	9.80
6	Total NAV of mutual fund investments on 31.03.2017 [4 x 5]	2,52,500	2,97,143	1,47,000
7	Increase/ decrease of NAV [6-1]	2,500	(2,857)	(3,000)
8	Dividend received up to 31.3.2017	4,500	5,700	Nil
9	Total yield [7+8]	7,000	2,843	(3,000)
10	Yield % [9/1] x 100	2.80%	0.95%	(2%)
11	Number of days	121	90	31
12	Effective yield p.a. [10/11] x 365 days	8.45%	3.85%	(23.55%)

Question 2 : May – 2018 – Paper

ABC Financiers Ltd. is an NBFC providing Hire Purchase Solutions for acquiring consumer durables. The following information is extracted from its books for the year ending 31st March, 2017:

Assets Funded	Interest Overdue but recognised in Profit & Loss		Net book value of Assets outstanding
	Paid Overdue	Interest (Rs. in lakhs)	(Rs.in lakhs)
Computers	Upto 12 months	960.00	40812.00
Televisions	For 20 months	205.00	4950.00
Washing Machines	For 32 months	104.20	2530.00
Refrigerators	For 45 months	53.50	1328.00
Air-conditioners	For 52 months	13.85	305.00

You are required to calculate the amount of provision to be made.

Solution :

Amount of provision to be made is as under:

Asset Funded			(Rs. in crore)
Computers	(a) Where hire charges are overdue upto 12 months	Nil	-
Televisions	(b) Where hire charges are overdue for more than 12 months but upto 24 months	10% of the net book value 10% x 4,950	495
Washing Machines	(c) Where hire charges are overdue for more than 24 months but upto 36 months	40 percent of the net book value 40% x 2,530	1,012
Refrigerators	(d) Where hire charges or lease rentals are overdue for more than 36 months but upto 48 months	70 percent of the net book value 70% x 1,328	929.6
Air Conditioners	(e) where hire charges or lease rentals are overdue for more than 48 months	100 percent of the net book value 305 x 100%	305
		Total	2,741.60

Question 3 : Nov – 2018 – Paper

While closing its books of accounts on 31st March 2018, a Non-Banking Finance Company has its advances classified as follows

	Rs. (in lakhs)
Standard assets	18,400
Sub-standard assets	1,250
Secured Portion of doubtful debts:	
Upto one year	300
One year to three years	90
More than three years	30
Unsecured portions of doubtful debts	92
Loss assets	47

Calculate the amount of provision which must be made against the Advances as per -

(i) The Non-banking Financial Company - Non-systematically Important Non-Deposit taking Company (Reserve Bank) Directions, 2016; and

(ii) Non-banking Financial Company - Systematically Important Non- Deposit taking Company (Reserve Bank) Directions, 2016.

Solution :

Calculation of provision required on advances as on 31st March, 2018 as per the Non-Banking Financial Company – Non-Systemically Important Non-Deposit taking Company (Reserve Bank) Directions, 2016

	Amount Rs. in lakhs	Percentage of provision	Provision Rs. in lakhs
Standard assets	18,400	0.25	46.00
Sub-standard assets	1,250	10	125.00
Secured portions of doubtful debts–			
– upto one year	300	20	60.00
– one year to three years	90	30	27.00
– more than three years	30	50	15.00
Unsecured portions of doubtful debts	92	100	92.00
Loss assets	47	100	47.00
			412.00

Calculation of provision required on advances as on 31st March, 2018 as per the Non-Banking Financial Company - Systemically Important Non-Deposit taking Company and Deposit taking Company (Reserve Bank) Directions, 2016

	Amount Rs. in lakhs	Percentage of provision	Provision Rs. in lakhs
Standard assets	18,400	0.40*	73.60
Sub-standard assets	1,250	10	125.00
Secured portions of doubtful debts–			
– upto one year	300	20	60.00
– one year to three years	90	30	27.00
– more than three years	30	50	15.00
Unsecured portions of doubtful debts	92	100	92.00
Loss assets	47	100	47.00
			439.60

***Note:** For the year ending on 31st March, 2018, the provision rate for standard assets is 0.40%.

Question 4 : Nov – 2018 – Paper

A Mutual Fund raised funds on 1st April, 2018 by issuing 10 lakhs units @ Rs. 20 per unit. Out of this Fund, Rs. 180 lakhs invested in several capital market securities. The initial expenses amount to Rs. 9 lakhs. During June, 2018, the fund sold certain securities of cost Rs. 140 lakhs for Rs. 175 lakhs and it bought certain securities for Rs. 125 lakhs. The Fund Management expenses

amounted to Rs. 5 lakhs per month and Rs. 0.75 lakh was in arrear. The dividend earned was Rs. 4.50 lakhs 80% of the realized earnings were distributed among the unit holders. The market value of the portfolio was Rs. 225 lakhs. Determine the Net Asset Value (NAV) per unit as on 30th June, 2018.

Solution :

	Rs. in lakhs	Rs. in lakhs
Opening bank balance [Rs. (200 – 180 - 9) lakhs]	11	
Add: Proceeds from sale of securities	175	
Dividend received	4.50	
		190.5
Less: Cost of securities	125	
Fund management expenses		
[Rs. (15–0.75) lakhs]	14.25	
Capital gains distributed		
[80% of Rs. (175 – 140) lakhs]	28	
Dividends distributed (80% of Rs. 4.5 lakhs)	3.6	
		(170.85)
Closing bank balance		19.65
Closing market value of portfolio		225
		244.65
Less: Arrears of expenses		(0.75)
Closing net assets(A)		243.9
Number of units (B)		10,00,000
Closing Net Assets Value (NAV) per unit (A/B)		**Rs. 24.39**

Question 5 : Nov – 2018 – Paper

Mutual fund has launched a new scheme "All Purpose Scheme". The Mutual Fund Asset Management Company wishes to Invest 25% of the NAV of the scheme in an unrated debt instrument of a company Zed Ltd., which has been paying above average returns for the past many years. The promoters of the company seek advice in light of the regulations of SEBI. Will the position change in case the debt instruments of the company Zed Ltd. are rated.

Solution :

The Seventh Schedule of SEBI (Mutual funds) Regulations, 1996 states that a mutual fund scheme shall not invest more than 10% of its NAV in unrated debt instruments issued by a single issuer and the total investment in such instruments shall not exceed 25% of the NAV of the scheme. All such investments shall be made with the prior approval of the Board of Trustees and the Board of Asset Management Company.

It also states that a mutual fund scheme shall not invest more than 10% of its NAV in debt instruments issued by a single issuer which are rated not below investment grade by an authorized credit rating agency. Such investment limit may be extended to 12% of the NAV of the

scheme with the prior approval of the Board of Trustees and the Board of Asset Management Company.

Accordingly, if the debts instruments of Zed Ltd. are unrated then Mutual Fund Asset Management Company (AMC) cannot invest more than 10% of its NAV in those instruments. If the debts instruments of Zed Ltd. are rated, even then, Mutual Fund Asset Management Company cannot invest more than 12% of its NAV in those instruments. Therefore, investment of 25% of its NAV of the scheme in debts instrument of Zed Ltd. by Mutual Fund Asset Management Company is not permissible as per the SEBI (Mutual Fund) Regulations, 1996.

Question 6 : May – 2019 – RTP / May – 2020 – RTP / Nov – 2020 – Paper / Jan – 2021 - Paper

LK Finance Ltd. is a non-banking financial company. It provides you with the following information regarding its outstanding amount, Rs. 400 lakhs of which installments are overdue on 400 accounts for last two months (amount overdue Rs. 80 lakhs), on 24 accounts for three months (amount overdue Rs. 48 lakhs), on 10 accounts for more than 30 months (amount overdue Rs. 40 lakhs) and on 4 accounts for more than three years (amount over due Rs. 40 lakhs-already identified as sub-standard assets) and one account of Rs. 20 lakhs which has been identified as non-recoverable by the management. Out of 10 accounts overdue for more than 30 months, 6 accounts are already identified as sub-standard (amount Rs. 12 lakhs) for more than fourteen months and other are identified as sub-standard asset for a period of less than fourteen months. Classify the assets of the company in line with Non-Banking Financial Company - Systemically Important Non-Deposit taking Company and Deposit taking Company (Reserve Bank) Directions, 2016.

Solution :

Statement showing classification as per Non-Banking Financial Company - Systemically Important Non-Deposit taking Company and Deposit taking Company (Reserve Bank) Directions, 2016

		Rs. in lakhs
Standard Assets		
Accounts (Balancing figure)	172.00	
400 accounts overdue for a period for 2 months	80.00	
24 accounts overdue for a period by 3 months	48.00	300.00
Sub-Standard Assets		
4 accounts identified as sub-standard asset for a period less than 14 months		28.00
Doubtful Debts		
6 accounts identified as sub-standard for a period more than 14 months		12.00
4 accounts identified as sub-standard for a period more than 3 years		40.00
Loss Assets		

1 account identified by management as loss asset	20.00
Total overdue	400.00

Question 7 : May – 2019 – RTP

What do you mean by "Net asset value" (NAV) in case of mutual fund units?

Solution :

The net asset value of a mutual fund scheme is basically the per unit market value of all the assets of the scheme. Simply stated, NAV is the value of the assets of each unit of the scheme, or even simpler value of one unit of the scheme. Thus, if the NAV is more than the face value (Rs. 10), it means your money has appreciated and vice versa. NAV also includes dividends, interest accruals and reduction of liabilities and expenses besides market value of investments. NAV is the value of net assets under a mutual fund scheme. NAV per unit is NAV of the scheme divided by number of units outstanding. NAV of a scheme keeps on changing with change in market value of portfolio under the scheme.

Net Asset Value (NAV) is calculated as under:

$$\frac{\text{Total market value of all Mutual Fund holdings - All Mutual Fund liabilities}}{\text{Unit size}}$$

Question 8 : May – 2019 – Paper / May – 2021 – RTP / July – 2021 – Paper / Nov – 2021 - RTP

Babu Bhai Financiers Ltd. is an NBFC providing Hire Purchase Solutions for acquiring consumer durables. The following information is extracted from its books for the year ended 31st March, 2018:

	Interest Overdue but recognised in Profit & Loss		Net book value of Assets outstanding
Assets Funded	**Paid Overdue**	**Interest (Rs. in crore)**	**(Rs.in crore)**
LCD Televisions	Up to 12 Months	500.00	20,000
Washing Machines	For 24 Months	100.00	2,000
Refrigerators	For 30 Months	50.00	1,250
Air Conditioners	For 45 Months	25.00	600
Mobile Phones	For 60 Months	10.00	100

You are required to calculate the amount of provision to be made

Solution :

On the basis of the information, in respect of hire purchase and leased assets, additional provision shall be made as under:

			(Rs. in crore)
(a)	Where hire charges are overdue upto 12 months	Nil	-
(b)	Where hire charges are overdue for more than 12 months upto 24 months	10% of the net book value 10% x 2,000	200

(c)	Where hire charges are overdue for more than 24 months upto 36 months	40 percent of the net book value 40% x 1,250	500
(d)	Where hire charges or lease rentals are overdue for more than 36 months but upto 48 months	70 percent of the net book value 70% x 600	420
(e)	Where hire charges or lease rentals are overdue for more than 48 hours	100% of net book value (100% x 100)	100
		Total	1,220

Question 9 : May – 2019 – Paper

A Mutual Fund purchased 20,000 debentures of a company on June 1, 2017 for Rs.21.40 lakh and further 10,000 debentures on 1st November, 2017 for Rs.10.90 lakh. The debentures carry fixed annual coupon of 12%, payable on every 31st March and 30th September. On Feb 28, 2018 the fund sold 12,000 of these debentures for Rs.13.56 lakh. Nominal value per debenture is Rs.100. Show Investment in Debentures A/c in books of the Mutual Fund.

Solution :

Investment in Debentures Account

		Rs. Lakh			Rs. Lakh
1-Jun-17	To Bank	21.40	1-Jun-17	By Interest Recoverable (Note 1)	0.40
1-Nov-17	To Bank	10.90	1-Nov-17	By Interest Recoverable (Note 2)	0.10
28-Feb-18	To Interest Recoverable (Note 3)	0.60	28-Feb-18	By Bank	13.56
28-Feb-18	To Profit on disposal (Note 4)	0.24	31-Mar-18	By Balance c/d	19.08
		33.14			**33.14**

Working Notes:

Note 1: 20,000 x 100 x 12/100 x 2/12 = Rs. 0.40 Lakhs

Note 2: 10,000 x 100 x 12/100 x 1/12 = Rs. 0.10 Lakhs

Note 3: 12,000 x 100 x 12/100 x 5/12 = Rs. 0.60 Lakhs

Note 4: Cost of investments (per unit) = [(21,40,000 – 40,000) +(10,90,000 – 10,000)]/30,000 units
= [21,00,000+ 10,80,000]/30,000 = Rs. 106

Cost of investments sold = Rs. 106 x 12,000 = Rs. 12,72,000

Sale proceeds = Rs. 13,56,000 - Rs. 60,000 (interest) = Rs. 12,96,000

Profit = Rs. 12,96,000 - Rs. 12,72,000 = Rs. 24,000

Question 10 : Nov – 2019 – RTP

While closing its books of account on 31st March, 2018 a Non-Banking Finance Company has its advances classified as follows:

	Rs. in lakhs
Standard assets	13,400
Sub-standard assets	670
Secured portions of doubtful debts:	
- Up to one year	160
- one year to three years	45
- more than three years	20
Unsecured portions of doubtful debts	48
Loss assets	24

You are required to Calculate the amount of provision, which must be made against the Advances as per the Non-Banking Financial Company –Systemically Important Non-Deposit taking Company (Reserve Bank) Directions, 2016.

Solution :

Calculation of provision required on advances as on 31st March, 2018:

	Amount Rs. in lakhs	Percentage of provision	Provision Rs. in lakhs
Standard assets	13,400	.40	53.60
Sub-standard assets	670	10	670
Secured portions of doubtful debts			
-up to one year	160	20	32
-one year to three years	45	30	13.5
-more than three years	20	50	10
Unsecured portions of doubtful debts	48	100	48
Loss assets	24	100	24
			851.10

Question 11 : Nov – 2019 – RTP

Surakshit Mutual Fund is registered with SEBI and is in the process of finalizing the annual statement of accounts of one of its open ended mutual fund schemes. From the information furnished below, you are required to prepare a statement showing the movement of unit holders' funds for the financial year ended 31st March, 2018.

	Rs. in '000
Opening Balance of net assets	54,00,000
Net Income for the year (Audited)	3,82,500
38,25,900 units issued during 2017-2018	4,34,250
33,85,350 units redeemed during 2017-2018	3,20,940
The par value per unit is Rs.100	

Solution :

Statement showing the Movement of Unit Holders' Funds for the year ended 31st March, 2018

	(Rs. '000)
Opening balance of net assets	54,00,000
Add: Par value of units issued (38,25,900 × Rs. 100)	3,82,590
Net Income for the year	3,82,500
Transfer from Reserve/Equalisation fund (Refer working note)	69,255
	62,34,345
Less: Par value of units redeemed (33,85,350 × Rs. 100)	(3,38,535)
Closing balance of net assets (as on 31st March, 2018)	58,95,810

Working Note :

Particulars	**Issued**	**Redeemed**
Units	38,25,900	33,85,350
	Rs. 000	Rs. 000
Par value	3,82,590	3,38,535
Sale proceeds / Redemption value	4,34,250	3,20,940
Profit transferred to Reserve / Equalization Fund	51,660	17,595
Balance in Reserve / Equalization Fund (Issued & Redeemed)	69,255	

Question 12 : Nov – 2019 – Paper

The investment portfolio of a mutual fund scheme includes 4,000 shares of P Ltd. and 3,200 shares of Q Ltd. acquired on 31-12-2017. The cost of P Ltd.'s share is Rs.50 and Q Ltd.'s share is Rs.75. The market value of these shares at the end of 2017-18 were Rs.47 and Rs.80 respectively. On 30th June, 2018 shares of both companies were disposed off realizing:

P Ltd.'s share at Rs.40 and

Q Ltd.' s share at Rs.82

Show important accounting entries in the books of the fund for the accounting years 2017-18 and 2018-19.

Solution :

Journal Entries :

			Rs. 000	**Rs. 000**
31.12.17	Investment in P Ltd's Shares	Dr.	200	
	Investment in Q Ltd's Shares	Dr.	240	
	To Bank			440
	(Being purchase of P Ltd., 4,000 shares @ Rs. 50 and 3,200 shares of Q Ltd., @ Rs. 75 each)			
31.3.18	Revenue A/c	Dr.	12	
	To Provision for Depreciation			12

	(Being market value of P Ltd shares depreciated for Rs. 3 each for 4,000 shares)			
	Investment in Q Ltd's Shares To Unrealised Appreciation Reserve (Being 3,200 shares of Q Ltd., appreciated @ Rs. 5 each per share on the closing date)	Dr.	16	 16
1.04.18	Unrealised Appreciation Reserve To Investment in Q Ltd's Shares (Being last year's reserve reversed)	Dr.	16	 16
30.6.18	Bank Account Loss on disposal of Investment To Investment in P Ltd. Shares (Being Rs. 2,00,000 of P Ltd. shares sold for Rs. 1,60,000)	Dr. Dr.	160 40	 200
	Provision for Depreciation Revenue A/c To Loss on disposal of Investment (Earlier depreciation provision provided being reversed on disposal of total shares of P Ltd. and the balance amount debited to Revenue Account)	Dr. Dr.	12 28	 40
	Bank Account To Investment in Q Ltd. Shares To Revenue A/c (Being 3,200 shares of Q Ltd. sold @ Rs. 82 accounted on the trade date since this is a regular transaction in the business)	Dr.	264.4	 240 22.4

Question 13 : Nov – 2020 – RTP

Write short note on Earning value (Equity share) as per NBFC Prudential Norms (RBI) directions.

Solution :

Earning value means the value of an equity share computed by taking the average of profits after tax as reduced by the preference dividend and adjusted for extra-ordinary and non-recurring items, for the immediately preceding three years and further divided by the number of equity shares of the investee company and capitalized at the following rate:

- in case of predominantly manufacturing company, eight per cent;
- in case of predominantly trading company, ten per cent; and
- in case of any other company, including non-banking financial company, twelve per cent;

Note: If an investee company is a loss making company the earning value will be taken at zero.

Question 14 : Nov – 2020 – RTP

While closing its books of account on 31st March, 2019 a Non-Banking Finance Company has its advances classified as follows:

	Rs.in lakhs
Sub-standard assets	2,680
Secured portions of doubtful debts:	
- Up to one year	640
- one year to three years	180
- more than three years	60
Unsecured portions of doubtful debts	194
Loss assets	96

Solution :

Calculation of provision required on advances as on 31st March, 2019 :

	Amount Rs. in lakhs	Percentage of provision	Provision Rs. in lakhs
Sub-standard assets	2,680	10	268.00
Secured portions of doubtful debts			
-up to one year	640	20	128.00
-one year to three years	180	30	54.00
-more than three years	60	50	30.00
Unsecured portions of doubtful debts	194	100	194.00
Loss assets	96	100	96.00
			770.00

Question 15 : Nov – 2020 – Paper

Vikas Finance Ltd is a Non-Banking Finance Company. The extracts of its Balance Sheet are as under

Liabilities	(Rs. In '000)	Assets	(Rs. In '000)
Paid up Equity Capital	250	Leased Out Assets	2,000
Free Reserves	1,250	**Investments**	
Loans	1,000	In Shares of subsidiaries and	
Deposits	1,000	Group Companies	275
		In Debentures of subsidiaries	
		and Group companies	558
		Cash & Bank Balances	500
		Deferred Expenditures	500
Total	**3,500**	**Total**	**3,500**

You are requested to compute the "Net Owned Funds" of Vikas Finance Ltd. as per Non-Banking Company – Systematically Important Non- Deposit taking company and Deposit taking company (Reserve Bank) Directions, 2016.

Solution :

Statement showing computation of 'Net Owned Fund'

		Rs. in 000
Paid up Equity Capital		250
Free Reserves		1,250
		1,500
Less: Deferred expenditure		(500)
	A	1,000
Investments		
In shares of subsidiaries and group companies		275
In debentures of subsidiaries and group companies		225
	B	500
10% of A		100
Excess of Investment over 10% of A (500-100)	C	400
Net Owned Fund [(A) - (C)] (1,000-400)		600

Question 16 : May – 2021 – RTP

Calculate 'Owned Fund' of a NBFC based on the following facts:
Paid up share capital: Rs. 400 lakhs
Free reserves: Rs. 200 lakhs
Securities Premium: Rs. 50 lakhs
Capital Reserves (surplus arising due to sale of assets): Rs.100 lakhs
Compulsory convertible preference shares (CCPS): Rs. 50 lakhs
Revaluation Reserve: Rs. 100 lakhs

Solution :

Owned fund calculation:
Paid up share capital: Rs. 400 lakhs
Free reserves: Rs. 200 lakhs
Compulsory convertible preference shares (CCPS): Rs. 50 lakhs
Securities Premium: Rs. 50 lakhs
Capital reserve: Rs. 100 lakhs
Total Owned fund: Rs. 800 lakhs ie. Rs. (400+200+50+50+100) lakhs

Question 17 : Nov – 2021 – RTP

Gaur Finance Ltd. is a non-banking finance company. It provides the following information:

	Rs. in crores
Leased out assets	600
Investment:	
In shares of subsidiaries and group companies	150
In debentures of subsidiaries and group Companies	50
Cash and bank balances	200

Deferred expenditure	100
Paid-up equity capital	100
Free reserves	400
Loans	400
Deposits	400

You are required to compute 'Net owned Fund' of Gaur Finance Ltd. as per Non-Banking Financial Company - Systemically Important Non-Deposit taking Company and Deposit taking Company (Reserve Bank) Directions, 2016.

Solution :

Statement showing computation of 'Net Owned Fund'

		Rs. in crores
Paid up Equity Capital		100
Free Reserves		400
		500
Less: Deferred expenditure		(100)
	A	400
Investments		
In shares of subsidiaries and group companies		150
In debentures of subsidiaries and group companies		50
	B	200
10% of A		40
Excess of Investment over 10% of A (200-40)	C	160
Net Owned Fund [(A) - (C)] (400-160)		240

Question 18 : Dec – 2021 – Paper

GEM Ltd. is a NBFC providing Hire Purchase solutions for acquiring consumer durables. The following information is extracted from its books for the year ended 31st March, 2021.

Particulars	**Rs. In lakhs**
Paid up Equity Capital	2520
Compulsory convertible preference shares	1035
Free Reserve	243
Share premium	56
Capital Reserve	319
(Rs.220 Lakhs surplus arising out of sale Building)	
Deferred revenue expenditure	54
Debenture issued	702
Cash & Bank Balances	243
Investments in debentures of subsidiaries	171
Investments in shares of other NBFC	942

You are required to calculate Owned Fund and Net owned Fund.

Solution :

Statement showing computation of 'Owned Fund' and 'Net Owned Fund'

		Rs. in lakhs
Paid up Equity Capital		2,520
Free Reserves		243
Compulsory convertible preference shares		1035
Securities Premium		56
Capital Reserve (arising out of sale of building)		220
		4074
Less: Deferred revenue expenditure		(54)
Owned Fund	A	4020
Investments		
In shares of other NBFC		945
In debentures of subsidiaries and group companies		171
	B	1116
10% of A		402
Excess of Investment over 10% of A (1116-402)	C	714
Net Owned Fund [(A) - (C)] (4020-714)		3306

Question 19 : May – 2022 – RTP

Calculate 'Owned Fund' of an NBFC based on the following information:
Paid up share capital: Rs. 200 lakhs
Free reserves: Rs. 150 lakhs
Compulsory convertible preference shares (CCPS): Rs. 50 lakhs
Revaluation reserve: Rs. 50 lakhs (created by revaluation of assets)
Securities premium: Rs. 25 lakhs
Book value of intangible assets: Rs. 10 lakhs
Capital reserves (surplus arising out of sale proceeds of assets): Rs. 15 lakhs

Solution :

Owned fund calculation:
Paid up share capital: Rs. 200 lakhs
Free reserves: Rs. 150 lakhs
Compulsory convertible preference shares (CCPS): Rs. 50 lakhs
Securities premium: Rs. 25 lakhs
Capital Reserves : 15 lakhs
Total of all above items : Rs. 440 lakhs reduced by the value of intangible assets Rs. 10 lakhs ie. owned fund is computed as Rs. 430 lakhs.
Note: Revaluation reserve to be excluded while computing owned fund.

Question 20 : May – 2022 – RTP

While closing its books of account at year end, a Non-Banking Finance Company has its advances classified as follows:

Standard assets	Rs. in lakhs
Sub-standard assets	1,26,000
Secured portions of doubtful debts:	10,050
– up to one year	2,400
– one year to three years	675
– more than three years	225
Unsecured portions of doubtful debts	727
Loss assets	360

Calculate the amount of provision, which must be made against the advances as per the Non-Banking Financial Company – Non-Systemically Important Non-Deposit taking Company (Reserve Bank) Directions, 2016.

Solution :

Calculation of provision required on advances as at year end, as per the Non-Banking Financial Company – Non-Systemically Important Non-Deposit taking Company (Reserve Bank) Directions, 2016

	Amount Rs. in lakhs	Percentage of provision	Provision Rs. in lakhs
Standard assets	1,26,000	0.25	315.00
Sub-standard assets	10,050	10	1,050.00
Secured portions of doubtful debts–			
– upto one year	2,400	20	480.00
– one year to three years	675	30	202.50
– more than three years	225	50	112.50
Unsecured portions of doubtful debts	727	100	727.00
Loss assets	360	100	360.00
			3,247.00

Question 21 : Nov – 2022 – RTP

XYZ Finance Ltd. is a non-banking finance company. The extract of its balance sheet are as follows:

(Rs. in lakhs)

	Amount
Equity and Liabilities	
Paid-up equity capital	200
General Reserve	600
Non-Current Liabilities	
Loans	500
Deposits	600

	1,900
Assets	
Non-current assets	
Property Plant and Equipment	900
Investments:	
In shares of subsidiaries	250
In debentures of group companies	400
Current Assets	
Cash and bank balances	350
	1,900

You are required to compute 'Net Owned Fund' of XYZ Finance Ltd. as per Non-Banking Financial Company – Systemically Important Non-Deposit taking company and Deposit taking company (Reserve Bank) Directions, 2016.

Solution :

Statement showing computation of 'Net Owned Fund'

S.No.			Rs. in lakhs
	Paid up Equity Capital		200
	Free Reserves		600
(i)		A	800
	Investments		
	In shares of subsidiaries		250
	In debentures of group companies		400
(ii)		B	650
(iii)	10% of A		80
(iv)	Excess of Investment over 10% of A (650 – 80)	C	570
(v)	Net Owned Fund [(A) - (C)] (800 – 570)		230

Question 22 : Nov – 2022 – Paper

DS Finance Limited is a non-banking financial company. It provides you with the following information regarding its outstanding amount, Rs.100 lakhs of which instalments are overdue on:

- 400 accounts for last one month (amount overdue Rs.20 lakhs),
- 24 accounts for two months (amount overdue Rs.12 lakhs),
- 10 accounts for more than 30 months (amount overdue Rs.10 lakhs)
- 4 accounts for more than 3 years (amounts overdue Rs.10 lakhs - already identified as sub-standard assets)
- 1 account of Rs.5 lakhs which has been identified as non-recoverable by management.

- Out of 10 accounts overdue for more than 30 months, 6 accounts are already identified as sub-standard (amount Rs.3 lakhs) for more than 12 months and others are identified as sub-standard assets for a period of less than twelve months.

Classify the assets of the company in line with Non-Banking Financial Company- Systemically Important Non-Deposit taking Company and Deposit taking Company (Reserve Bank) Directions, 2016.

Thanks ....

CHAPTER 22

CONSOLIDATION FINANCIAL STATEMENTS

Question 1 : May – 2018 – Paper / Nov – 2019 - RTP

The following summarised Balance Sheets of H Ltd. and its subsidiary S Ltd. were prepared as on 31st March, 2019:

	H Ltd. (Rs.)	S Ltd. (Rs.)
Equity and Liabilities		
Shareholders' Funds		
Equity Share Capital (fully paid up shares of Rs.10 each)	12,00,000	2,00,000
Reserves and Surplus		
General Reserve	4,35,000	1,55,000
Profit and Loss Account	2,80,000	65,000
Current Liabilities		
Trade Payables	3,25,000	1,25,000
Total	**22,40,000**	**5,45,000**
	H Ltd. (Rs.)	**S Ltd. (Rs.)**
Assets		
Non-Current Assets		
Property, Plant and Equipment		
Machinery	6,40,000	1,80,000
Furniture	3,75,000	34,000
Non-Current Investments		
Shares in S Ltd. - 16,000 shares @ Rs.20 each	3,20,000	-
Current Assets		
Inventories	2,68,000	62,000
Trade Receivables	4,73,000	2,37,000
Cash and Bank	1,64,000	32,000
Total	**22,40,000**	**5,45,000**

H Ltd. acquired the 80% shares of S Ltd. on 1st April, 2018. On the date of acquisition, General Reserve and Profit Loss Account of S Ltd. stood at Rs. 50,000 and Rs. 30,000 respectively.

Machinery (book value Rs. 2,00,000) and Furniture (book value Rs. 40,000) of S Ltd. were revalued at Rs. 3,00,000 and Rs. 30,000 respectively on 1st April,2018 for the purpose of fixing the price of its shares (rates of depreciation computed on the basis of useful lives: Machinery 10% and Furniture 15%). Trade Payables of H Ltd. include Rs. 40,000 due to S Ltd. for goods supplied since the acquisition of the shares. These goods are charged at

10% above cost. The inventories of H Ltd. includes goods costing Rs. 55,000 (cost to H Ltd.) purchased from S Ltd.

You are required to prepare the Consolidated Balance Sheet of H Ltd. with its subsidiary S Ltd. as at 31st March, 2019.

Solution :

Consolidated Balance Sheet of H Ltd. and its Subsidiary S Ltd.
as at 31st March, 2019

	Particulars	Notes	Rs.
I.	**Equity and Liabilities**		
	(1) Shareholder's Funds		
	(a) Share Capital		12,00,000
	(1,20,000 equity shares of Rs. 10 each)		
	(b) Reserves and Surplus	1	8,16,200
	(2) Minority Interest (W.N.4)		99,300
	(3) Current Liabilities		
	(a) Trade Payables	2	4,10,000
	Total		**25,25,500**
II.	**Assets**		
	(1) Non-current assets		
	(a) Property, Plant and Equipment		
	(i) Tangible assets	3	13,10,500
	(ii) Intangible assets	4	24,000
	(b) Current assets		
	(i) Inventories	5	3,25,000
	(ii) Trade Receivables	6	6,70,000
	(iii) Cash at Bank	7	1,96,000
	Total		**25,25,500**

Notes to Accounts :

				Rs.
1	Reserves and Surplus			
	General Reserves		4,35,000	
	Add: 80% share of S Ltd.'s post- acquisition reserves (W.N.3)		84,000	5,19,000
	Profit and Loss Account		2,80,000	
	Add: 80% share of S Ltd.'s post- acquisition profits (W.N.3)	21,200		
	Less: Unrealised gain	(4,000)	17,200	2,97,200
				8,16,200
2	Trade Payables			

	H Ltd.		3,25,000	
	S Ltd.		1,25,000	
	Less: Mutual transaction		(40,000)	4,10,000
3	Tangible Assets			
	Machinery			
	H Ltd.		6,40,000	
	S Ltd.	2,00,000		
	Add: Appreciation	1,00,000		
		3,00,000		
	Less: Depreciation	(30,000)	2,70,000	9,10,000
	Furniture			
	H. Ltd.		3,75,000	
	S Ltd.	40,000		
	Less: Decrease in value	(10,000)		
		30,000		
	Less: Depreciation	(4,500)	25,500	4,00,500
				13,10,500
4	Intangible assets			
	Goodwill [WN 5]			24,000
5	Inventories			
	H Ltd.		2,68,000	
	S Ltd.		62,000	3,30,000
	Less: Inventory reserve			(5,000)
				3,25,000
6	Trade Receivables			
	H Ltd.		4,73,000	
	S Ltd.		2,37,000	
				7,10,000
	Less: Mutual transaction			(40,000)
				6,70,000
7	Cash and Bank			
	H Ltd.		1,64,000	
	S Ltd.		32,000	1,96,000

Working Notes:

1. Profit or loss on revaluation of assets in the books of S Ltd. and their book values as on 1.4.2018

	Rs.
Machinery	
Revaluation as on 1.4.2018	3,00,000
Less: Book value as on 1.4.2018	(2,00,000)
Profit on revaluation	1,00,000

Furniture	
Revaluation as on 1.4.2018	30,000
Less: Book value as on 1.4.2018	(40,000)
Loss on revaluation	(10,000)

2. Calculation of short/excess depreciation

	Machinery	Furniture
Upward/ (Downward) Revaluation (W.N. 4)	1,00,000	(10,000)
Rate of depreciation	10% p.a.	15% p.a.
Difference [(short)/excess]	(10,000)	1,500

3. Analysis of reserves and profits of S Ltd. as on 31.03.2019

	Pre-acquisition profit upto 1.4.2018	Post-acquisition profits (1.4.2018 – 31.3.2019)	
	(Capital profits)	General Reserve	Profit and loss account
General reserve as on 31.3.2019	50,000	1,05,000	
Profit and loss account as on 31.3.2019	30,000		35,000
Upward Revaluation of machinery as on 1.4.2018	1,00,000		
Downward Revaluation of Furniture as on 1.4.2018	(10,000)		
Short depreciation on machinery (W.N. 5)			(10,000)
Excess depreciation on furniture (W.N. 5)			1,500
Total	1,70,000	1,05,000	26,500

4. Minority Interest

	Rs.
Paid-up value of (2,00,000 x 20%)	40,000
Add: 20% share of pre-acquisition profits and reserves [(20% of (50,000 + 30,000)]	16,000
20% share of profit on revaluation	18,000
20% share of post-acquisition reserves	21,000
20% share of post-acquisition profit	5,300
	1,00,300
Less: Unrealised Profit on Inventory (55,000 x 10/110) x 20%	(1,000)
	99,300

5. Cost of Control or Goodwill

	Rs.	Rs.
Cost of Investment		3,20,000
Less: Paid-up value of 80% shares	1,60,000	
80% share of pre-acquisition profits and reserves		
(Rs.64,000 + Rs.72,000)	1,36,000	(2,96,000)
Cost of control or Goodwill		24,000

Question 2 : Nov – 2018 – Paper

The Profit and Loss Accounts of A Ltd. and its subsidiary B Ltd. for the year ended 31st March, 2018 are given below :

Rs. in Lakhs

	A Ltd.	B Ltd.
Sales and other income	7,500	1,500
Increase in Inventory	1,500	300
Total	9,000	1,800
Expenses		
Raw material consumed	1,200	300
Wages and Salaries	1,200	225
Production expenses	300	150
Administrative expenses	300	150
Selling and distribution expenses	300	75
Interest	150	75
Depreciation	150	75
Total	3,600	1,050
Profit before tax	5,400	750
Provision for tax	1,800	300
Profit after tax	3,600	450
Dividend paid	1,800	225
Balance of Profit	1,800	225

The following information is also given:

(i) A Ltd sold goods of Rs.180 Lakhs to B Ltd at cost plus 25%. (1/6 of such goods were still in inventory of B Ltd at the end of the year)

(ii) Administrative expenses of B Ltd include Rs.8 Lakhs paid to A Ltd as consultancy fees.

(iii) Selling and distribution expenses of A Ltd include Rs.15 Lakhs paid to B Ltd as commission.

(iv) A Ltd holds 72% of the Equity Capital of B Ltd. The Equity Capital of B Ltd prior to 2016-17 is Rs.1,500 Lakhs

Prepare a consolidated Profit and Loss Account for the year ended 31st March, 2018.

Solution :

Consolidated Profit & Loss Account of A Ltd. and its subsidiary B Ltd.
for the year ended on 31st March, 2018

	Particulars	Note No.	Rs. in Lacs
I.	Revenue from operations	1	8,797
II.	Total revenue		8,797
III.	Expenses		
	Cost of Material purchased/Consumed	3	1,770
	Changes of Inventories of finished goods	2	(1,794)
	Employee benefit expense	4	1,425
	Finance cost	6	225
	Depreciation and amortization expense	7	225
	Other expenses	5	802
	Total expenses		2,653
IV.	Profit before Tax(II-III)		6,144
V.	Tax Expenses	8	2,100
VI.	Profit After Tax		4,044

Notes to Accounts

		Rs. in Lacs	Rs. in Lacs
1	Revenue from Operations		
	Sales and other income		
	A Ltd.	7,500	
	B Ltd.	1,500	
		9,000	
	Less: Inter-company Sales	(180)	
	Consultancy fees received by A Ltd. from B Ltd.	(8)	
	Commission received by B Ltd. from A Ltd.	(15)	8,797
2	Increase in Inventory		
	A Ltd.	1,500	
	B Ltd.	300	
		1,800	
	Less: Unrealised profits Rs. 180 × 1/6 x 25/125	(6)	1,794
3	Cost of Material purchased/consumed		
	A Ltd.	1,200	
	BLtd.	300	
		1,500	
	Less: Purchases by B Ltd. from A Ltd.	(180)	1,320
	Direct Expenses		
	A Ltd.	300	
	BLtd.	150	450

			1,770
4	Employee benefits and expenses		
	Wages and Salaries:		
	A Ltd.	1,200	
	B Ltd.	225	1,425
5	Other Expenses		
	Administrative Expenses		
	A Ltd.	300	
	B Ltd.	150	
		450	
	Less: Consultancy fees received by A Ltd. from BLtd.	(8)	442
	Selling and Distribution Expenses:		
	A Ltd.	300	
	B Ltd.	75	
		375	
	Less: Commission received from B Ltd. from A Ltd.	(15)	360
			802
6	Finance Cost		
	Interest:		
	A Ltd.	150	
	B Ltd.	75	225
7	Depreciation and Amortisation		
	Depreciation:		
	A Ltd.	150	
	B Ltd.	75	225
8	Provision for tax		
	A Ltd.	1800	
	B Ltd.	300	2100

Note : it is assumed that dividend adjustment has not be done in sales & other income of A Ltd i.e. dividend received from B Ltd is not included in other income of A Ltd. Alternative answer is possible considering is otherwise.

Question 3 : May – 2019 – RTP

The following data is provided to you:

Case	Subsidiary Company	% shares owned	Cost	Date of acquisition		Consolidation Date	
				1.1.2018		31.12.2018	
				Share Capital	Profit & Loss Account	Share Capital	Profit & Loss Account
			Rs.	Rs.	Rs.	Rs.	Rs.
Case 1	A	90%	1,40,000	1,00,000	50,000	1,00,000	70,000

Case 2	B	85%	1,04,000	1,00,000	30,000	1,00,000	20,000
Case 3	C	80%	56,000	50,000	20,000	50,000	20,000
Case 4	D	100%	1,00,000	50,000	40,000	50,000	55,000

Determine in each case:

(1) Minority interest at the date of acquisition and at the date of consolidation.

(2) Goodwill or Capital Reserve.

Solution :

(1) **Minority Interest** = Equity attributable to minorities

Equity is the residual interest in the assets of an enterprise after deducting all its liabilities i.e. in this case it should be equal to Share Capital + Profit & Loss A/c.

	Minority % Shares Owned [E]	Minority interest as at the date of acquisition [E] x [A + B] Rs.	Minority interest as at the date of consolidation [E] X [C + D] Rs.
Case 1 [100-90]	10%	15,000	17,000
Case 2 [100-85]	15%	19,500	18,000
Case 3 [100-80]	20%	14,000	14,000
Case 4 [100-100]	NIL	Nil	Nil

A = Share capital on 1.1.2018

B = Profit & loss account balance on 1.1.2018

C = Share capital on 31.12.2018

D = Profit & loss account balance on 1.1.2018

(2) **Calculation of Goodwill or Capital Reserve**

	Shareholding % [F]	Cost [G]	Total Equity [A] + [B] = [H]	Parent's Portion of equity [F] x [H]	Goodwill Rs. [G] – [H]	Capital Reserve Rs. [H] – [G]
Case 1	90%	1,40,000	1,50,000	1,35,000	5,000	—
Case 2	85%	1,04,000	1,30,000	1,10,500	—	6,500
Case 3	80%	56,000	70,000	56,000	Nil	Nil
Case 4	100%	1,00,000	90,000	90,000	10,000	—

Question 4 : May – 2019 – Paper

H Ltd. acquire 70% of equity share of S Ltd. as on 1st January, 2011 at a cost of Rs.5,00,000 when S Ltd. had an equity share capital of Rs.5,00,000 and reserves and surplus of Rs.40,000.

Both the companies follow calendar year as the accounting year.

In the four consecutive years, S Ltd. performed badly and suffered losses of Rs.1,25,000, Rs.2,00,000, Rs.2,50,000 and Rs.60,000 respectively.
Thereafter in 2015, S Ltd. experienced turnaround and registered an annual profit of Rs.25,000. In the next two years i.e. 2016 and 2017, S Ltd. recorded annual profits of Rs.50,000 and Rs.75,000 respectively.
Show the Minority Interests and Cost of Control at the end of each year for the purpose of consolidation

Solution :

The losses applicable to the minority in a consolidated subsidiary may exceed the minority interest in the equity of the subsidiary. The excess, and any further losses applicable to the minority, are adjusted against the majority interest except to the extent that the minority has a binding obligation to, and is able to, make good the losses. If the subsidiary subsequently reports profits, all such profits are allocated to the majority interest until the minority's share of losses previously absorbed by the majority has been recovered.
Accordingly,

Year	Profit / (Loss)	Minority Interest (30%)	Additional Consolidated P & L (Dr.) or Cr.	Minority's Share of losses borne by H Ltd.		Cost of Control
				Rs.	Balance	
At the time of acquisition on 1.1.2011		1,62,000 (W.N.)				
2011	(1,25,000)	(37,500)	(87,500)			1,22,000 (W.N.)
Balance		1,24,500				
2012	(2,00,000)	(60,000)	(1,40,000)			1,22,000
Balance		64,500				
2013	(2,50,000)	(75,000)	(1,75,000)			1,22,000
		(10,500)				
	Loss of minority borne by Holding Co.	10,500	(10,500)	10,500	10,500	
Balance		Nil	(1,85,500)			
2014	(60,000)	(18,000)	(42,000)			1,22,000
	Loss of minority borne by Holding Co.	18,000	(18,000)	18,000	28,500	
Balance		Nil	(60,000)			
2015	25,000	7,500	17,500			1,22,000

	Profit share of minority adjusted against losses of minority absorbed by Holding Co.	(7,500)	7,500	(7,500)	21,000	
Balance		Nil	25,000			
2016	50,000	15,000	35,000	(15,000)	6,000	1,22,000
		(15,000)	15,000			
Balance		Nil	50,000			
2017	75,000	22,500	52,500	-6,000	Nil	1,22,000
		(6,000)	6,000			
Balance		16,500	58,500			

Working Note:

Calculation of Minority interest and Cost of control on 1.1.2011

		Share of Holding Co.	Minority Interest
	100%	70%	30%
	Rs.	Rs.	Rs.
Share Capital	5,00,000	3,50,000	1,50,000
Reserve	40,000	28,000	12,000
		3,78,000	1,62,000
Less: Cost of investment		(5,00,000)	
Goodwill		1,22,000	

Question 5 : Nov – 2019 – Paper

Consider the following summarized Balance Sheets of subsidiary MNT Ltd.

Liabilities	2017-18 Amount in Rs.	2018-19 Amount in Rs.
Share Capital		
Issued and subscribed 7500 Equity Shares of Rs.100	7,50,000	7,50,000
Reserve and Surplus		
Revenue Reserve	2,14,000	5,05,000
Securities Premium	72,000	2,07,000
Current Liabilities and Provisions		
Trade Payables	2,90,000	2,46,000
Bank Overdraft	-	1,70,000
Provision for Taxation	2,62,000	4,30,000
	15,88,000	23,08,000
Assets		
Fixed Assets (Cost)	9,20,000	9,20,000

Less: Accumulated Depreciation	(1,70,000)	2,82,500)
	7,50,000	6,37,500
Investment at Cost	-	5,30,000
Current Assets		
Inventory	4,12,300	6,90,000
Trade Receivable	2,95,000	3,43,000
Prepaid expenses	78,000	65,000
Cash at Bank	52,700	42,500
	15,88,000	23,08,000

Other Information:

(1) MNT Ltd. is a subsidiary of LTC Ltd.

(2) LTC Ltd. values inventory on FIFO basis, while MNT Ltd. used LIFO basis. To bring MNT Ltd.'s inventories values in line with those of LTC Ltd., its value of inventory is required to be reduced by Rs.5,000 at the end of 2017-2018 and increased by Rs.12,000 at the end of 2018-2019. (Inventory of 2017-18 has been sold out during the year 2018-19)

(3) MNT Ltd. deducts 2% from Trade Receivables as a general provision against doubtful debts.

(4) Prepaid expenses in MNT Ltd. include Sales Promotion expenditure carried forward of Rs. 25 ,000 in 2017-18 and Rs. 12,500 in 2018-19 being part of initial Sales Promotion expenditure of Rs. 37,500 in 2017-18, which is being written off over three years. Similar nature of Sales Promotion expenditure of LTC Ltd. has been fully written off in 2017-18.

Restate the balance sheet of MNT Ltd. as on 31st March, 2019 after considering the above information for the purpose of consolidation. Such restatement is necessary to make the accounting policies adopted by LTC Ltd. and MNT Ltd. uniform.

Solution :

Restated Balance Sheet of MNT Ltd.
as at 31st December, 2019

		Particulars	Notes	Rs.
I.		**Equity and Liabilities**		
1		**Shareholder's Funds**		
	a	Share Capital		7,50,000
	b	Reserves and Surplus	1	7,18,500
2		**Current Liabilities**		
	a	Short term borrowings	2	1,70,000
	b	Trade Payables		2,46,000
		Short-term provision	3	4,30,000
		Total		**23,14,500**
II.		**Assets**		
1		Non-current assets		
	a	Property, Plant & Equipment	4	6,37,500

	b	Non-current Investment		5,30,000
2		**Current assets**		
	a	Inventories (6,90,000 +12,000)	5	7,02,000
	b	Trade Receivables $\left(\frac{3{,}43{,}00}{98}\times 100\right)$		3,50,000
	c	Cash & Cash Equivalents		42,500
	d	Other current assets	6	52,500
		Total		**23,14,500**

Notes to Accounts

			Rs.
1	**Reserves and Surplus**		
	Revenue Reserve (refer W.N.)	5,11,500	
	Securities Premium	2,07,000	7,18,500
2	**Short term borrowings**		
	Bank overdraft		1,70,000
3	**Short-term provision**		
	Provision for taxation		4,30,000
4	**Property, Plant and Equipment**		
	Cost	9,20,000	
	Less: Depreciation to date	(2,82,500)	6,37,500
5	**Inventories**	6,90,000	
	Increase in value as per FIFO	12,000	7,02,000
6	**Other current assets**		
	Prepaid expenses (After adjusting sales promotion expenses to be written off each year) (65,000 - 12,500)		52,500

Working Note:

Adjusted revenue reserves of MNT Ltd.:

	Rs.	Rs.
Revenue reserves as given		5,05,000
Add: Provision for doubtful debts [3,43,000 X 2/98]	7,000	
Add: Increase in value of inventory	12,000	19,000
		5,24,000
Less: Sales Promotion expenditure to be written off		(12,500)
Adjusted revenue reserve		5,11,500

Question 6 : Nov – 2019 – Paper / Nov – 2020 – RTP

From the following data, determine Minority Interest on the date of acquisition and on the date of consolidation in each case:

Case	Subsidiary Company	% of Share Owned	Cost	Date of Acquisition		Consolidation date	
				1/1/2019		31-12-2019	
				Share Capital	Profit and Loss A/c	Share Capital	Profit and Loss A/c
				Rs.	Rs.	Rs.	Rs.
Case-A	X	90%	2,00,000	1,50,000	75,000	1,50,000	85,000
Case-B	Y	75%	1,75,000	1,40,000	60,000	1,40,000	20,000
Case-C	Z	70%	98,000	40,000	20,000	40,000	20,000
Case-D	M	95%	75,000	60,000	35,000	60,000	55,000
Case-E	N	100%	1,00,000	40,000	40,000	40,000	65,000

Solution :

Minority Interest = Equity attributable to minorities

Equity is the residual interest in the assets of an enterprise after deducting all its liabilities i.e. in this case, it should be equal to Share Capital + Profit & Loss A/c

A = Share capital on 1.1.2019

B = Profit & loss account balance on 1.1.2019

C = Share capital on 31.12.2019

D = Profit & loss account balance on 31.12.2019

	Minority % Shares Owned [E]	Minority interest as at the date of acquisition [E] x [A + B] Rs.	Minority interest as at the date of consolidation [E] X [C + D] Rs.
Case A [100-90]	10%	22,500	23,500
Case B [100-75]	25%	50,000	40,000
Case C [100-70]	30%	18,000	18,000
Case D [100-95]	5%	4,750	5,750
Case E [100-100]	NIL	NIL	NIL

Question 7 : May – 2020 – RTP

From the following summarized balance sheets of Kedar Ltd. and its subsidiary Vijay Ltd. drawn up at 31st March, 2019, prepare a consolidated balance sheet as at that date, having regard to the following:

(i) Reserves and Profit and Loss Account of Vijay Ltd. stood at Rs. 62,500 and Rs. 37,500 respectively on the date of acquisition of its 80% shares by Kedar Ltd. on 1st April, 2018.

(ii) Machinery (Book-value Rs. 2,50,000) and Furniture (Book value Rs. 50,000) of Vijay Ltd. were revalued at Rs. 3,75,000 and Rs. 37,500 respectively on 1st April, 2018 for the

purpose of fixing the price of its shares. [Rates of depreciation computed on the basis of useful lives: Machinery 10%, Furniture 15%.]

Summarised Balance Sheet of Kedar Ltd. and Vijay Ltd. as on 31st March, 2019

Liabilities	Kedar Ltd. Rs.	Vijay Ltd. Rs.	Assets	Kedar Ltd. Rs.	Vijay Ltd. Rs.
Equity and Liabilities			Non-current assets		
Shareholders' funds			Fixed assets		
Share Capital			Machinery	7,50,000	2,25,000
Shares of Rs.100 each	15,00,000	2,50,000	Furniture	3,75,000	42,500
Reserves	5,00,000	1,87,500	Other non-current assets	11,00,000	3,75,000
Profit and Loss Account	2,50,000	62,500	Non-current Investments		
Trade Payables	3,75,000	1,42,500	Shares in Vijay Ltd.:		
			2,000 shares at Rs.200 each	4,00,000	-
	26,25,000	**6,42,500**		**26,25,000**	**6,42,500**

Solution :

Consolidated Balance Sheet of Kedar Ltd. and its Subsidiary Vijay Ltd.
as at 31st March, 2019

		Particulars	Notes	Rs.
I.		**Equity and Liabilities**		
1		**Shareholder's Funds**		
	a	Share Capital		15,00,000
	b	Reserves and Surplus	1	8,61,500
2		**Minority Interest** (W.N.5)		1,20,375
3		**Current Liabilities**		
	a	Trade Payables	2	5,17,500
		Total		**29,99,375**
		Assets		
1		**Non-current assets**		
	a	(i) Property, Plant & Equipment	3	14,94,375
		(ii) Intangible assets	4	30,000
	b	Other non- current assets	5	14,75,000
		Total		**29,99,375**

Notes to Accounts

				Rs.
1	**Reserves and Surplus**			
	Reserves		5,00,000	
	Add: 4/5th share of Vijay Ltd.'s post-acquisition reserves (W.N.3)		1,00,000	6,00,000
	Profit and Loss Account		2,50,000	
	Add: 4/5th share of Vijay Ltd.'s post-acquisition profits (W.N.4)		11,500	2,61,500
				8,61,500
2	**Trade Payables**			
	Kedar Ltd.		3,75,000	
	Vijay Ltd.		1,42,500	5,17,500
3	**Property, Plant & Equipment**			
	Machinery			
	Kedar Ltd.		7,50,000	
	Vijay Ltd.	2,50,000		
	Add: Appreciation	1,25,000		
		3,75,000		
	Less: Depreciation	(37,500	3,37,500	
	Furniture	-		
	Kedar Ltd.	-	3,75,000	
	Vijay Ltd.	50,000		
	Less: Decrease in value	(12,500)		
		37,500		
	Less: Depreciation	(5,625)	31,875	14,94,375
4	**Intangible assets**			
	Goodwill [WN 6]			30,000
5	**Other non-current assets**			
	Kedar Ltd.		11,00,000	
	Vijay Ltd.		3,75,000	14,75,000

Working Notes :

		Rs.
1	**Pre-acquisition profits and reserves of Vijay Ltd.**	
	Reserves	62,500
	Profit and Loss Account	37,500
		1,00,000
	Kedar Ltd.'s = 4/5 × 1,00,000	80,000
	Minority Interest = 1/5 × 1,00,000	20,000
2	**Profit on revaluation of assets of Vijay Ltd.**	-
	Profit on Machinery Rs. (3,75,000 – 2,50,000)	1,25,000
	Less: Loss on Furniture Rs. (50,000 – 37,500)	12,500

	Net Profit on revaluation	1,12,500
	Kedar Ltd.'s share 4/5 × 1,12,500	90,000
	Minority Interest 1/5 × 1,12,500	22,500
3	**Post-acquisition reserves of Vijay Ltd.**	-
	Post-acquisition reserves (Total reserves less pre-acquisition reserves = Rs. 1,87,500 – 62,500)	1,25,000
	Kedar Ltd.'s share 4/5 × 1,25,000	1,00,000
	Minority interest 1/5 × 25,000	25,000
4	**Post -acquisition profits of Vijay Ltd.**	
	Post-acquisition profits (Profit & loss account balance less pre-acquisition profits = Rs. 62,500 – 37,500)	25,000
	Add: Excess depreciation charged on furniture @ 15% on Rs. 12,500 i.e. (50,000 – 37,500)	1,875
		26,875
	Less: Under depreciation on machinery @ 10% on Rs. 1,25,000 i.e. (3,75,000 – 2,50,000)	-12,500
	Adjusted post-acquisition profits	14,375
	Kedar Ltd.'s share 4/5 × 14,375	11,500
	Minority Interest 1/5 × 14,375	2,875
5	**Minority Interest**	-
	Paid-up value of (2,500 – 2,000) = 500 shares held by outsiders i.e. 500 × Rs. 100	50,000
	Add: 1/5th share of pre-acquisition profits and reserves	20,000
	1/5th share of profit on revaluation	22,500
	1/5th share of post-acquisition reserves	25,000
	1/5th share of post-acquisition profit	2,875
		1,20,375
6	**Cost of Control or Goodwill**	
	Paid-up value of 2,000 shares held by Kedar Ltd. i.e. 2,000 × Rs. 100	2,00,000
	Add: 4/5th share of pre-acquisition profits and reserves	80,000
	4/5th share of profit on the revaluation	90,000
	Intrinsic value of shares on the date of acquisition	3,70,000
	Price paid by Kedar Ltd. for 2,000 shares	4,00,000
	Less: Intrinsic value of the shares	(3,70,000)
	Cost of control or Goodwill	30,000

Question 8 : Nov – 2020 – RTP

A Ltd holds 75% of the equity capital and voting power in B Ltd. A Ltd purchases inventories costing Rs. 150 lacs from B Ltd at a price of Rs. 200 lacs. The entire inventories remain unsold with A Ltd at the financial year end i.e. 31 March 2019. Suggest the accounting treatment for this

transaction in the consolidated financial statements of A Ltd giving reference of the relevant accounting standard.

Solution :

As per para provisions of AS 21, Intragroup balances and intragroup transactions and resulting unrealized profits should be eliminated in full. Unrealized losses resulting from intragroup transactions should also be eliminated unless cost cannot be recovered.

Intragroup balances and intragroup transactions, including sales, expenses and dividends, are eliminated in full. Unrealised profits resulting from intragroup transactions that are included in the carrying amount of assets, such as inventory and fixed assets, are eliminated in full. Unrealised losses resulting from intragroup transactions that are deducted in arriving at the carrying amount of assets are also eliminated unless cost cannot be recovered. One also needs to see whether the intragroup transaction is "upstream" or "down-stream". Upstream transaction is a transaction in which the subsidiary company sells goods to holding company. While in the downstream transaction, holding company is the seller and subsidiary company is the buyer.

In the case of upstream transaction, since the goods are sold by the subsidiary to holding company; profit is made by the subsidiary company, which is ultimately shared by the holding company and the minority shareholders. In such a transaction, if some goods remain unsold at the balance sheet date, the unrealized profit on such goods should be eliminated from minority interest as well as from consolidated profit on the basis of their share-holding besides deducting the same from unsold inventory.

But in the case of downstream transaction, the whole profit is earned by the holding company, therefore, whole unrealized profit should be adjusted from unsold inventory and consolidated profit and loss account only irrespective of the percentage of the shares held by the parent.

The case given in the question is the case of upstream transaction. In the consolidated profit and loss account for the year ended 31 March 2019, entire transaction of sale and purchase of Rs. 200 lacs each, would be eliminated by reducing both sales and purchases (cost of sales). Further, the unrealized profits of Rs. 50 lacs (i.e. Rs. 200 lacs – Rs. 150 lacs), would be eliminated in the consolidated financial statements for financial year ended 31 March 2019, by reducing the value of closing inventories by Rs. 50 lacs as of 31 March 2019. In the consolidated balance sheet as of 31 March 2019, A Ltd's share of profit from B Ltd will be reduced by Rs. 37.50 lacs (being 75% of Rs. 50 lacs) and the minority's share of the profits of B Ltd would be reduced by Rs. 12.50 lacs (being 25% of Rs. 50 lacs).

Question 9 : Nov – 2020 – Paper

H Ltd acquires 64000 Equity Shares of Rs. 10 each in S Ltd as on 1st October 2019. The Balance Sheets of the two companies as on 31st March 2020 were as under

Particulars	H Ltd (Rs.)	S Ltd (Rs.)
Equities and liabilities		
Equity Share Capital of Rs. 10 each	20,00,000	8,00,000
General Reserve (1st April 2019)	9,60,000	4,20,000
Profit and loss accounts	2,28,000	3,28,000

Preliminary Expenses (1st April 2019)	-	-20,000
Bank Overdraft	3,00,000	-
Bills Payable	-	52,000
Trade Payable	1,66,400	80,000
Total	**36,55,200**	**16,60,000**
Assets		
Land and building	7,20,000	7,60,000
Plant & Machinery	9,60,000	5,40,000
Investments in equity shares of S Ltd	12,27,200	-
Inventories	4,56,000	1,68,000
Trade Receivables	1,76,000	1,60,000
Bills Receivables	59,200	-
Cash in hand	56,800	32,000
Total	**36,55,200**	**16,60,000**

Additional Information :

1. The Profit & Loss Accounts of S Ltd showed a balance of Rs. 1,20,000 on 1st April 2019. S. Ltd paid a dividend of 10% out of the same on 1st November 2019 for the year 2018-19. The dividend was correctly accounted for by H Ltd
2. The Plant & Machinery of S Ltd which stood at Rs. 6,00,000 on 1st April 2019 was considered worth Rs. 5,20,000 on the date of acquisition by H Ltd. S Ltd charges depreciation @ 10% per annum on Plant & Machiney

Prepare consolidated Balance Sheet of H Ltd and its subsidiary S Ltd as on 31st March 2020 as per scheduled III of the companies Act, 2013.

Solution :

Consolidated Balance Sheet of H Ltd. and its subsidiary, S Ltd.
as at 31st March, 2020

Particulars	Note No.	Rs.
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	20,00,000
(b) Reserves and Surplus	2	13,07,200
(2) Minority Interest (W.N 4)		2,96,400
(3) Current Liabilities		
(a) Trade Payables	3	2,98,400
(b) Short term borrowings		3,00,000
Total		**42,02,000**
II. Assets		
(1) Non-current assets		
(i) Property, Plant and Equipment	4	29,34,000
(ii) Intangible assets (W.N.5)		1,60,000
(2) Current assets		

(a) Inventories	5	6,24,000
(b) Trade receivables	6	3,95,200
(c) Cash & Cash equivalents (Cash)	7	88,800
Total		**42,02,000**

Note to Accounts

			Rs.	**Rs.**
1	Share Capital			
	2,00,000 equity shares of Rs.10 each			20,00,000
2	Reserves and Surplus			
	Reserves		9,60,000	
	Profit & loss			
	H Ltd.	2,28,800		
	S Ltd. (As per W.N. 3)	1,18,400	3,47,200	13,07,200
3	Trade Payables			
	H Ltd.		1,66,400	
	S Ltd. (80,000 + 52,000)		1,32,000	2,98,400
4	Property, Plant and Equipment			
	Land and building			
	H Ltd.	7,20,000		
	S Ltd.	7,60,000	14,80,000	
	Plant & Machinery			
	H Ltd.	9,60,000		
	S Ltd. (As per W.N. 7)	4,94,000	14,54,000	29,34,000
5	Inventories			
	H Ltd.		4,56,000	
	S Ltd.		1,68,000	6,24,000
6	Trade Receivables			
	H Ltd.	1,76,000		
	S Ltd.	1,60,000	3,36,000	
	Bills receivable: H Ltd.		59,200	3,95,200
7	Cash & Cash equivalents			
	Cash			
	H Ltd.		56,800	
	S Ltd.		32,000	88,800

Working Notes:

1. Share holding pattern

Total Shares of S Ltd 80,000 shares

Shares held by H Ltd 64,000 shares i.e. 80 %;

Minority Shareholding 16,000 shares i.e. 20 %

2. Capital profits of S Ltd.

	Rs.	Rs.
Reserve on 1st October, 2019 (Assumed there is no movement in reserves during the year and hence balance as on 1st October, 2019 is same as of 31st March 2020)		4,20,000
Profit & Loss Account Balance on 1st April, 2019	1,20,000	
Less: Dividend paid	(80,000)	40,000
Profit for year:		
Total Rs. 3,28,000		
Less: Rs. 40,000 (opening balance)		
Rs. 2,88,000		
Proportionate up to 1st October, 2019 on time basis (Rs. 2,88,000/2)		1,44,000
Reduction in value of Plant & Machinery (WN 6)		(50,000)
		5,54,000
Less: Preliminary expenses written off		(20,000)
Total Capital Profit		5,34,000
Holding company's share (5,34,000 × 80%)		4,27,200
Minority Interest (5,34,000 × 20%)		1,06,800

Note: Preliminary expenses as on 1st April, 2019 amounting Rs. 20,000 have been written off.

3. Revenue profits of S Ltd.

Profit after 1st October, 2019 (3,28,000 - 40,000)/2		1,44,000
Less 10% depreciation on Rs.5,20,000 for 6 months	(26,000)	
Add: Depreciation already charged for 2nd half year on 6,00,000	30,000	4,000
		1,48,000
Holding company's share (1,48,000 X 80%)		1,18,400
Minority Interest (1,48,000 X 20%)		29,600

4. Minority interest

Par value of 16,000 shares (8,00,000 X 20%)	1,60,000
Add: 1/5 Capital Profits [WN 2]	1,06,800
1/5 Revenue Profits [WN 3]	29,600
	2,96,400

5. Cost of Control

Amount paid for 64,000 shares		12,27,200
Less:		
Par value of shares (8,00,000 × 80%)	6,40,000	

Capital Profits – share of H Ltd. [WN 2]	4,27,200	(10,67,200)
Cost of Control or Goodwill		1,60,000

6. Calculation of revaluation loss on Plant and Machinery of S Ltd. on 1st October, 2019

	Rs.
Value of plant and machinery as on 1st April,2019	6,00,000
Less: Depreciation for the six months	(30,000)
Value of plant and machinery as on 1st October, 2019	5,70,000
Less: Plant and machinery valued by H Ltd. on 1st October,2019	(5,20,000)
Revaluation Loss	50,000

7. Value of plant & Machinery of S Ltd. On 31st March,2020

Value of machinery on 1st October, 2019	5,20,000
Less: depreciation for next six month	(26,000)
	4,94,000

Question 10 : Jan – 2021 – Paper

On 31st march, 2020 the summarised Balance Sheets of H Ltd. and its subsidiary S Ltd. stood as follows :

	H Ltd. Rs.	S Ltd. Rs.
Shareholder's Fund		
Issued and subscribed		
Equity shares of Rs.10 each	13,40,000	2,40,000
Reserves and Surplus	4,80,000	1,80,000
Profit & Loss Account	2,40,000	60,000
Secured Loans		
12% Debentures	1,00,000	–
Current Liabilities		
Trade Payables	2,00,000	1,22,000
Bank Overdraft	1,00,000	–
Bills Payable	60,000	14,800
Total	**25,20,000**	**6,16,800**
Assets		
Non-Currents Assets		
(a) Property, Plant and Equipment		
Machinery	7,20,000	2,16,000
Furniture	3,60,000	40,800
(b) Investments		
Investments in S Ltd.	3,84,000	–
(19,200 shares at Rs.20 each)		

Current Assets		
Inventories	6,00,000	2,00,000
Trade Receivables	3,00,000	90,000
Bills Receivables	1,00,000	30,000
Cash at Bank	56,000	40,000
Total	**25,20,000**	**6,16,800**

The following information is also provided to you :

(a) H Ltd. purchased 19,200 shares of S Ltd. on 1st April, 2019, when the balances of Reserves & Surplus and Profit & Loss Account of S Ltd. stood at Rs.60,000 and Rs.36,000 respectively.

(b) Machinery (Book value Rs.2,40,000) and Furniture (Book value Rs.48,000) of S Ltd. were revalued at Rs.3,60,000 and Rs.36,000 respectively on 1st April, 2019, for the purpose of fixing the price of its shares. (Rates of depreciation computed on the basis of useful lives : Machinery 10%, Furniture 15%)

(c) On 31st March, 2020, Bills payable of Rs.12,000 in s Ltd.'s Balance Sheet were accepted in favour of H Ltd.

You are required to prepare Consolidate Balance Sheet of H Ltd. and its Subsidiary S Ltd. as at 31st March, 2020.

Solution :

Consolidated Balance Sheet of H Ltd. and its Subsidiary S Ltd. as at 31st March, 2020

Particulars	Note No.	Rs.
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	13,40,000
(b) Reserves and Surplus	2	8,27,040
(2) Minority Interest		1,15,560
(3) Non- Current Liabilities		
(a) 12% Debentures		1,00,000
(4) Current Liabilities		
(a) Trade Payables	3	3,84,800
(b) Short term Borrowings (Bank overdraft)		1,00,000
Total		**28,67,400**
II. Assets		
(1) Non-current assets		
(a)		
(i) Property, Plant and Equipment	4	14,34,600
(ii) Intangible assets	5	28,800
Current assets		
(a) Inventory (6,00,000+2,00,000)		8,00,000
(b) Trade Receivables	6	5,08,000
(c) Cash and Cash equivalents		96,000

Total		**28,67,400**

Notes to Accounts

				Rs.
	Share Capital			
	Equity share capital			13,40,000
	1,34,000 shares of Rs. 10 each fully paid up			
	Reserves and Surplus			
	Reserves		4,80,000	
	Add: 4/5th share of S Ltd.'s postacquisition reserves (W.N.3)		96,000	5,76,000
	Profit and Loss Account		2,40,000	
	Add: 4/5th share of S Ltd.'s postacquisition profits (W.N.4)		11,040	2,51,040
				8,27,040
	Trade Payables			
	H Ltd.	2,00,000		
	S Ltd.	1,22,000	3,22,000	
	Bills Payables			
	H Ltd.	60,000		
	S Ltd.	14,800	74,800	
			3,96,800	
	Less: Mutual Owings		(12,000)	3,84,800
	Property Plant and Equipment			
	Machinery			
	H. Ltd.		7,20,000	
	S Ltd.	2,40,000		
	Add: Appreciation	1,20,000		
		3,60,000		
	Less: Depreciation (3,60,000 X 10%)	(36,000)	3,24,000	
	Furniture			
	H. Ltd.		3,60,000	
	S Ltd.	48,000		
	Less: Decrease in value	(12,000)		
		36,000		
	Less: Depreciation (36,000 X 15%)	5,400	30,600	14,34,600
	Intangible assets			
	Goodwill [WN 6]			28,800
	Trade receivables			

	H Ltd.	3,00,000		
	S Ltd.	90,000	3,90,000	
	Bills Receivables			
	H Ltd.	1,00,000		
	S Ltd.	30,000	1,30,000	
			5,20,000	
	Less: Mutual Owings		(12,000)	5,08,000

Working Notes :

1	Pre-acquisition profits and reserves of S Ltd.	Rs.
	Reserves	60,000
	Profit and Loss Account	36,000
		96,000
	H Ltd.'s = 4/5 (or 80%) × 96,000	76,800
	Minority Interest= 1/5 (or 20%) × 96,000	19,200
2	Profit on revaluation of assets of S Ltd.	
	Profit on Machinery Rs. (3,60,000 – 2,40,000)	1,20,000
	Less: Loss on Furniture Rs.(48,000 –36,000)	(12,000)
	Net Profit on revaluation	1,08,000
	H Ltd.'s share 4/5 × 1,08,000	86,400
	Minority Interest 1/5 × 1,08,000	21,600
3	Post-acquisition reserves of S Ltd.	
	Total reserves	1,80,000
	Less: Pre- acquisition reserves	(60,000)
	Post-acquisition reserves	1,20,000
	H Ltd.'s share 4/5 × 1,20,000	96,000
	Minority interest 1/5 × 1,20,000	24,000
4	Post -acquisition profits of S Ltd.	
	Post-acquisition profits (Profit & loss account balance pre-acquisition profits = Rs. 60,000 – 36,000)	24,000
	Add: Excess depreciation charged on furniture @ 15% on Rs. 12,000 i.e. (48,000 – 36,000)	1,800
		25,800
	Less: Under depreciation on machinery @ 10% on Rs. 1,20,000 i.e. (3,60,000 – 2,40,000)	(12,000)
	Adjusted post-acquisition profits	13,800
	H Ltd.'s share 4/5 × 13,800	11,040
	Minority Interest 1/5 × 13,800	2,760
5	Minority Interest	

	Paid-up value of (24,000 – 19,200) = 4,800 shares held by outsiders i.e. 2,40,000 X 20%	48,000
	Add: 1/5th share of pre-acquisition profits and reserves	19,200
	1/5th share of profit on revaluation	21,600
	1/5th share of post-acquisition reserves	24,000
	1/5th share of post-acquisition profit	2,760
		1,15,560
6	Cost of Control or Goodwill	
	Price paid by H Ltd. for 19,200 shares (A)	3,84,000
	Less: Intrinsic value of the shares	
	Paid-up value of shares held by H Ltd. i.e. 2,40,000 X 80%	1,92,000
	Add: 4/5th share of pre-acquisition profits and reserves	76,800
	4/5th share of profit on the revaluation	86,400
	Intrinsic value of shares on the date of acquisition (B)	3,55,200
	Cost of control or Goodwill (A – B)	28,800

Question 11 : May – 2021 – RTP

A Ltd. acquired 70% equity shares of B Ltd. @ Rs.20 per share (Face value - Rs.10) on 31st March, 2021 at a cost of Rs. 140 lakhs. Calculate the amount of share of A Ltd. and minority interest in the net assets of B Ltd. on this date. Also compute goodwill/capital reserve for A Ltd. on acquisition of shares of B Ltd. from the following information available from the balance sheet of B Ltd. as on 31st March, 2021:

	Rs. in lakhs
Property, plant and equipment	360
Investments	90
Current Assets	140
Loans & Advances	30
15% Debentures	180
Current Liabilities	100

Solution :

Net assets of B Ltd. as on 31st March, 2021

	Rs. in lakhs	**Rs. in lakhs**
Property, plant and equipment		360
Investments		90
Current Assets		140
Loans and Advances		30
Total Assets		620
Less: 15% Debentures	180.0	
Current Liabilities	100.0	(280)

Equity / Net Worth		340
Share of Minority Interest in net assets (30% of 340)		102
A Ltd.'s share in net assets (70% of 340)		238
A Ltd.'s cost of acquisition of shares of B Ltd. (Rs.140 lakhs)		(140)
Capital reserve		98

Question 12 : July – 2021 – Paper

The Trial Balances of X Limited and Y Limited as on 31st March, 2021 were as under :

	X Limited		Y Limited	
	(Rs. in 000)		(Rs. in 000)	
	Dr.	Cr.	Dr.	Cr.
Equity Share capital (Share of Rs.100 each)	–	2,000	–	400
7% Preference share capital	–	–	–	400
Reserve	–	600	–	200
6% Debentures	–	400	–	400
Trade Payable/Trade Receivables	160	180	100	120
Profit & Loss A/c balance	–	40	–	30
Purchases/Sales	1,000	1,800	1,200	1,000
Wages and Salaries	200	–	300	–
Debenture Interest	24	–	24	–
General Expenses	160	–	120	–
Preference share dividend up to 30.09.2020	–	7	14	–
Inventory (as on 31.03.2021)	200	–	100	–
Cash at Bank	27	–	12	–
Investment in Y Limited	1,056	–	–	–
Fixed Assets	2,200	–	1,580	–
Total	**5,027**	**5,027**	**3,450**	**3,450**

Investment in Y Limited was acquired on 1st July, 2020 and consisted of 80% of Equity Share Capital and 50% of Preference Share Capital.

– After acquiring control over Y Limited, X Limited supplied to Y Limited goods at cost plus 25%, the total invoice valued of such goods being Rs.1,20,000, one fourth of such goods were still lying in inventory at the end of the year.

– Depreciation to be charged @ 10% in X Limited and 15% in Y Limited on Fixed Assets.

You are required to prepare the Consolidated Statement of Profit and Loss for the year ended on 31st March, 2021.

Solution :

Consolidated Statement of Profit & Loss Account of X Ltd. and Y Ltd.
for the year ended 31st March, 2021

Particulars		Note No.	Rs.
I.	Revenue from operations	1	35,80,000
II.	Total revenue		35,80,000
III.	Expenses		
	Cost of Material purchased/Consumed	2	20,80,000
	Changes of Inventories of finished goods		-
	Employee benefit expense	3	5,00,000
	Finance cost	4	48,000
	Depreciation and amortization expense	5	4,57,000
	Other expenses	6	2,80,000
	Total expenses		33,65,000
IV.	Profit before Tax (II-III)		2,15,000
Profit transferred to Consolidated Balance Sheet			
Profit After Tax			2,15,000
Preference dividend		7,000	
Preference dividend payable		7,000	(14,000)
			2,01,000
Share in pre-acquisition loss (WN 3)			1,800
Share of Minority interest in losses (WN 1)			1,800
Less:	Investment Account- dividend for 3 months (prior to acquisition)		(3,500)
Inventory reserve (WN 2)			(6,000)
Profit to be transferred to consolidated balance sheet			1,95,100

Notes to Accounts :

		Rs.	Rs.
1	Revenue from Operations		
	X Ltd.	18,00,000	
	Y Ltd.	19,00,000	
	Total	37,00,000	
	Less: Intra-group sales (X sold to Y)	(1,20,000)	35,80,000
2	Cost of Materials Purchased/Consumed		
	X Ltd.	10,00,000	
	Y Ltd.	12,00,000	
	Total	22,00,000	
	Less: Intra-group sales (X sold to Y)	(1,20,000)	20,80,000
3	Employee benefit and expenses		

	Wages and salaries		
	H Ltd.	2,00,000	
	S Ltd.	3,00,000	5,00,000
4	Finance cost		
	Interest		
	H Ltd.	24,000	
	S Ltd.	24,000	48,000
5	Depreciation		
	H Ltd.	2,20,000	
	S Ltd.	2,37,000	4,57,000
6	Other expenses		
	H Ltd.	1,60,000	
	S Ltd.	1,20,000	2,80,000

Working Notes:

1. Profit of Subsidiary

		Rs.
Revenue from Operations		19,00,000
Less: Expenses		
Cost of Material purchased/Consumed	12,00,000	
Changes of Inventories of finished goods	-	
Employee benefit expense	3,00,000	
Finance cost	24,000	
Depreciation and amortization expense	2,37,000	
Other expenses	1,20,000	
Total expenses		(18,81,000)
Profit Before Tax		19,000
Less: Preference Dividend	14,000	
Less: Preference Dividend Payable	14,000	(28,000)
Profit available for shareholders		(9,000)
Minority Share (20% of loss Rs. 9,000)		(1,800)

2. **Inventory reserve** = $\left[\frac{1,20,000}{4} \times \frac{25}{125}\right]$ = Rs. 6,000

3. **Pre-acquisition loss** = 80% of 3 month's profit up to 30th June,2020 i.e. 80 % of ¼ of loss Rs. 9,000. Hence, pre-acquisition loss = Rs. 1,800

4. Investment account includes Preference dividend for 3 months prior to acquisition i.e. Rs. 4,00,000 x 50% x 7% x 1/4 = Rs. 3,500

Question 13 : July – 2021 – Paper

Long Limited acquired 60% stake in Short Limited for a consideration of Rs.112 lakhs. On the date of acquisition Short Limited's Equity Share Capital was Rs.100 lakhs, Revenue Reserve was Rs.40 lakhs and balance in Profit and Loss Account was Rs.30 lakhs. From the above information you are required to calculate Goodwill/Capital Reserve in the following situations :

(i) On consolidation of Balance Sheet.

(ii) If Long Limited showed the investment in subsidiary at a carrying amount of Rs.104 lakhs.

(iii) If the consideration paid for acquiring the 60% stake was Rs.92 lakhs.

Solution :

	Rs.
60% of the Equity Share Capital Rs. 100 Lakhs	60
60% of Accumulated Reserve Rs. 70 Lakhs (40+30) Lakhs	42
Book value of shares of Short Ltd.	102

(i) Goodwill / Capital Reserve computation on consolidation of balance sheet
Long Ltd. paid a positive differential of Rs. 10 Lakhs (112 - 102). This differential Rs. 10 Lakhs is called goodwill and is shown in the balance sheet under the head intangibles.

(ii) If Long Ltd. showed the investment in Short Ltd. at carrying amount of Rs. 104 Lakhs, then the goodwill will be Rs. 2 Lakhs.

(iii) If the consideration paid is Rs. 92 lakhs, then there would have been capital reserve amounting Rs. 10 Lakhs (102- 92).

Question 14 : Nov – 2021 – RTP

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. Rs.	**Q Ltd. 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:

(a) Before issue of bonus shares.

(b) Immediately after issue of bonus shares.

Solution :

Shareholding pattern

	Particulars	Number of Shares	% of holding
a.	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%
b.	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:

(a) 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 (Before and after issue of bonus shares)	Revenue Profits	
		Before Bonus Issue	After Bonus Issue
	Rs.	Rs.	Rs.
Pre-incorporation profits	30,000		
Profit and loss account on 31.3.2015	60,000		
	90,000		
General reserve*		19,05,000	19,05,000
Less: Bonus shares			(7,50,000)
			11,55,000
Profit for period of 1st April, 2015 to 31st 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 15 : Dec – 2021 – Paper

Moon ltd. and its subsidiary Star Ltd. provided the following information for the year ended 31st March, 2021.

Particulars	Moon Ltd. (Rs.)	Star Ltd. (Rs.)
Equity Share Capital	20,00,000	6,000,000
Finished goods Inventory as on 01.04.2020	4,200,000	3,010,000
Finished Goods Inventory as on 31.03.2021	8,575,000	3,762,500
Dividend Income	1,680,000	437,500
Other non-operating Income	350,000	105,000
Raw material consumed	13,930,000	4,725,000
Selling and Distributed Expenses	3,325,000	1,575,000
Production Expenses	3,150,000	1,400,000
Loss on sale of investments	262,500	Nil
Sales and other operating income	33,250,000	19,075,000
Wages and Salaries	13,300,000	2,450,000
General and Administrative Expenses	2,800,000	1,225,000
Royalty paid	Nil	50,000
Depreciation	315,000	140,000
Interest expense	175,000	52,500

Other information :

- On 1st September, 2018 Moon Ltd. acquired 50,000 equity shares of Rs.100 each fully paid up in Star Ltd.
- Star Ltd. paid a dividend of 10% for the year ended 31st March, 2020. The dividend was correctly accounted for by Moon Ltd.
- Moon Ltd. sold goods of Rs.17,50,000 to Star Ltd. at a profit of 20% on selling price. Inventory of Star Ltd. includes goods of Rs.7,00,000 received from Moon Ltd.
- Selling and Distribution expenses of Star Ltd. include Rs.2,12,500 paid to Moon Ltd. as brokerage fees.
- General and Administrative expenses of Moon Ltd. include Rs.2,80,000 paid to Star Ltd. as consultancy fees.
- Star Ltd. used some resources of Moon Ltd. and Star Ltd. paid Rs.50,000 to Moon Ltd. as royalty.

Prepare consolidated statement of Profit and Loss of Moon Ltd. and its subsidiary Star Ltd. for the year ended 31.03.2021 as per schedule II of the Companies Act, 2013.

Solution :

Consolidated statement of profit and loss of Moon Ltd. and its subsidiary Star Ltd. for the year ended on 31st March, 2021

Particulars	Note No.	Rs.
Revenue from operations	1	5,00,32,500
Other Income	2	23,10,000

Total revenue (I)		5,23,42,500
Expenses:		
Cost of material purchased/consumed	3	2,14,55,000
Changes (Increase) in inventories of finished goods	4	-49,87,500
Employee benefit expense	5	1,57,50,000
Finance cost	6	2,27,500
Depreciation and amortization expense	7	4,55,000
Other expenses	8	84,32,500
Total expenses (II)		4,13,32,500
Profit before tax (II-III)		1,10,10,000

Notes to Accounts:

			Rs.	Rs.
1	Revenue from operations			
	Sales and other operating revenues1			
	Moon Ltd.		3,32,50,000	
	Star Ltd.		1,90,75,000	
			5,23,25,000	
	Less: Inter-company sales		(17,50,000)	
	Consultancy fees received by Star Ltd. from Moon Ltd.		(2,80,000)	
	Royalty received by Moon Ltd. from Star Ltd.		(50,000)	
	Brokage received by Moon Ltd. from Star Ltd.		(2,12,500)	5,00,32,500
2	Other Income			
	Dividend income:			
	Moon Ltd.	16,80,000		
	Star Ltd.	4,37,500	21,17,500	
	Loss on sale of investments Star Ltd.		(2,62,500)	
	Other Non-operating Income			
	Moon Ltd.	3,50,000		
	Star Ltd.	1,05,000	4,55,000	23,10,000
3	Cost of material purchased/consumed			
	Moon Ltd.	1,39,30,000		
	Star Ltd.	47,25,000		
		1,86,55,000		
	Less: Purchases by Star Ltd. From Moon Ltd.	(17,50,000)	1,69,05,000	
	Direct expenses (Production)			
	Moon Ltd.	31,50,000		

	Star Ltd.	14,00,000	45,50,000	
4	Changes (Increase) in inventories of finished goods			
	Moon Ltd.		43,75,000	
	Star Ltd.		7,52,500	
			51,27,500	
	Less: Unrealized profits Rs. 7,00,000 × 20/100		(1,40,000)	49,87,500
5	Employee benefits and expenses			
	Wages and salaries:			
	Moon Ltd.		1,33,00,000	
	Star Ltd.		24,50,000	1,57,50,000
6	Finance cost			
	Interest:			
	Moon Ltd.		1,75,000	
	Star Ltd.		52,500	2,27,500
7	Depreciation			
	Moon Ltd.		3,15,000	
	Star Ltd.		1,40,000	4,55,000
8	Other expenses			
	General & Administrative expenses:			
	Moon Ltd.	28,00,000		
	Star Ltd.	12,25,000		
		40,25,000		
	Less: Consultancy fees received by Star Ltd. from Moon Ltd.	(2,80,000)	37,45,000	
	Royalty:			
	Star Ltd.	50,000		
	Less: Received by Moon Ltd.	(50,000)	Nil	
	Selling and distribution Expenses:			
	Moon Ltd.	33,25,000		
	Star Ltd.	15,75,000		
		49,00,000		
	Less: Brokerage received by Moon Ltd. from Star Ltd.	(2,12,500)	46,87,500	84,32,500

Question 16 : May – 2022 – RTP

From the following information of Beta Ltd. and its subsidiary Gamma Ltd. drawn up at 31st March, 2021, prepare a consolidated balance sheet as at that date:

	Beta Ltd. Rs.	Gamma Ltd. Rs.
Share Capital:		
Shares of Rs. 100 each	15,00,000	2,50,000
Reserves	5,00,000	1,87,500
Profit and Loss Account	2,50,000	62,500
Trade Payables	3,75,000	1,42,500
Property, plant and Equipment:		
Machinery	7,50,000	2,25,000
Furniture	3,75,000	42,500
Other non-current assets	11,00,000	3,75,000
Non-current Investments:		
Shares in Gamma Ltd.: 2,000 shares at Rs. 200 each	4,00,000	

Other information:

Reserves and Profit and Loss Account of Gamma Ltd. stood at Rs. 62,500 and Rs. 37,500 respectively on the date of acquisition of its 80% shares by Beta Ltd. on 1st April, 2020. Machinery (Book-value Rs. 2,50,000) and Furniture (Book value Rs. 50,000) of Gamma Ltd. were revalued at Rs. 3,75,000 and Rs. 37,500 respectively on 1st April, 2020 for the purpose of fixing the price of its shares. [Rates of depreciation computed on the basis of useful lives: Machinery 10%, Furniture 15%.]

Solution :

Consolidated Balance Sheet of Beta Ltd. and its Subsidiary Gamma Ltd. as at 31st March, 2021

Particulars			Note No.	Rs.
I.	**Equity and Liabilities**			
	(1)	**Shareholder's Funds**		
		(a) Share Capital		15,00,000
		(b) Reserves and Surplus	1	8,61,500
	(2)	**Minority Interest** (W.N.5)		1,20,375
	(3)	**Current Liabilities**		
		(a) Trade Payables	2	5,17,500
		Total		**29,99,375**
II.	**Assets**			
	(1)	**Non-current assets**		
		(a) (i) Property, Plant & Equipment	3	14,94,375
		(ii) Intangible assets	4	30,000
		(b) Other non- current assets	5	14,75,000
		Total		**29,99,375**

Notes to Accounts

				Rs.
1	**Reserves and Surplus**			
	Reserves		5,00,000	
	Add: 4/5th share of Gamma Ltd.'s post-acquisition reserves (W.N.3)		1,00,000	6,00,000
	Profit and Loss Account		2,50,000	
	Add: 4/5th share of Gamma Ltd.'s post-acquisition profits (W.N.4)		11,500	2,61,500
				8,61,500
2	**Trade Payables**			
	Beta Ltd.		3,75,000	
	Gamma Ltd.		1,42,500	5,17,500
3	**Property, Plant & Equipment**			
	Machinery			
	Beta Ltd.		7,50,000	
	Gamma Ltd.	2,50,000		
	Add: Appreciation	1,25,000		
		3,75,000		
	Less: Depreciation	(37,500)	3,37,500	
	Furniture			
	Beta Ltd.		3,75,000	
	Gamma Ltd.	50,000		
	Less: Decrease in value	(12,500)		
		37,500		
	Less: Depreciation	(5,625)	31,875	14,94,37
4	**Intangible assets**			
	Goodwill [WN 6]			30,000
5	**Other non-current assets**			
	Beta Ltd.		11,00,000	
	Gamma Ltd.		3,75,000	14,75,00

Working Notes :

1	**Pre-acquisition profits and reserves of Gamma Ltd.**	**Rs.**
	Reserves	62,500
	Profit and Loss Account	37,500
		1,00,000

	Beta Ltd.'s = 4/5 × 1,00,000	80,000
	Minority Interest = 1/5 × 1,00,000	20,000
2	**Profit on revaluation of assets of Gamma Ltd.**	
	Profit on Machinery Rs. (3,75,000 – 2,50,000)	1,25,000
	Less: Loss on Furniture Rs. (50,000 – 37,500)	12,500
	Net Profit on revaluation	1,12,500
	Beta Ltd.'s share 4/5 × 1,12,500	90,000
	Minority Interest 1/5 × 1,12,500	22,500
3	**Post-acquisition reserves of Gamma Ltd.**	
	Post-acquisition reserves (Total reserves less pre-acquisition reserves = Rs. 1,87,500 – 62,500)	1,25,000
	Beta Ltd.'s share 4/5 × 1,25,000	1,00,000
	Minority interest 1/5 × 25,000	25,000
4	**Post -acquisition profits of Gamma Ltd.**	
	Post-acquisition profits (Profit & loss account balance less pre-acquisition profits = Rs. 62,500 – 37,500)	25,000
	Add: Excess depreciation charged on furniture @ 15% on Rs. 12,500 i.e. (50,000 – 37,500)	1,875
		26,875
	Less: Under depreciation on machinery @ 10% on Rs. 1,25,000 i.e. (3,75,000 – 2,50,000)	(12,500)
	Adjusted post-acquisition profits	14,375
	Beta Ltd.'s share 4/5 × 14,375	11,500
	Minority Interest 1/5 × 14,375	2,875
5	**Minority Interest**	
	Paid-up value of (2,500 – 2,000) = 500 shares held by outsiders i.e. 500 × Rs. 100	50,000
	Add: 1/5th share of pre-acquisition profits and reserves	20,000
	1/5th share of profit on revaluation	22,500
	1/5th share of post-acquisition reserves	25,000
	1/5th share of post-acquisition profit	2,875
		1,20,375
6	**Cost of Control or Goodwill**	
	Paid-up value of 2,000 shares held by Beta Ltd. i.e. 2,000 × Rs. 100	2,00,000
	Add: 4/5th share of pre-acquisition profits and reserves	80,000
	4/5th share of profit on the revaluation	90,000

	Intrinsic value of shares on the date of acquisition	3,70,000
	Price paid by Beta Ltd. for 2,000 shares	4,00,000
	Less: Intrinsic value of the shares	(3,70,000)
	Cost of control or Goodwill	30,000

Question 17 : May – 2022 – Paper

White Ltd. acquired 2,250 shares of Black Ltd. on 1st October, 2020. The summarized balance sheets of both the companies as on 31st March, 2021 are given below :

			White Ltd. (Rs.)	Black Ltd. (Rs.)
(I)	**Equity and Liabilities**			
	(1)	**Shareholder's fund**		
		Share capital (Equity shares of Rs.100 each fully paid up)	6,50,000	3,00,000
		Reserves and Surplus		
		General Reserve	60,000	30,000
		Profit and loss account	1,50,000	90,000
	(2)	**Current Liabilities**		
		Trade payables	1,15,000	75,000
		Due to White Ltd.	-	30,000
Total			**9,75,000**	**5,25,000**
(II)	**Assets:**			
	Non-current assets			
	Property, Plant and Equipment		5,80,000	3,51,000
	Investments			
	Shares in Black Ltd. (2,250 shares)		2,70,000	-
	Current assets			
	Inventories		50,000	1,20,000
	Due from Black Ltd.		36,000	-
	Cash and Cash equivalents		39,000	54,000
Total			**9,75,000**	**5,25,000**

Other information :

(i) During the year, Black Limited fabricated a machine, which is sold to White Ltd. for Rs.39,000, the transaction being completed on 30th March, 2021.

(ii) Cash in transit from Black Ltd. to White Ltd. was Rs.6,000 on 31st March, 2021.

(iii) Profits during the year 2020-2021 were earned evenly.

(iv) The balances of Reserves and Profit and Loss account as on 1st April, 2020 were as follows:

	Reserves Rs.	Profit and loss a/c Rs.
White Ltd.	30,000	15,000 Profit
Black Ltd.	30,000	10,000 Loss

You are required to prepare consolidated Balance Sheet of the group as on 31st March, 2021 as per the requirement of Schedule III of the Companies Act, 2013.

Solution :

Consolidated Balance Sheet of White Ltd. and its Subsidiary Black Ltd.
as at 31st March, 2021

Particulars	Note No.	Rs.
I. Equity and Liabilities		
(1) **Shareholder's Funds**		
(a) Share Capital	1	6,50,000
(b) Reserves and Surplus	2	2,55,000
(2) **Minority Interest**	3	1,05,000
(3) **Current Liabilities**		
(a) Trade Payables	4	1,90,000
Total		12,00,000
II. Assets		
(1) **Non-current assets**		
(a) Property, Plant and Equipment	5	9,31,000
(2) **Current assets**		
(a) Inventory	6	1,70,000
(b) Cash & cash equivalent	7	99,000
Total		12,00,000

Notes to Accounts

			Rs.
1	**Share capital**		
	6,500 equity shares of Rs. 100 each, fully paid up		6,50,000
	Total		6,50,000
2	**Reserves and Surplus**		
	General Reserves		60,000
	Profit and Loss Account	1,50,000	
	Add: 75% share of Black Ltd.'s post-acquisition profits (W.N.1)	37,500	1,87,500
	Capital reserve (W.N. 5)		7,500
	Total		2,55,000
3	**Minority interest in Black Ltd. (WN 4)**		1,05,000

4	**Trade payables**		
	White Ltd.	1,15,000	
	Black Ltd.	75,000	1,90,000
5	**Property, plant and equipment**		
	White Ltd.	5,80,000	
	Black Ltd.	3,51,000	9,31,000
6	**Inventory**		
	White Ltd.	50,000	
	Black Ltd.	1,20,000	1,70,000
7	**Cash & cash equivalent**		
	White Ltd.	39,000	
	Black Ltd.	54,000	
	Cash in transit	6,000	99,000

Working Notes :

1	**Post-acquisition profits of Black Ltd.**	**Rs.**
	profits earned during the year = Rs. 90,000 + Rs.10,000	1,00,000
	Pre-acquisition profits (1.4.20 to 30.9.20)	50,000
	Post-acquisition profits (1.10.20 to 31.3.21)	50,000
	White Ltd.'s share 75% of 50,000	37,500
	Minority Interest 25% of 50,000	12,500
2	**Pre-acquisition profits and reserves of Black Ltd.**	
	Reserves as on 1.4.2020	30,000
	Profit and Loss Account	40,000
	[10,000 (loss as on 1.4.20) +50,000 (6 month Adjusted pre-acquisition profits)]	
		70,000
	White Ltd.'s = (75%) × 70,000	52,500
	Minority Interest= (25%) × 70,000	17,500
3	**Post-acquisition reserves of Black Ltd.**	
	Post-acquisition reserves (Total reserves less pre-acquisition reserves = Rs. 30,000 – 30,000)	nil
4	**Minority Interest**	
	Paid-up value of (3,000 – 2,250) = 750 shares	
	held by outsiders i.e. 750 × Rs. 100	75,000
	Add: 25% share of pre-acquisition reserves & Profit	17,500
	25% share of post-acquisition profit	12,500
		1,05,000
5	**Capital Reserve**	
	Price paid by White Ltd. for 2,250 shares (A)	2,70,000

	Intrinsic value of the shares- Paid-up value of 2,250 shares held by White Ltd. i.e. 2,250 × Rs. 100	2,25,000	
	Add 75% share of pre-acquisition reserves & profit (70,000 x 75%) (B)	52,500	2,77,500
	Capital reserve (A – B)		7,500

Question 18 : Nov – 2022 – RTP

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 at which 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, 2021, 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 on 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		
	Authorised share capital		
	5 lakhs equity shares of Rs. 10 each		5,000
	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*x 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 $\left(\frac{2,400 \times 3}{8}\right)$	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 $\frac{1,500 \times 20}{100}$	300	By Net Profit for the year (Balancing figure)	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
Share of H Ltd. (60%)	340.2
Share of Minority shareholders (567– 340.20)	226.8

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 working note (4)		559.80
		1,999.80
Less: Investments in S Ltd.	1,500	
Less: Dividends received out of pre- acquisition profits $\frac{Rs.300 \times 60}{100}$	(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
	1560.00

Question 19 : Nov – 2022 – Paper

H Ltd. and S Ltd. provide the following information as at 31st March, 2022:

	H Ltd. Rs.	S Ltd. Rs.
Property, Plant and Equipment	2,00,000	2,60,000
Investments (14,000 Equity Shares of S Ltd.)	2,52,000	-

Current Assets	1,48,000	1,40,000
Share capital (Fully paid equity shares of Rs.10 each)	3,00,000	2,00,000
Profit and loss account	1,00,000	80,000
Trade Payables	2,00,000	1,20,000

Additional information :

H Ltd. acquired the shares of S Ltd. on 1st July, 2021 and Balance of profit and loss account of S Ltd. on 1st April, 2021 was Rs.60,000.

Prepare consolidated balance sheet of H Ltd. and its subsidiary as at 31st March, 2022.

Thanks ....

Rahul Malkan

CHAPTER 23

SCHEDULE 3 OF COMPANIES ACT, 2013

Question 1 : Nov – 2018 – Paper

Sagar Ltd. has issued convertible bonds for Rs.65 crores which are due to mature on 30th September, 2018.

While preparing financial statements for the year ending 31st March, 2018, company expects that bond holders will not exercise their option of converting bonds to equity shares. How should the company classify the convertible bonds as per the requirements of Schedule-Ill to the Companies Act, 2013 as on 31st March, 2018?

Also state, whether classification of convertible Bonds as per Schedule-III to the Companies Act will change if the company expects that convertible bond holders will convert their holdings into equity shares of Sagar Ltd.

Solution :

Schedule III to the companies Act, 2013 provides that:

"A liability should be classified as current when it satisfies any of the following criteria:

(a) it is expected to be settled in the company's normal operating cycle;

(b) it is held primarily for the purpose of being traded;

(c) it is due to be settled within twelve months after the reporting date; or

(d) the company does not have an unconditional right to defer settlement of the liability for at least twelve months after the reporting date. Terms of a liability that could, at the option of the counterparty, result in its settlement by the issue of equity instruments and do not affect its classification."

In the present situation, Sagar Ltd. does not have an unconditional right to defer settlement of the liability for at least 12 months after the reporting date, hence Sagar Ltd. should classify the FCCBs as current liabilities as on 31st March 2018.

The position will be same even when the bond holders are expected to convert their holdings into equity shares of Sagar Ltd. Expectations cannot be called as unconditional rights. Thus, in this situation also, Sagar Ltd. should classify the FCCBs as current liabilities as on 31st March 2018.

Question 2 : Nov – 2019 – Paper

X Ltd. is a company engaged in manufacture and sale of industrial and FMCG products. One of their division also deals in Leasing of properties - Mobile Towers. The accountant showed the rent arising from the leasing of such properties as other income in the Statement of Profit and Loss. Comment whether the classification of the rent income made by the accountant is correct or not in light of Schedule III to the Companies Act, 2013.

Solution :

As per para 4 of the 'General Instructions for preparation of Statement of Profit and Loss' given in the Schedule III to the Companies Act, 2013, 'other income' does not include operating income. The term "Revenue from operations" has not been defined under Schedule III to the Companies Act 2013. However, as per Guidance Note on Schedule III to the Companies Act 2013 this would include revenue arising from a company's operating activities i.e. either its principal or ancillary revenue-generating activities. Whether a particular income constitutes "Revenue from operations" or "other income" is to be decided based on the facts of each case and detailed understanding of the company's activities. The classification of income would also depend on the purpose for which the particular asset is acquired or held.

As per the information given in the question, X Ltd is a group engaged in manufacture and sale of industrial and FMCG products and its one of the division deals in leasing of properties- Mobile Towers. Since its one division is continuously engaged in leasing of properties, it shall be considered as its principal or ancillary revenue-generating activities. Therefore, the rent arising from such leasing shall be shown under the head "Revenue from operations" and not as "Other Income".

Hence the presentation of rent arising from the leasing of such properties as "other income" in the statement of Profit and Loss is not correct. It should be shown under the head "Revenue from operations".

Thanks ....

Rahul Malkan

CHAPTER 24

THEORY

Question 1 : May – 2018 – Paper

Describe the different types of marine losses.

Solution :

Marine losses may be broadly of two types –

(i) **Total Loss:** When the subject matter of insurance, i.e., cargo, ship, freight etc. is totally lost, it is known as a 'total loss'. Total loss is also of two types:

   (a) **Actual Total Loss :** When the subject-matter of insurance is absolutely destroyed or totally lost to the insured, it is known as actual total loss.

   (b) **Constructive Total Loss :** When the subject matter is not actually totally lost but is lost for all practical purposes e.g., where the ship or cargo is reasonably abandoned and taken as lost or expenses to be incurred for saving the cargo or the ship are expected to be more than the value thereof, it is known as constructive total loss.

(ii) **Partial Loss:** When only a part of the subject matter is lost, it is known as partial loss. This loss may also be of two types as discussed below :

   (a) **General Average Loss :** Such a loss is caused by extraordinary voluntary sacrifice made or expenditure incurred with the objective of protecting the interests of all owners in a voyage. An example of this type of loss is when the ship has run aground and part of the cargo is to be jettisoned to lighten the ship to save it as well as the cargo from total loss.

   (b) **Particular Average Loss :** It is a partial loss of the subject matter of insurance caused by a peril against which it is insured but which is not a general average loss.

Question 2 : May – 2018 – Paper

How is Minimum Alternative Tax (MAT) to be presented in the financial statements?

Solution :

MAT is treated as the current tax. The tax expense arising on account of payment of MAT should be charged at the gross amount, in the normal way, to the profit and loss account in the year of payment of MAT. In the year in which the MAT credit becomes eligible to be recognized as an asset in accordance with the recommendations contained in the Guidance Note on Accounting

for Credit Available in respect of Minimum Alternate Tax under the Income Tax Act, the said asset should be created by way of a credit to the profit and loss account and presented as a separate line item therein.

MAT credit should be presented under the head under the head 'Non-current Assets' sub head 'Long-term Loans and Advances' as per Schedule III to the Companies Act, 2013 considering that there being a convincing evidence of realization of the asset, it is of the nature of a pre-paid tax which would be adjusted against the normal income tax during the specified period. The asset may be reflected as 'MAT credit entitlement'.

In the year of set-off of credit, the amount of credit availed should be shown as a deduction from the 'Provision for Taxation' on the liabilities side of the balance sheet. The unavailed amount of MAT credit entitlement, if any, should continue to be presented under the head 'Loans and Advances' if it continues to meet the considerations stated in the Guidance Note.

Question 3 : Nov – 2018 – Paper

What are the initial disclosure requirements of AS 24 for discontinuing operations?

Solution :

An enterprise should include the following information relating to a discontinuing operation in its financial statements beginning with the financial statements for the period in which the initial disclosure event occurs:

A. A description of the discontinuing operation(s)

B. The business or geographical segment(s) in which it is reported as per AS 17

C. The date and nature of the initial disclosure event.

D. The date or period in which the discontinuance is expected to be completed if known or determinable

E. The carrying amounts, as of the balance sheet date, of the total assets to be disposed of and the total liabilities to be settled

F. The amounts of revenue and expenses in respect of the ordinary activities attributable to the discontinuing operation during the current financial reporting period

G. The amount of pre-tax profit or loss from ordinary activities attributable to the discontinuing operation during the current financial reporting period, and the income tax expense related thereto

H. The amounts of net cash flows attributable to the operating, investing, and financing activities of the discontinuing operation during the current financial reporting period

Question 4 : May – 2019 – Paper

Distinguish between Amalgamation, Absorption and External Reconstruction of Company.

Solution :

Difference between Amalgamation, Absorption and External Reconstruction

Basis	Amalgamation	Absorption	External Reconstruction
Meaning	Two or more companies are wound up and a new company is formed to take over their business.	In this case, an existing company takes over the business of one or more existing companies.	In this case, a newly formed company takes over the business of an existing company.
Minimum number of Companies involved	At least three companies are involved.	At least two companies are involved.	Only two companies are involved.
Number of new resultant companies	Only one resultant company is formed. Two companies are wound up to form a single resultant company.	No new resultant company is formed.	Only one resultant company is formed. Under this case a newly formed company takes over the business of an existing company.
Objective	Amalgamation is done to cut competition and reap the economies in large scale.	Absorption is done to cut competition and reap the economies in large scale.	External reconstruction is done to reorganise the financial structure of the company.
Example	A Ltd. and B Ltd. amalgamate to form C Ltd.	A Ltd. takes over the business of another existing company B Ltd.	B Ltd. is formed to take over the business of an existing company A Ltd.

Question 5 : May – 2019 – Paper

What do you mean by 'Accrual' in reference to AS-1? Also, specify any three reasons for 'Accrual Basis of Accounting'.

Solution :

The term "Accrual" has been explained in the AS 1 on Disclosure of Accounting Policies, as "Revenues and costs are accrued, that is, recognised as they are earned or incurred (and not as money is received or paid) and recorded in the financial statements of the periods to which they relate"

Reasons for Accrual Basis of Accounting

1. Accrual basis of accounting, attempts to record the financial effects of the transactions, events, and circumstances of an enterprises in the period in which they occur rather than recording them in the period(s) in which cash is received or paid by the enterprise.

2. Receipts and payments of the period will not coincide with the buying producing or selling events and other economic events that affect entity performance.
3. The goal of Accrual basis of accounting is to follow the matching concept of income and expenditure so that reported net income measures an enterprise's performance during a period instead of merely listing its cash receipts and payments.
4. Accrual basis of accounting recognizes assets, liabilities or components of revenues and expenses for amounts received or paid in cash in past, and amounts expected to be received or paid in cash in the future.
5. Important point of difference between accrual and accounting based on cash receipts and outlay is in timing of recognition of revenues, expenses, gains and losses.

Question 6 : Nov – 2019 – Paper

Explain the criterion of income recognition in the case of Non Banking Financial Companies.

Solution :

Income Recognition in case of NBFC

(1) The income recognition shall be based on recognised accounting principles.

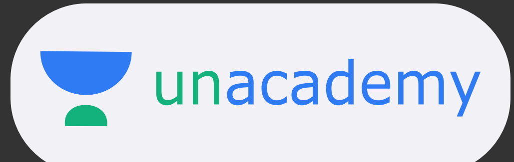
(2) Income including interest/ discount or any other charges on NPA shall be recognised only when it is actually realised. Any such income recognised before the asset became non-performing and remaining unrealised shall be reversed.

(3) In respect of hire purchase assets, where instalments are overdue for more than 12 months, income shall be recognised only when hire charges are actually received. Any such income taken to the credit of profit and loss account before the asset became nonperforming and remaining unrealized, shall be reversed.

(4) In respect of lease assets, where lease rentals are overdue for more than 12 months, the income shall be recognised only when lease rentals are actually received. The net lease rentals* taken to the credit of profit and loss account before the asset became non-performing and remaining unrealised shall be reversed.

*'Net lease rentals' mean gross lease rentals as adjusted by the lease adjustment account debited/credited to the profit and loss account and as reduced by depreciation at the rate applicable under Schedule XIV of the Companies Act, 1956 (1 of 1956)/ 2013.

Thanks ....



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Rahul Malkan is a proficient faculty of Financial Reporting and Strategic Financial Management at CA Final level. He is an MBA in business financial. He has 20 years of experience in teaching industry and has authored 20 books in academics.

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