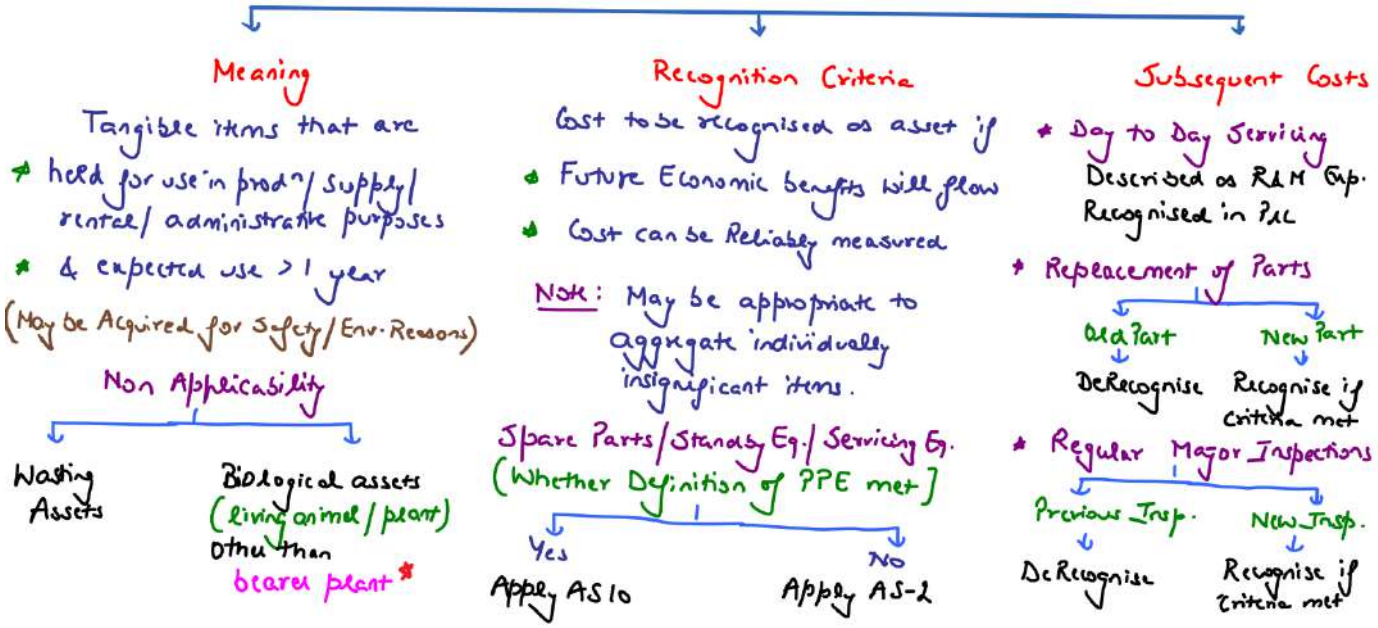
AS-10: PROPERTY, PLANT & EQUIPMENT



Bearer Plant:

is a plant that
(a) is used in the production or supply of agricultural produce;
(b) is expected to bear produce for more than a period of 12 months; and
(c) has a remote likelihood of being sold as agricultural produce, except for incidental scrap sales.
This AS applies to bearer plants but it does not apply to the produce on bearer plants

The following are not Bearer Plants:
(a) Plants cultivated to be ***harvested*** *as* Agricultural produce
Example: Trees grown for use as lumber
(b) Plants cultivated ***to produce*** Agricultural produce when there is more than a remote likelihood that the entity will ***also harvest and sell*** the plant as agricultural produce, other than as incidental scrap sales
Example: Trees which are cultivated both for their fruit and their lumber
(c) Annual crops
Example: Maize and wheat

Measurement of PPE

Initial Recognition (Cost Model)

Direct Purchase

☑
- Purchase Price
- \+ Non Refundable Taxes
- \+ Directly Attributable Costs (Site Prep, Installation fees, Professional fees, Testing cost)
- \+ Decommissioning, Restoration & Liab.

☒
- Cost of Opening new facility
- Cost of Introducing new product
- Costs of Staff training
- Costs of Relocating
- Initial operating losses

Self Constructed

Internal Profits eliminated

Special Cases

1) Deferred Credit
   - Total Payment − Cash Price
   - Recognised as Interest
2) Exchange
   - Measured at Fair value unless
     - Trans^ lacks commercial substance
     - F.V. not measurable
   - Measured at carrying Amt. of asset given
3) Consolidated Price:
   - Apportioned on Fair value basis.

Subsequent Recognition

Choose Either

Cost Model

Revaluation Model

Apply to Entire class of PPE (Assets of Similar Nature & use)

Revaluation Frequency

- Significant & volatile changes in F.V. → ANNUAL
- Insignificant → Interval of 3–5 years

Exchange

Ex: 1

Acquire: Old PPM

Give: Equity shares of company (FV = 10 MP = 30), No: 10000

Value = 10000 × 30 = 300000

Ex: 2

Acquire: New PPM (Fair value = 400000)

Give: Equity shares of company (Unlisted)

Value = 400000

Ex: 2

Acquire: New PPM (Fair value = 400000)

Give: Equity shares of company, No. 10000 (FV = 10 MP = 30)

Value = 3L / 4L w.e. is more clearly evident

Ex: 4

Acquire: Old PPM ~~FV~~

Give: Old car ~~FV~~ (Book value = 200000)

Value = 200000

Ex: 5

Acquire: Car X (FV = 6L)

Give: Car Y (FV = 7L) (Book value = 680000)

Transaction lacks Commercial Substance.

Value = 680000

Revaluation : Accounting Treatment

First Revaluation

- **Upward** → Use Revaluation Surplus (R/s)
- **Downward** → Use P&L A/c

Subsequent Revaluation (Depends)

1st	Use	IInd	Use
↑	R/s	↑	R/s
↓	P&L	↓	P&L
↑	R/s	↓	R/s & then P&L
↓	P&L	↑	P&L & then R/s

Method I :

Proportionate Increase in both Cost & Acc. dep.

Asset
To Acc. dep.
To Rev. Surplus

Method II :

Acc. dep. is eliminated & Balance through Cost

Acc. Dep.
Asset
To Rev. Surplus

Transfer of Rev. Surplus to Revenue Reserve

- **During use of asset** → Some may be treated as Dep. (on Revalued Amt.) − Dep. (on original cost)
- **When asset is derecognised** → Whole surplus is transferred

Example :

Original cost = 500000
Acc. Depreciation = 100000
Revalued at 740000

Method I

	Before Rev.	Increase	After Rev.
Cost	500000	400000	900000
Acc. Dep.	(100000)	(80000)	(180000)
Net/Book Value	400000	320000	740000

Asset 400000
To Acc. Dep. 80000
To Rev. Surplus 320000

Method II :

Acc. Dep. – Dr 100000
Asset – Dr 220000
To Rev. Surplus 320000

OR

Acc. Dep. 100000
To Asset 100000
Asset 320000
To Rev. Surplus 320000

Depreciation

Meaning: Systematic allocation of depreciable amount of asset over its useful life

Component Method: Each part of PPE that is significant in relation to total cost of item should be depreciated separately E.g: Airframe & Engine of Aircraft

Depreciable Amount: Cost/Revalued Amt. − Residual Value

Useful Life: On Basis of Period: Period over which asset is expected to be used
On Basis of Units: No. of units expected to be obtained

Commencement: When asset is available for use.

Cessation of dep.
1. Asset's Residual value ≥ Carrying Amount
2. Earlier of
   - Asset retired from Active use & held for disposal
   - Asset is derecognised

Method of Depreciation

Method should reflect the pattern in which future economic benefits are expected to be consumed by enterprise

- Straight Line Method
- Diminishing Balance/ WDV Method
- Units of Production Method

Review of Dep. Method: Change in Accounting Estimate (Prospective Effect)

Review of Residual value & useful life: Change in A/cing Estimate (Prospective Effect)

Change in Historical Cost: Cost may undergo subsequent changes due to Exchange Rate fluctuations, Price Adjustments, Change in Duties, etc.
(Included in Cost of Asset – Prospective Effect)

Land & Buildings: Separable assets & accounted separately even when acquired together

Land: Whether Depreciable: No since Unlimited useful life
Exception: If Land has limited useful life.

Retirement: Asset retired from active use & held for disposal
Recorded at Lower of Carrying Amt. or NRV.
Expected loss to be immediately Recognised

Derecognition: On Disposal by sale/donation (OR) When no future benefits expected
Profit/Loss on it to be transferred to P&L A/c.

Question 1

Neon Enterprise operates a major chain of restaurants located in different cities. The company has acquired a new restaurant located at Chandigarh. The new-restaurant requires significant renovation expenditure. Management expects that the renovations will last for 3 months during which the restaurant will be closed. Management has prepared the following budget for this period –

Salaries of the staff engaged in preparation of restaurant before its opening Rs. 7,50,000
Construction and remodelling cost of restaurant Rs. 30,00,000

Explain the treatment of these expenditures as per provisions of AS 10 "Property, Plant and Equipment".

Solution

As per provisions of AS 10, any cost directly attributable to bring the assets to the location and conditions necessary for it to be capable of operating in the manner indicated by the management are called directly attributable costs and would be included in the costs of an item of PPE.

Management of Neon Enterprise should capitalize the costs of construction and remodelling the restaurant, because they are necessary to bring the restaurant to the condition necessary for it to be capable of operating in the manner intended by management. The restaurant cannot be opened without incurring the construction and remodelling expenditure amounting Rs. 30,00,000 and thus the expenditure should be considered part of the asset.

However, the cost of salaries of staff engaged in preparation of restaurant Rs. 7,50,000 before its opening are in the nature of operating expenditure that would be incurred if the restaurant was open and these costs are not necessary to bring the restaurant to the conditions necessary for it to be capable of operating in the manner intended by management. Hence, Rs. 7,50,000 should be expensed.

Question 2

ABC Ltd. is installing a new plant at its production factory. It provides you the following information:

Cost of the plant (cost per supplier's invoice plus taxes)	31,25,000
Estimated dismantling costs to be incurred after 5 years	2,50,000
Initial Operating losses before commercial production	3,75,000
Initial delivery and handling costs	1,85,000
Cost of site preparation	4,50,000
Consultants used for advice on the acquisition of the plant	6,50,000

Please advise ABC Ltd. on the costs that can be capitalised for plant in accordance with AS 10: Property, Plant and Equipment.

Solution

According to AS 10 on Property, Plant and Equipment, the costs which will be capitalized by ABC Ltd. are as follows:

Cost of the plant (cost per supplier's invoice plus taxes)	31,25,000
Estimated dismantling costs to be incurred after 5 years	2,50,000
Initial delivery and handling costs	1,85,000
Cost of site preparation	4,50,000
Consultants used for advice on the acquisition of the plant	6,50,000
	46,60,000

Note: Operating losses before commercial production amounting to Rs. 3,75,000 will not be capitalized as per AS 10. They should be written off to the Statement of Profit and Loss in the period they are incurred.

Question 3

Shrishti Ltd. contracted with a supplier to purchase machinery which is to be installed in its Department A in three months' time. Special foundations were required for the machinery which were to be prepared within this supply lead time. The cost of the site preparation and laying foundations were Rs. 1,41,870. These activities were supervised by a technician during the entire period, who is employed for this

purpose of Rs. 45,000 per month. The technician's services were given by Department B to Department A, which billed the services at Rs. 49,500 per month after adding 10% profit margin.

The machine was purchased at Rs. 1,58,34,000 inclusive of IGST @ 12% for which input credit is available to Shrishti Ltd. Rs. 55,770 transportation charges were incurred to bring the machine to the factory site. An Architect was appointed at a fee of Rs. 30,000 to supervise machinery installation at the factory site.

Ascertain the amount at which the Machinery should be capitalized under AS 10 considering that IGST credit is availed by the Shristhi Limited. Internally booked profits should be eliminated in arriving at the cost of machine.

Solution

Particulars		Amount
Purchase Price	Given (158,34,000 x 100/112)	1,41,37,500
Add: Site Preparation Cost	Given	1,41,870
Technician's Salary	Specific/Attributable overheads for 3 months (45,000 x3)	1,35,000
Initial Delivery Cost	Transportation	55,770
Professional Fees for Installation	Architect's Fees	30,000
Total Cost of Asset		**1,45,00,140**

Question 4

In the year 2019-20, an entity has acquired a new freehold building with a useful life of 25 years for Rs. 45,00,000. The entity desires to calculate the depreciation charge per annum using a straight line method. It has identified the following components (with no residual value of lifts & fixtures at the end of their useful life) as follows:

Component	Useful life (Years)	Cost
Land	Infinite	10,00,000
Roof	25	5,00,000
Lifts	10	2,50,000
Fixtures	5	2,50,000
Remainder of building	25	25,00,000
		45,00,000

(i) Calculate depreciation for the year 2019-20 as per componentization method.
(ii) Also state the treatment, in case Roof requires replacement at the end of its useful life.

Solution

(i) Statement showing amount of depreciation as per Componentization Method

Component	Depreciation = Cost / Useful life	Depreciation (p.a.)
Land	-	Nil
Roof	5,00,000/25	20,000
Lifts	2,50,000/10	25,000
Fixtures	2,50,000/5	50,000
Remainder of building	25,00,000/25	1,00,000
		1,95,000

(ii) When the roof requires replacement at the end of its useful life, the carrying amount will be Nil. The cost of replacing the roof should be recognised as a new component.

Question 5

B Ltd. owns an asset with an original cost of Rs. 2,00,000. On acquisition, management determined that the useful life was 10 years and the residual value would be Rs. 20,000. The asset is now 8 years old, and during this time there have been no revisions to the assessed residual value. At the end of year 8, management has reviewed the useful life and residual value and has determined that the useful life can be extended to 12 years in view of the maintenance program adopted by the company. As a result, the residual value will reduce to Rs. 10,000. How would the above changes in estimates be made by B Ltd.?

Solution

The above changes in estimates would be effected in the following manner:
The asset has a carrying amount of Rs. 56,000 at the end of year 8 [Rs. 2,00,000 – Rs. 1,44,000] i.e. Accumulated Depreciation.

Accumulated depreciation is calculated as

Depreciable amount {Cost less residual value} = Rs. 2,00,000 – Rs. 20,000 = Rs. 1,80,000.
Annual depreciation = Depreciable amount / Useful life = 1,80,000 / 10 = Rs. 18,000.
Accumulated depreciation = 18,000 × No. of years (8) = Rs. 1,44,000.
Revision of the useful life to 12 years results in a remaining useful life of 4 years (12 – 8).
The revised depreciable amount is Rs. 46,000. (56,000 – 10,000)
Thus, depreciation should be charged in future at Rs. 11,500 per annum (Rs. 46,000/4 years).