EKAGRATA

न भूतो न भविष्यति!

NEW SYLLABUS

CA INTERMEDIATE

PAPER 1

ADVANCED ACCOUNTING

self practice book

VOLUME 3

by CA CS ANSHUL AGRAWAL

EKAGRATA

न भूतो न भविष्यति!

CA – INTERMEDIATE (NEW SYLLABUS)

ADVANCED ACCOUNTING

Volume-III

By

CA. CS. Anshul Agrawal

Self - Practice Book

This study material contains the explanation of topic with blank spaces to write, unsolved questions from various resources of ICAI. This classbook is meant for those students who are doing their CA-Intermediate classes from CA CS Anshul Agrawal.

Typing, Formatting and Editing by CA. Anshul Agrawal

Published by

Copyright with

Study with

Volume-III 31st January 2024 Edition

Note from the Author

This Self-Practice Book is a wonderful compilation of questions on various topics from multiple sources of ICAI like ICAI's Revisionary Test Papers (RTPs), Mock Test Papers (MTPs), Previous Years Question Papers (PYQs) and Old Syllabus Study Material.

This book is made to compliment the studies of the students who are preparing for CA-Intermediate Exams. After attending classes and studying from my book's Volume-I and Volume-II, when students are well conversant with the various concept of the respective topic and they have practiced well all the questions covered in class, they can refer this book wherein they can find additional questions along with solutions for additional practice which will help them ace in CA Intermediate Exams.

Every possible care has been taken in preparing this booklet, yet it may contain some errors. Sincere apologies in advance for the same.

I wish you all Happy Reading – Happy Studying!!!

"Padhte Raho – Seekhte Raho – Age Badhte Raho
Kyunki
Padhna Band to Seekhna Band; aur
Seekhna Band to Aagey Badhna Band"

Anshul

From the Author...

Dear Students,

It gives me immense pleasure to share this masterpiece with you – which is an outcome of in-depth research, persistent hard work and innovation. This book is designed keeping in mind to simplify studies for the students making learning a fun filled experience. Further it is well synchronized with the study material issued by 'The Institute of Chartered Accountants of India', New Delhi, so that the students find it easy to refer and understand.

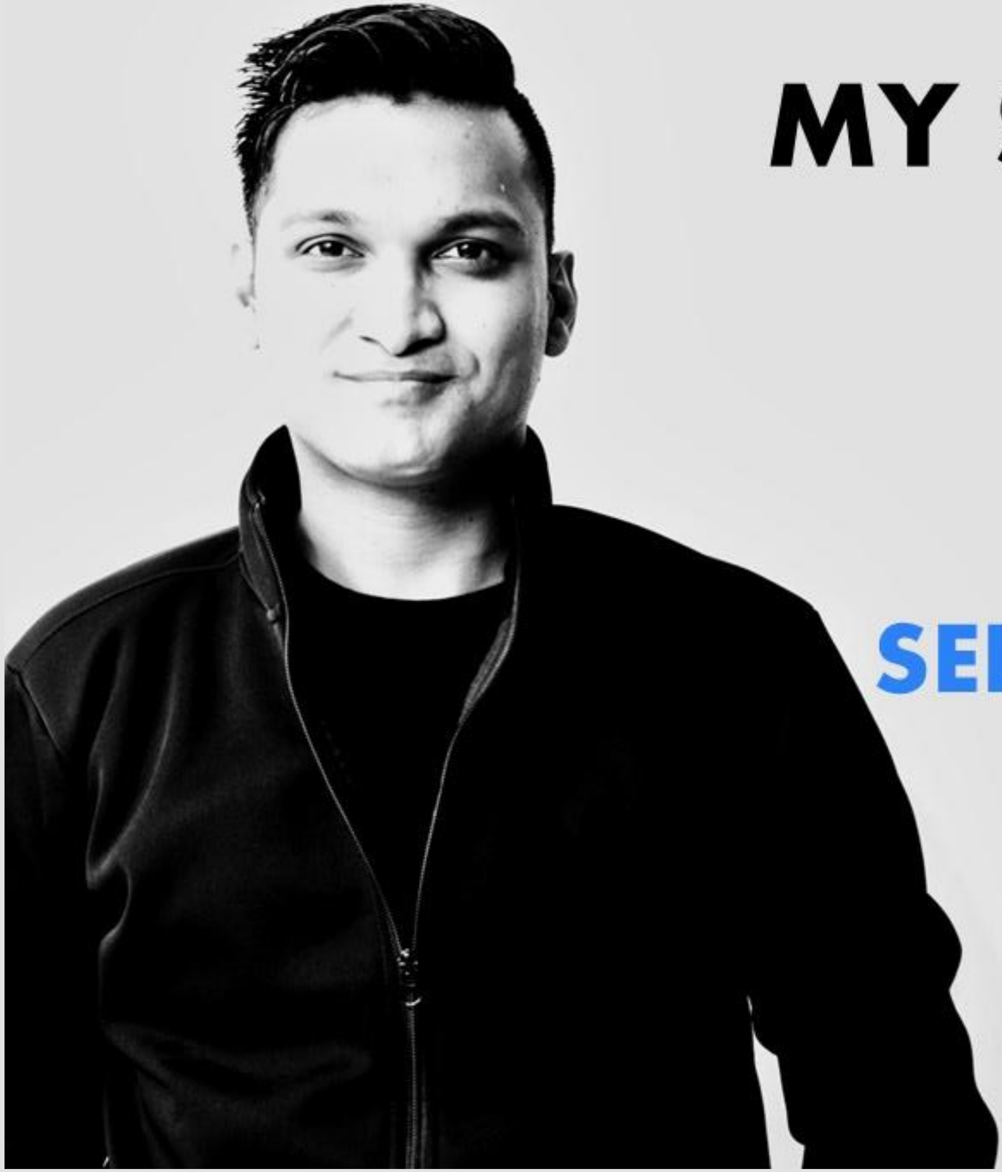
Firstly, I would like to welcome you all to the Intermediate Course and would like to wish you All the very Best for your journey of Intermediate Course. "ACCOUNTANCY" is the core subject for any Chartered Accountant, and therefore as a CA student, you are expected to gain in-depth knowledge about this subject. Accountancy is not just a subject, but it is a basic necessity of day-to-day life of every person – whether self employed or in employment. We have studied basics of accounting at CA-Foundation level and now at Intermediate level, we will understand advanced aspects of accounting, specially focusing on Company Accounts and Accounting Standards.

Firstly, thanks for believing in me and giving me an opportunity to guide you with this new subject. Lastly, I would like to just say that, now then when you have already decided to be with me, follow me whole-heartedly. I promise you that you study with me as I guide you and you will not only pass but will create wonders in exam.

As I always say,

"I am not Teaching you, rather We are doing SELF STUDIES"

Happy Learning Happy Studying



MY SUCCESS MANTRAS

PATIENCE धैर्य

विश्वास **TRUST**

SELF-RELIANCE आत्मनिर्भरता

CHAPTER – 1

CASH FLOW STATEMENTS

Q1. Basic – Classification of Activities (CA-Inter M18 5M) **REG. PAGE NO.**

Classify the following activities as - Operating Activities, Investing Activities or Financing activities and Cash Equivalents:

(1) Cash receipts from Trade Receivables
(2) Marketable Securities
(3) Purchase of investment
(4) Proceeds from long term borrowings
(5) Wages and Salaries paid
(6) Bank overdraft
(7) Purchase of Goodwill
(8) Interim dividend paid on equity shares
(9) Short term Deposits
(10) Underwriting commission paid

Solution:

(a) Operating Activities: Items 1 and 5.
(b) Investing Activities: Items 3,7 and 9
(c) Financing Activities: Items 4,6,8 and 10
(d) Cash Equivalent: 2

Q2. CF Full (Both Direct and Indirect Method) (CA-Inter M19 10M) **REG. PAGE NO.**

The following information was provided by PQR Ltd. for the year ended 31st March, 2019 :

(1) Gross Profit Ratio was 25% for the year, which amounts to Rs. 3,75,000.
(2) Company sold goods for cash only.
(3) Opening inventory was lesser than closing inventory by Rs. 25,000.
(4) Wages paid during the year Rs. 5,55,000.
(5) Office expenses paid during the year Rs. 35,000.
(6) Selling expenses paid during the year Rs. 15,000.
(7) Dividend paid during the year Rs. 40,000 (including dividend distribution tax).
(8) Bank Loan repaid during the year Rs. 2,05,000 (included interest Rs. 5,000)
(9) Trade Payables on 31st March, 2018 were Rs. 50,000 and on 31st March, 2019 were Rs. 35,000.
(10) Amount paid to Trade payables during the year Rs. 6,10,000
(11) Income Tax paid during the year amounts to Rs. 55,000 (Provision for taxation as on 31st March, 2019 Rs. 30,000)·
(12) Investments of Rs. 8,20,000 sold during the year at a profit of Rs. 20,000.
(13) Depreciation on furniture amounts to Rs. 40,000.
(14) Depreciation on other tangible assets amounts to Rs. 20,000.
(15) Plant and Machinery purchased on 15th November, 2018 for Rs. 3,50,000
(16) On 31st March, 2019 Rs. 2,00,000, 7% Debentures were issued at face value in an exchange for a plant.
(17) Cash and Cash equivalents on 31st March, 2018 Rs. 2,25,000.

(A) Prepare cash flow statement for the year ended 31st March, 2019, using direct method.
(B) Calculate cash flow from operating activities, using indirect method.

Solution:

(i) **PQR Ltd.**

Cash Flow Statement for the year ended 31st March, 2019
(Using direct method)

Particulars	Rs.	Rs.
Cash flows from Operating Activities:		
Cash sales (Rs. 3,75,000/25%)		15,00,000
Less: Cash payments for trade payables	(6,10,000)	
Wages Paid	(5,55,000)	
Office and selling expenses Rs. (35,000 + 15,000)	(50,000)	(12,15,000)
Cash generated from operations before taxes		2,85,000
Income tax paid		(55,000)

Net cash generated from operating activities (A)		2,30,000
Cash flows from Investing activities		
Sale of investments Rs. (8,20,000 + 20,000)	8,40,000	
Payments for purchase of Plant & machinery	(3,50,000)	
Net cash used in investing activities (B)		4,90,000
Cash flows from financing activities		
Bank loan repayment (including interest)	(2,05,000)	
Dividend paid (including dividend distribution tax)	(40,000)	
Net cash used in financing activities (C)		(2,45,000)
Net increase in cash (A+B+C)		4,75,000
Cash and cash equivalents at beginning of the period		2,25,000
Cash and cash equivalents at end of the period		7,00,000

(ii) **'Cash Flow from Operating Activities' by indirect method**

Net Profit for the year before tax and extraordinary items		2,80,000
Add: Non-Cash and Non-Operating Expenses:		
Depreciation		60,000
Interest Paid		5,000
Less: Non-Cash and Non-Operating Incomes:		
Profit on Sale of Investments		(20,000)
Net Profit after Adjustment for Non-Cash Items		3,25,000
Less: Decrease in trade payables	15,000	
Increase in inventory	25,000	(40,000)
Cash generated from operations before taxes		2,85,000

Working Note:

Calculation of net profit earned during the year

Gross profit		3,75,000
Less: Office expenses, selling expenses	50,000	
Depreciation	60,000	
Interest paid	5,000	(1,15,000)
		2,60,000
Add: Profit on sale of investments		20,000
Net profit before tax		2,80,000

Q3. Cash Flow from Investing Activity Only (CA-Inter N19 5M) **REG. PAGE NO.**

Prepare Cash Flow from Investing Activities as per AS-3 of M/s Shubham Creative Ltd. for the year ended 31st March 2019:

Machinery acquired by issue of shares at face value	Rs. 2,00,000
Claim received for loss of machinery in earthquake	Rs. 55,000
Unsecured loans given to associates	Rs. 5,00,000
Interest on Loans received from an associate company	Rs. 70,000
Pre-acquisition dividend received on investment made	Rs. 52,600
Debenture Interest Paid	Rs. 1,45,200
Term Loan Repaid	Rs. 4,50,000
Interest received on investment (TDS of Rs. 8,200 was deducted on the above interest)	Rs. 73,800
Purchased Debentures of X Ltd. on 1st December 2018, redeemable in 3 Months	Rs. 3,00,000
Book Value of Plant & Machinery sold (Loss incurred Rs. 9,600)	Rs. 90,000

Solution:

Cash Flow Statement from Investing Activities of
Subham Creative Limited for the year ended 31-03-2019

Cash generated from investing activities	**Rs.**	**Rs.**
Interest on loan received	70,000	
Pre-acquisition dividend received on investment made	52,600	
Unsecured loans given to subsidiaries	(5,00,000)	

Interest received on investments (gross value)	82,000	
TDS deducted on interest	(8,200)	
Sale of Plant & Machinery ` (90,000 – 9,600)	80,400	
Cash used in investing activities (before extra-ordinary item)		(2,23,200)
Extraordinary claim received for loss of machinery		55,000
Net cash used in investing activities (after extra-ordinary item)		(1,68,200)

Note:

1. Debenture interest paid and Term Loan repaid are financing activities and therefore not considered for preparing cash flow from investing activities.
2. Machinery acquired by issue of shares does not amount to cash outflow, hence also not considered in the above cash flow statement.
3. The investments made in debentures are for short-term, it will be treated as 'cash equivalent' and will not be considered as outflow in cash flow statement.

Q4. CF Full (Indirect Method) (CA-Inter N20 10M) **REG. PAGE NO.**

The following figures have been extracted from the books of Manan Jo Limited for the year ended on 31.3.2020. You are required to prepare the Cash Flow statement as per AS 3 using indirect method.

(i) Net profit before taking into account income tax and income from law suits but after taking into account the following items was Rs. 30 lakhs :

(a) Depreciation on Property, Plant & Equipment Rs. 7.50 lakhs.
(b) Discount on issue of Debentures written off Rs. 45,000.
(c) Interest on Debentures paid Rs. 5,25,000.
(d) Book value of investments Rs. 4.50 lakhs (Sale of Investments for Rs. 4,80,000).
(e) Interest received on investments Rs. 90,000.

(ii) Compensation received Rs.1,35,000 by the company in a suit filed.
(iii) Income tax paid during the year Rs. 15,75,000.
(iv) 22,500, 10% preference shares of Rs. 100 each were redeemed on 02-04-2019 at a premium of 5%.
(v) Further the company issued 75,000 equity shares of Rs.10 each at a premium of 20% on 30.3.2020 (Out of 75,000 equity shares, 25,000 equity shares were issued to a supplier of machinery)
(vi) Dividend for FY 2018-19 on preference shares were paid at the time of redemption.
(vii) Dividend on Equity shares paid on 31.01.2020 for the year 2018-2019 Rs. 7.50 lakhs (including dividend distribution tax) and interim dividend paid Rs. 2.50 lakhs for the year 2019-2020.
(viii) Land was purchased on 02.4.2019 for Rs.3,00,000 for which the company issued 22,000 equity shares of Rs. 10 each at a premium of 20% to the land owner and balance in cash as consideration.
(ix) Current assets and current liabilities in the beginning and at the end of the years were as detailed below:

	As on 01.04.2019 (Rs.)	As on 31.3.2020 (Rs.)
Inventory	18,00,000	19,77,000
Trade receivables	3,87,000	3,79,650
Cash in hand	3,94,450	16,950
Trade payables	3,16,500	3,16,950
Outstanding expenses	1,12,500	1,22,700

Solution:

Manan Ltd.
Cash Flow Statement
for the year ended 31st March, 2020

	Rs.	Rs.
Cash flow from Operating Activities		
Net profit before income tax and extraordinary items:		30,00,000
Adjustments for:		
Depreciation on Property, plant and equipment	7,50,000	
Discount on issue of debentures	45,000	
Interest on debentures paid	5,25,000	
Interest on investments received	(90,000)	
Profit on sale of investments	(30,000)	12,00,000

Operating profit before working capital changes		42,00,000
Adjustments for:		
Increase in inventory	(1,77,000)	
Decrease in trade receivable	7,350	
Increase in trade payables	450	
Increase in outstanding expenses	10,200	(1,59,000)
Cash generated from operations		40,41,000
Income tax paid		(15,75,000)
Cash flow from ordinary items		24,66,000
Cash flow from extraordinary items:		
Compensation received in a suit filed		1,35,000
Net cash flow from operating activities		26,01,000
Cash flow from Investing Activities;		
Sale proceeds of investments	4,80,000	
Interest received on investments	90,000	
Purchase of land (3,00,000 less 2,64,000)	(36,000)	
Net cash flow from investing activities		5,34,000
Cash flow from Financing Activities		
Proceeds of issue of equity shares at 20% premium	6,00,000	
Redemption of preference shares at 5% premium	(23,62,500)	
Preference dividend paid	(2,25,000)	
Interest on debentures paid	(5,25,000)	
Dividend paid (7,50,000 + 2,50,000)	(10,00,000)	
Net cash used in financing activities		(35,12,500)
Net decrease in cash and cash equivalents during the year		(3,77,500)
Add: Cash and cash equivalents as on 31.3.2019		3,94,450
Cash and cash equivalents as on 31.3.2020		16,950

Q5. CF Full (Indirect Method) (CA-Inter New Jan 21 12M) **REG. PAGE NO.**

Following information was extracted from the books of S Ltd. for the year ended 31st March,2020 :

(1) Net profit before taking into account income tax and after taking into account the following items was Rs.30 lakhs;

(i) Depreciation on Property, Plant & Equipment Rs.7,00,000

(ii) Discount on issue of debentures written off Rs.45,000.

(iii) Interest on debentures paid Rs.4,35,000

(iv) Investment of Book value Rs.3,50,000 sold for Rs.3,75,000.

(v) Interest received on Investments Rs.70,000

(2) Income tax paid during the year Rs. 12,80,000

(3) Company issued 60,000 Equity Shares of Rs.10 each at a premium of 20% on 10th April,2019.

(4) 20,000,9% Preference Shares of Rs.100 each were redeemed on 31st March, 2020 at a premium of 5%

(5) Dividend paid during the year amounted to Rs.11 Lakhs (including dividend distribution tax)

(6) A new Plant costing Rs.7 Lakhs was purchased in part exchange of an old plant on 1st January,2020. The book value of the old plant was Rs.8 Lakhs but the vendor took over the old plant at a value of Rs.6 Lakhs only. The balance amount was paid to vendor through cheque on 30th March,2020.

(7) Company decided to value inventory at cost, whereas previously the practice was to value inventory at cost less 10%. The inventory according to books on 31.03.2020 was Rs. 14,76,000.

The inventory on 31.03.2019 was correctly valued at Rs. 13,50,000.

(8) Current Assets and Current Liabilities in the beginning and at the end of year 2019-2020 were as:

	01.04.2019 (Rs.)	31.3.2020 (Rs.)
Inventory	13,50,000	14,76,000
Trade receivables	3,27,000	3,13,200
Cash in hand	2,40,700	3,70,500
Trade payables	2,84,700	2,87,300
Outstanding expenses	97,000	1,01,400

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

Solution:

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

	Rs.	Rs.
Cash flows from operating activities		
Net profit before taxation*		30,00,000
Adjustments for:		
Depreciation on PPE	7,00,000	
Discount on debentures	45,000	
Profit on sale of investments	(25,000)	
Interest income on investments	(70,000)	
Interest on debentures	4,35,000	
Stock adjustment {14,76,000 less 16,40,000(14,76,000/90X100)}	1,64,000	
Operating profit before working capital changes		12,49,000
Changes in working capital (Excluding cash and bank balance):		42,49,000
Less: Increase in inventory {16,40,000(14,76,000/90X100) less 13,50,000}	(2,90,000)	
Add: Decrease in Trade receivables	13,800	
Increase in trade payables	2,600	
Increase in o/s expenses	4,400	(2,69,200)
Cash generated from operations		39,79,800
Less: Income taxes paid		(12,80,000)
Net cash generated from operating activities		26,99,800
Cash flows from investing activities		
Sale of investments	3,75,000	
Interest received	70,000	
Payments for purchase of fixed assets (7,00,000 – 6,00,000)	(1,00,000)	
Net cash used in investing activities		3,45,000
Cash flows from financing activities		
Redemption of Preference shares	(21,00,000)	
Issue of shares	7,20,000	
Interest paid	(4,35,000)	
Dividend paid	(11,00,000)	
Net cash used in financing activities		(29,15,000)
Net increase in cash		1,29,800
Cash at beginning of the period		2,40,700
Cash at end of the period		3,70,500

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

Q6. CF Full (Direct Method) (CA-Inter July 21 5M) **REG. PAGE NO.**

Prepare cash flow statement of Gama Limited for the year ended 31st March, 2021 in accordance with AS-3(Revised) from the following cash account summary:

Cash summary Account

Inflows	**Rs. ('000)**	**Outflows**	**Rs. ('000)**
Opening Balance	945	Payment to suppliers	54,918
Receipts from Customers	74,682	Purchase of Investments	351
Sale of Investments (Cost Rs.4,05,000)	459	Property, plant and equipment acquired	6,210
Issue of Shares	8,100	Wages and salaries	1,863
Sale of Property, Plant and equipment	3,456	Payment of overheads	3,105
		Taxation	6,561

		Dividends	2,160
		Repayment of Bank Overdraft	6,750
		Interest paid on Bank Overdraft	1,350
		Closing Balance	4,374
	87,642		87,642

Solution:

Gama Limited
Cash Flow Statement
For the Year Ended 31st March 2021

Particulars	**Amount (Rs. '000)**	**Amount (Rs. '000)**
Cash flow from Operating Activities:		
Cash receipts from customers	74,682	
Cash payments to suppliers	(54,918)	
Cash payments for wages & salaries	(1,863)	
Cash payments of overheads	(3,105)	
Cash Generated from Operations	14,796	
Payment of Taxation	(6,561)	
Net Cash from Operating Activities		8,235
Cash Flow from Investing Activities:		
Proceeds from sale of investments	459	
Proceeds from sale of Property, Plant and Equipment	3,456	
Purchase of Investments	(351)	
Purchase of Property, Plant and Equipment	(6,210)	
Net Cash Used in Investing Activities		(2,646)
Cash Flow from Financing Activities:		
Proceeds from issue of shares	8,100	
Payment of Dividend	(2,160)	
Repayment of Bank Overdraft	(6,750)	
Interest paid on Bank Overdraft	(1,350)	
Net Cash Used in Financing Activities		(2,160)
Net Increase in Cash & Cash Equivalent		3,429
Cash and Cash Equivalent in the Beginning of the year		945
Cash and Cash Equivalent in the end of the year		4374

Q7. Basic – Classification of Activities (CA-Inter D21 5M) **REG. PAGE NO.**

Following are the extracts from the Balance Sheet of ABC Ltd.

Liabilities	**31.3.2020 (Rs.)**	**31.3.2021 (Rs.)**
Equity Share Capital	25,00,000	35,60,000
10% Preference Share Capital	7,00,000	6,00,000
Securities Premium Account	5,00,000	5,50,000
Profit & Loss A/c	20,00,000	28,00,000

Equity Share Capital for the year ended 31st March, 2021 includes Rs. 60,000 of equity shares issued to Grey Ltd. at par for supply of Machinery of Rs. 60,000. Profit & Loss account on 31st March, 2021 includes Rs. 50,000 of dividend received on Equity shares invested in X Ltd.

Show how the related items will appear in the Cash Flow Statement of ABC Ltd. as per AS-3 (Revised)

Solution:

The related items given in the question will appear in the Cash Flow Statement of ABC Limited for the year ended 31st March, 2021 as follows:

	Rs.	**Rs.**
Cash flows from operating activities		

Closing Balance as per Profit and Loss Account		28,00,000	
Less: Opening Balance as per Profit and Loss Account		(20,00,000)	
		8,00,000	
Less: Dividend received		50,000	
			7,50,000
Cash flows from investing activities			
Dividend received			50,000
Cash flows from financing activities			
Proceeds from issuance of share capital			
Equity shares issued for cash	Rs. 10,00,000		
Proceeds from securities premium (Rs. 5,50,000 – 5,00,000)	Rs. 50,000		
		10,50,000	
Less: Redemption of Preference shares (Rs. 7,00,000 – Rs. 6,00,000)		(1,00,000)	9,50,000

Note:
1. Machinery acquired by issue of shares does not amount to cash outflow, hence also not considered in the cash flow statement.
2. ABC Ltd. has been considered as a non-financial company in the given answer.

Q8. CF from operating activities (Indirect Method) (CA-Inter M22 5M) REG. PAGE NO.

The following information is provided by Alpha Limited, for the year ended 31st March, 2022:
(i) Net profit before taking into account income tax and income from law suits but after taking into account the following items was Rs. 40 lakhs.
(ii) Depreciation on Fixed Assets Rs. 10 lakhs.
(iii) Discount on issue of Debentures written of Rs. 60,000.
(iv) Interest on Debentures paid Rs. 7,00,000.
(v) Book value of investments Rs. 6 lakhs (Sale of Investments for Rs. 6,40,000)
(vi) Interest received on investments Rs. 1,20,000.
(vii) Compensation received Rs. 1,80,000 by the company in a suit filed.
(viii) Income tax paid Rs. 21,00,000
(ix) Current assets and current liabilities in the beginning and at the end of the year were as detailed below:

	As on 31.3.2021 (Rs.)	As on 31.3.2022 (Rs.)
Stock	24,00,000	26,36,000
Sundry Debtors	4,16,000	4,26,200
Cash in hand	3,92,600	70,600
Bills Receivable	1,00,000	80,000
Bills Payable	90,000	80,000
Sundry Creditors	3,32,000	3,42,600
Outstanding expenses	1,50,000	1,63,600

You are required to prepare Cash Flow Statement from Operating Activities in accordance with AS-3 (revised) using the indirect method for the year ended 31st March,2022.

Solution:

Alpha Ltd.
Cash Flow Statement (from Operating Activities)
for the year ended 31st March, 2022

	Rs.	Rs.
Cash flow from Operating Activities		
Net profit before income tax and extraordinary items:		40,00,000
Adjustments for:		
Depreciation on Property, plant and equipment	10,00,000	
Discount on issue of debentures	60,000	
Interest on debentures paid	7,00,000	
Interest on investments received	(1,20,000)	

Profit on sale of investments	(40,000)	16,00,000
Operating profit before working capital changes		56,00,000
Adjustments for:		
Increase in inventory	(2,36,000)	
Increase in Sundry Debtors	(10,200)	
Decrease in Bills receivables	20,000	
Increase in Sundry Creditors	10,600	
Increase in Bills payables	(10,000)	
Increase in outstanding expenses	13,600	(2,12,000)
Cash generated from operations		53,88,000
Income tax paid		(21,00,000)
Cash flow from ordinary items		32,88,000
Cash flow from extraordinary items:		
Compensation received in a suit filed		1,80,000
Net cash flow from operating activities		34,68,000

Q9. Basic – Classification of Activities (CA-Inter N22 5M) REG. PAGE NO.

Ridgeway Limited, a Non-Financial company has the following activities:
(i) Dividend paid for the year.
(ii) TDS on interest income earned on investments made.
(iii) Loans and advances given to suppliers and interest earned from them.
(iv) Deposit with bank for a term of two years.
(v) Highly liquid Marketable Securities (without risk of change in value).
(vi) Investments made and dividends earned on them.
(vii) Insurance claims received against loss of stock or loss of profits
(viii) Loans and advances given to subsidiaries and interest earned from them.
(ix) Issue of Bonus Shares.
(x) Term loan repaid.
You are required to classify the above activities in Cash Flow Statement as per 'AS-3'.

Solution:

No.		Activities
(i)	Dividend paid for the year	Financing
(ii)	TDS on interest income earned on investments made	Investing
(iii)	Loans and advances given to suppliers and interest earned from them	Operating
(iv)	Deposit with bank for a term of two years	Investing
(v)	Highly liquid Marketable Securities (without risk of change in value)	Cash Equivalent
(vi)	Investments made and dividends earned on them	Investing
(vii)	Insurance claims received against loss of stock or loss of profits	Operating
(viii)	Loans and advances given to subsidiaries and interest earned from them	Investing
(ix)	Issue of Bonus Shares	No Cash Inflow/ outflow
(x)	Term Loan repaid	Financing

Q10. CF Full (Direct Method) (RTP May 2018,RTP Nov 21, RTP Nov 23) REG. PAGE NO.

A company provides you the following information:
(i) Total sales for the year were Rs. 398 crores out of which cash sales amounted to Rs. 262 crores.
(ii) Receipts from credit customers during the year, aggregated Rs. 134 crores.
(iii) Purchases for the year amounted to Rs. 220 crores out of which credit purchase was 80%.

Balance in creditors as on
1.4.2016 Rs. 84 crores
31.3.2017 Rs. 92 crores

(iv) Suppliers of other consumables and services were paid Rs. 19 crores in cash.
(v) Employees of the enterprises were paid 20 crores in cash.
(vi) Fully paid preference shares of the face value of Rs. 32 crores were redeemed. Equity shares of the face value of Rs. 20 crores were allotted as fully paid up at premium of 20%.

(vii) Debentures of Rs. 20 crores at a premium of 10% were redeemed. Debenture holders were issued equity shares in lieu of their debentures.
(viii) Rs. 26 crores were paid by way of income tax.
(ix) A new machinery costing Rs. 25 crores was purchased in part exchange of an old machinery. The book value of the old machinery was Rs. 13 crores. Through the negotiations, the vendor agreed to take over the old machinery at a higher value of Rs. 15 crores. The balance was paid in cash to the vendor.
(x) Investment costing Rs. 18 cores were sold at a loss of Rs. 2 crores.
(xi) Dividends amounting Rs. 15 crores (including dividend distribution tax of Rs. 2.7 crores) was also paid.
(xii) Debenture interest amounting Rs. 2 crore was paid.
(xiii) On 31st March 2016, Balance with Bank and Cash on hand was Rs. 2 crores.
On the basis of the above information, you are required to prepare a Cash Flow Statement for the year ended 31st March, 2017 (Using direct method)

Solution:

Cash flow statement (using direct method) for the year ended 31st March, 2017

		(Rs. in crores)
Cash flow from operating activities		
Cash sales	262	
Cash collected from credit customers	134	
Less: Cash paid to suppliers for goods & services and to employees (Refer Working Note)	(251)	
Cash from operations	145	
Less: Income tax paid	(26)	
Net cash generated from operating activities		119
Cash flow from investing activities		
Net Payment for purchase of Machine (25 – 15)	(10)	
Proceeds from sale of investments	16	
Net cash used in investing activities		6
Cash flow from financing activities		
Redemption of Preference shares	(32)	
Proceeds from issue of Equity shares	24	
Debenture interest paid	(2)	
Dividend Paid	(15)	
Net cash used in financing activities		(25)
Net increase in cash and cash equivalents		100
Add: Cash and cash equivalents as on 1.04.2016		2
Cash and cash equivalents as on 31.3.2017		102

Working Note:

Calculation of cash paid to suppliers of goods and services and to employees

	Rs. in crores
Opening Balance in creditors Account	84
Add: Purchases (220x .8)	176
Total	260
Less: Closing balance in Creditors Account	92
Cash paid to suppliers of goods	168
Add: Cash purchases (220x .2)	44
Total cash paid for purchases to suppliers (a)	212
Add: Cash paid to suppliers of other consumables and services (b)	19
Add: Payment to employees (c)	20
Total cash paid to suppliers of goods & services and to employees [(a)+ (b) + (c)]	251

Q11. CF Full (Indirect Method) (RTP Nov 2018) (Similar RTP Nov 2022) REG. PAGE NO.

The Balance Sheet of Harry Ltd. for the year ending 31st March, 2018 and 31st March, 2017 were summarised as follows:

	2018 (Rs.)	**2017 (Rs.)**
Equity share capital	1,20,000	1,00,000

Reserves:		
Profit and Loss Account	9,000	8,000
Current Liabilities:		
Trade Payables	8,000	5,000
Income tax payable	3,000	2,000
Declared Dividends	4,000	2,000
	1,44,000	**1,17,000**
Fixed Assets (at W.D.V) :		
Building	19,000	20,000
Furniture & Fixture	34,000	22,000
Cars	25,000	16,000
Long Term Investments	32,000	28,000
Current Assets:		
Inventory	14,000	8,000
Trade Receivables	8,000	6,000
Cash & Bank	12,000	17,000
	1,44,000	**1,17,000**

The Profit and Loss account for the year ended 31st March, 2018 disclosed:

	Rs.
Profit before tax	8,000
Income Tax	(3,000)
Profit after tax	5,000
Declared Dividends	(4,000)
Retained Profit	1,000

Further Information is available:
1. Depreciation on Building Rs. 1,000.
2. Depreciation on Furniture & Fixtures for the year Rs. 2,000.
3. Depreciation on Cars for the year Rs. 5,000. One car was disposed during the year for Rs. 3,400 whose written down value was Rs. 2,000.
4. Purchase investments for Rs. 6,000.
5. Sold investments for Rs. 10,000, these investments cost Rs. 2,000.

You are required to prepare Cash Flow Statement as per AS-3 (revised) using indirect method.

Solution:

Harry Ltd.
Cash Flow Statement
for the year ended 31st March, 2018

	Rs.	**Rs.**
Cash flows from operating activities		
Net Profit before taxation	8,000	
Adjustments for:		
Depreciation (1,000 + 2,000 +5,000)	8,000	
Profit on sale of Investment	(8,000)	
Profit on sale of car	(1,400)	
Operating profit before working capital changes	6,600	
Increase in Trade receivables	(2,000)	
Increase in inventories	(6,000)	
Increase in Trade payables	3,000	
Cash generated from operations	1,600	
Income taxes paid	(2,000)	
Net cash generated from operating activities (A)		(400)
Cash flows from investing activities		
Sale of car	3,400	
Purchase of car	(16,000)	
Sale of Investment	10,000	
Purchase of Investment	(6,000)	

Purchase of Furniture & fixtures	(14,000)	
Net cash used in investing activities (B)		(22,600)
Cash flows from financing activities		
Issue of shares for cash	20,000	
Dividends paid*	(2,000)	
Net cash from financing activities(C)		18,000
Net decrease in cash and cash equivalents (A + B +C)		(5,000)
Cash and cash equivalents at beginning of period		17,000
Cash and cash equivalents at end of period		12,000

* Dividend declared for the year ended 31st March, 2017 amounting ` 2,000 must have been paid in the year 2017-18. Hence, it has been considered as cash outflow for preparation of cash flow statement of 2017-18.

Working Notes:

1. Calculation of Income taxes paid

Income tax expense for the year	3,000
Add: Income tax liability at the beginning of the year	2,000
	5,000
Less: Income tax liability at the end of the year	(3,000)
	2,000

2. Calculation of Fixed assets acquisitions

	Furniture & Fixtures (Rs.)	**Car (Rs.)**
W.D.V. at 31.3.2018	34,000	25,000
Add back: Depreciation for the year	2,000	5,000
Disposals	—	2,000
	36,000	32,000
Less: W.D.V. at 31. 3. 2017	(22,000)	(16,000)
Acquisitions during 2016-2018	14,000	16,000

Q12. CF Full (Indirect Method) (RTP May 2019) **REG. PAGE NO.**

Preet Ltd. presents you the following information for the year ended 31 st March, 2019:

		(Rs. in lacs)
(i)	Net profit before tax provision	72,000
(ii)	Dividend paid	20,404
(iii)	Income-tax paid	10,200
(iv)	Book value of assets sold	444
	Loss on sale of asset	96
(v)	Depreciation debited to P & L account	48,000
(vi)	Capital grant received - amortized to P & L A/c	20
(vii)	Book value of investment sold	66,636
	Profit on sale of investment	240
(viii)	Interest income from investment credited to P & L A/c	6,000
(ix)	Interest expenditure debited to P & L A/c	24,000
(x)	Interest actually paid (Financing activity)	26,084
(xi)	Increase in working capital [Excluding cash and bank balance]	1,34,580
(xii)	Purchase of fixed assets	44,184
(xiii)	Expenditure on construction work	83,376
(xiv)	Grant received for capital projects	36
(xv)	Long term borrowings from banks	1,11,732
(xvi)	Provision for Income-tax debited to P & L A/c	12,000
	Cash and bank balance on 1.4.2018	12,000
	Cash and bank balance on 31.3.2019	16,000

You are required to prepare a cash flow statement as per AS-3 (Revised).

Solution:

Cash Flow Statement as per AS 3		Rs. in lacs
Cash flows from operating activities:		
Net profit before tax provision		72,000
Add: Non cash expenditures:		
Depreciation	48,000	
Loss on sale of assets	96	
Interest expenditure (non-operating activity)	24,000	72,096
		1,44,096
Less: Non cash income		
Amortisation of capital grant received	(20)	
Profit on sale of investments (non-operating income)	(240)	
Interest income from investments (non-operating income)	(6,000)	6,260
Operating profit		1,37,836
Less: Increase in working capital		(1,34,580)
Cash from operations		3,256
Less: Income tax paid		(10,200)
Net cash generated from operating activities		(6,944)
Cash flows from investing activities:		
Sale of assets (444 – 96)	348	
Sale of investments (66,636+240)	66,876	
Interest income from investments	6,000	
Purchase of fixed assets	(44,184)	
Expenditure on construction work	(83,376)	
Net cash used in investing activities		(54,336)
Cash flows from financing activities:		
Grants for capital projects	36	
Long term borrowings	1,11,732	
Interest paid	(26,084)	
Dividend paid	(20,404)	
Net cash from financing activities		65,280
Net increase in cash		4,000
Add: Cash and bank balance as on 1.4.2018		12,000
Cash and bank balance as on 31.3.2019		16,000

Q13. CF Full (Indirect Method) (RTP Nov 2019) REG. PAGE NO.

From the following information, prepare a Cash Flow Statement for the year ended 31st March, 2019.

BALANCE SHEET

PARTICULARS	NOTE REF.	31.03.2019 (Rs.)	31.03.2018 (Rs.)
I. EQUITY & LIABILITIES			
1. Shareholder's Funds			
(A) Share Capital	1	3,50,000	3,00,000
(B) Reserves & Suplus	2	82,000	38,000
2. Non Current Liabilities			
3. Current Liabilities			
Trade Payables		65,000	44,000
Other Current Liabilities	3	37,000	27,000
Short term provisons (provision for tax)		32,000	28,000
TOTAL		**5,66,000**	**4,37,000**
II. ASSETS			
1. Non-Current Assets			
Tangible Assets	4	2,66,000	1,90,000
Intangible Assets (Goodwill)		47,000	60,000
Non Current Investments		35,000	10,000
2. Current Assets			
Inventories		78,000	85,000

Trade Receivables	1,08,000	75,000
Cash & Cash Equivalents	32,000	17,000
TOTAL	**5,66,000**	**4,37,000**

Note 1: Share Capital

Particulars	**31.03.2019 (Rs.)**	**31.03.2018 (Rs.)**
Equity Share Capital	2,50,000	1,50,000
8% Preference Share Capital	1,00,000	1,50,000
	3,50,000	3,00,000

Note 2: Reserves and Surplus

Particulars	**31.03.2019 (Rs.)**	**31.03.2018 (Rs.)**
General Reserve	30,000	20,000
Profit and Loss A/c	27,000	18,000
Capital Reserve	25,000	
	82,000	38,000

Note 3: Current Liabilities

Particulars	**31.03.2019 (Rs.)**	**31.03.2018 (Rs.)**
Dividend declared	37,000	27,000
	37,000	27,000

Note 4: Tangible Assets

Particulars	**31.03.2019 (Rs.)**	**31.03.2018 (Rs.)**
Land & Building	75,000	1,00,000
Machinery	1,91,000	90,000
	2,66,000	1,90,000

Additional Information:

(i) Rs. 18,000 depreciation for the year has been written off on plant and machinery and no depreciation has been charged on Land and Building.

(ii) A piece of land has been sold out for Rs. 50,000 and the balance has been revalued, profit on such sale and revaluation being transferred to capital reserve. There is no other entry in Capital Reserve Account.

(iii) A plant was sold for Rs. 12,000 WDV being Rs. 15,000 on the date of sale (after charging depreciation).

(iv) Dividend received amounted to Rs. 2,100 which included pre-acquisition dividend of Rs. 600.

(v) An interim dividend of Rs. 10,000 including Dividend Distribution Tax has been paid.

(vi) Non-current investments given in the balance sheet represents investment in shares of other companies.

(vii) Amount of provision for tax existing on 31.3.2018 was paid during the year 2018-19.

Solution:

Cash flow Statement for the year ending 31st March, 2019

		Particulars	**Rs.**	**Rs.**
1		Cash Flow from Operating Activities		
	A.	Closing balance as per Profit and Loss Account		27,000
		Less: Opening balance as per Profit and Loss Account		(18,000)
		Add: Dividend declared during the year		37,000
		Add: Interim dividend paid during the year		10,000
		Add: Transfer to reserve		10,000
		Add: Provision for Tax		32,000
	B.	Net profit before taxation, and extra-ordinary item		98,000
	C.	Add: Items to be added		
		Depreciation	18,000	
		Loss on sale of Plant	3,000	
		Goodwill written off	13,000	34,000
	D.	Less: Dividend Income		(1,500)
	E.	Operating profit before working capital changes [B + C - D]		1,30,500
	F.	Add: Decrease in Current Assets and Increase in Current Liabilities		
		Decrease in Inventories	7,000	

		Increase in Trade Payables	21,000	28,000
	G.	Less: Increase in Trade Receivables		(33,000)
	H	Cash generated from operations (E+F-G)		1,25,500
	I	Less: Income taxes paid		(28,000)
	J	Net Cash from (used in) operating activities		97,500
II.		Cash Flows from investing activities:		
		Purchase of Plant		(1,34,000)
		Sale of Land		50,000
		Sale of plant		12,000
		Purchase of investments		(25,600)
		Dividend Received		2,100
		Net cash used in investing activities		(95,500)
III.		Cash Flows from Financing Activities:		
		Proceeds from issue of equity share capital		1,00,000
		Redemption of preference shares		(50,000)
		Interim Dividend (inclusive of DDT) paid		(10,000)
		Final dividend (inclusive of DDT) paid		(27,000)
		Net cash from financing activities		13,000
IV.		Net increase in cash and cash equivalents (I+II+III)		15,000
V.		Cash and cash equivalents at beginning of period		17,000
VI.		Cash and cash equivalents at end of period (IV+V)		32,000

Working Notes:

1. Land and Building Account

Particulars	Rs.	Particulars	Rs.
To Balance b/d	1,00,000	By Bank A/c (Sale)	50,000
To Capital Reserve A/c (Profit on sale/revaluation)	25,000	By Balance c/d	75,000
	1,25,000		**1,25,000**

2. Plant and machinery Account

Particulars	Rs.	Particulars	Rs.
To Balance b/d	90,000	By Depreciation A/c	18,000
To Bank A/c (Purchase)	1,34,000	By Bank A/c (sale)	12,000
		By Profit and Loss A/c (Loss on sale)	3,000
		By balance c/d	1,91,000
	2,24,000		**2,24,000**

3. Investments Account

Particulars	Rs.	Particulars	Rs.
To Balance b/d	10,000	By Bank A/c (Dividend Received)	600
To Bank A/c (Purchase)	25,600	By Balance c/d	35,000
	35,600		**35,600**

Q14. CF Full (Indirect Method) (RTP May 2020) **REG. PAGE NO.**

The following figures have been extracted from the books of X Limited for the year ended on 31.3.2019. You are required to prepare a cash flow statement as per AS 3 using indirect method.

(i) Net profit before taking into account income tax and income from law suits but after taking into account the following items was Rs. 20 lakhs:

(a) Depreciation on Property, Plant & Equipment Rs. 5 lakhs.

(b) Discount on issue of Debentures written off Rs. 30,000.

(c) Interest on Debentures paid Rs. 3,50,000.

(d) Book value of investments Rs. 3 lakhs (Sale of Investments for Rs. 3,20,000).

(e) Interest received on investments Rs. 60,000.

(f) Compensation received Rs. 90,000 by the company in a suit filed.

(ii) Income tax paid during the year Rs. 10,50,000.

(iii) 15,000, 10% preference shares of Rs. 100 each were redeemed on 31.3.2019 at a premium of 5%. Further the company issued 50,000 equity shares of Rs. 10 each at a premium of 20% on 2.4.2018. Dividend on preference shares were paid at the time of redemption.

(iv) Dividend paid for the year 2017-2018 Rs. 5 lakhs and interim dividend paid Rs. 3 lakhs for the year 2018-2019.

(v) Land was purchased on 2.4.2018 for Rs. 2,40,000 for which the company issued 20,000 equity shares of Rs. 10 each at a premium of 20% to the land owner as consideration.

(vi) Current assets and current liabilities in the beginning and at the end of the years were as detailed below:

	As on 31.3.2018 (Rs.)	**As on 31.3.2019 (Rs.)**
Inventory	12,00,000	13,18,000
Trade receivables	2,58,000	2,53,100
Cash in hand	1,96,300	35,300
Trade payables	2,11,000	2,11,300
Outstanding expenses	75,000	81,800

Solution:

X Ltd.
Cash Flow Statement
for the year ended 31st March, 2019

Particulars	**Rs.**	**Rs.**
Cash flow from Operating Activities		
Net profit before income tax and extraordinary items:		20,00,000
Adjustments for:		
Depreciation on PPE	5,00,000	
Discount on issue of debentures	30,000	
Interest on debentures paid	3,50,000	
Interest on investments received	(60,000)	
Profit on sale of investments	(20,000)	8,00,000
Operating profit before working capital changes		28,00,000
Adjustments for:		
Increase in inventory	(1,18,000)	
Decrease in trade receivable	4,900	
Increase in trade payables	300	
Increase in outstanding expenses	6,800	(1,06,000)
Cash generated from operations		26,94,000
Income tax paid		(10,50,000)
		16,44,000
Cash flow from extraordinary items:		
Compensation received in a suit filed		90,000
Net cash flow from operating activities		17,34,000
Cash flow from Investing Activities		
Sale proceeds of investments	3,20,000	
Interest received on investments	60,000	
Net cash flow from investing activities		3,80,000
Cash flow from Financing Activities		
Proceeds by issue of equity shares at 20% premium	6,00,000	
Redemption of preference shares at 5% premium	(15,75,000)	
Preference dividend paid	(1,50,000)	
Interest on debentures paid	(3,50,000)	
Dividend paid (5,00,000 + 3,00,000)	(8,00,000)	
Net cash used in financing activities		(22,75,000)
Net decrease in cash and cash equivalents during the year		(1,61,000)
Add: Cash and cash equivalents as on 31.3.2018		1,96,300
Cash and cash equivalents as on 31.3.2019		35,300

Note: Purchase of land in exchange of equity shares (issued at 20% premium) has not been considered in the cash flow statement as it does not involve any cash transaction.

Q15. CF Full (Direct Method) (RTP Nov 2020) **REG. PAGE NO.**

Prepare Cash Flow Statement of Light Ltd. for the year ended 31st March, 2020, in accordance with AS 3 (Revised) from the following Summary Cash Account:

Summary Cash Account

		(Rs. in '000)
Balance as on 01.04.2019		315
Receipts from Customers		24,894
Sale of Investments (Cost Rs. 1,35,000)		153
Issue of Shares		2,700
Sale of Fixed Assets		1,152
		29,214
Payment to Suppliers	18,306	
Purchase of Investments	117	
Purchase of Fixed Assets	2,070	
Wages & Salaries	621	
Selling & Administration Expenses	1,035	
Payment of Income Tax	2,187	
Payment of Dividends	720	
Repayment of Bank Loan	2,250	
Interest paid on Bank Loan	450	(27,756)
Balance as on 31.03.2020		1,458

Solution:

Cash Flow Statement of Light Ltd. for the year ended 31st March, 2020

		(Rs. in '000)
Cash flows from operating activities		
Cash receipts from customers	24,894	
Cash payments to suppliers	(18,306)	
Cash paid to employees	(621)	
Other cash payments (for Selling & Administrative expenses)	(1,035)	
Cash generated from operations	4,932	
Income taxes paid	(2,187)	
Net cash from operating activities		2,745
Cash flows from investing activities		
Payments for purchase of fixed asset	(2,070)	
Proceeds from sale of fixed assets	1,152	
Purchase of investments	(117)	
Sale of investments	153	
Net cash used in investing activities		(882)
Cash flows from financing activities		
Proceeds from issuance of share capital	2,700	
Bank loan repaid	(2,250)	
Interest paid on bank loan	(450)	
Dividend paid	(720)	
Net cash used in financing activities		(720)
Net increase in cash and cash equivalents		1,143
Cash and cash equivalents at beginning of period		315
Cash and cash equivalents at end of period		1,458

Q16. CF Full (Direct Method) (RTP May 2021) **REG. PAGE NO.**

The following are the extracts of Balance Sheet and Statement of Profit and Loss of Supriya Ltd.

(Rs. in '000)

Extract of Balance Sheet

PARTICULARS	NOTE REF.	2021	2020
I. EQUITY & LIABILITIES			
1. Shareholder's Funds			
Share Capital	1	500	200
2. Non Current Liabilities			
Long term loan from bank			250
3. Current Liabilities			
Trade Payables		1,000	3,047
II. ASSETS			
1. Non-Current Assets			
Property, Plant and Equipment		230	128
2. Current Assets			
Trade Receivables		2,000	4,783
Cash & Cash Equivalents		212	35

Extract of Statement of Profit and Loss

PARTICULARS	NOTE REF.	2021	2020
I. Expenses:			
Employee benefits expense		69	25
Other expenses	2	115	110
II. Tax expense:			
Current tax (paid during year)		243	140

Notes to accounts

	2021	2020
1. Share Capital		
Equity Shares of Rs.10 each, fully paid up	500	200
2. Other expenses		
Overheads	115	110

Prepare Cash Flow Statement of Supriya Ltd. for the year ended 31st March, 2021 in accordance with AS-3 (Revised) using direct method. All transactions were done in cash only. There were no outstanding/prepaid expenses as on 31st March, 2020 and on 31st March, 2021. Ignore deprecation. Dividend amounting Rs. 80,000 was paid during the year ended 31st March, 2021.

Solution:

Supriya Ltd.
Cash Flow Statement for the year ended 31st March, 2021
(Using direct method)

(Rs. in '000)

Cash flows from operating activities		
Cash receipts from customers	2,783	
Cash payments to suppliers	(2,047)	
Cash paid to employees	(69)	
Other cash payments (for overheads)	(115)	
Cash generated from operations	552	
Income taxes paid	(243)	
Net cash from operating activities		309
Cash flows from investing activities		
Payments for purchase of Property, Plant and Equipment	(102)	
Net cash used in investing activities		(102)
Cash flows from financing activities		
Proceeds from issuance of share capital	300	
Bank loan repaid	(250)	
Dividend paid	(80)	
Net cash used in financing activities		(30)
Net increase in cash and cash equivalents		177
Cash and cash equivalents at beginning of period		35

Cash and cash equivalents at end of period	212

Q17. CF Full (Indirect Method) (RTP May 2022) **REG. PAGE NO.**

From the following details relating to the accounts of Omega Ltd. prepare Cash Flow Statement for the year ended 31st March, 2021:

	31.03.2021(Rs.)	31.03.2020 (Rs.)
Share Capital	14,00,000	11,20,000
General Reserve	5,60,000	3,50,000
Profit and Loss Account	1,40,000	84,000
Debentures	2,80,000	-
Provision for taxation	1,40,000	98,000
Trade payables	9,80,000	11,48,000
Plant and Machinery	9,80,000	7,00,000
Land and Building	8,40,000	5,60,000
-Investments	1,40,000	-
Trade receivables	7,00,000	9,80,000
Inventories	5,60,000	2,80,000
Cash in hand and at Bank	2,80,000	2,80,000

(i) Depreciation @ 20% was charged on the opening value of Plant and Machinery.

(ii) At the year end, one old machine costing 70,000 (WDV 28,000) was sold for Rs. 49,000. Purchase of machinery was also made at the year end.

(iii) Rs. 70,000 was paid towards Income tax during the year.

(iv) Land & Building is not subject to any depreciation. Expenses on renovation of building amount Rs. 2,80,000 were incurred during the year.

Prepare Cash Flow Statement.

Solution:

Omega Ltd.
Cash Flow Statement for the year ended 31st March, 2021

Cash Flow from Operating Activities		
Increase in balance of Profit and Loss Account	56,000	
Provision for taxation	1,12,000	
Transfer to General Reserve	2,10,000	
Depreciation	1,40,000	
Profit on sale of Plant and Machinery	(21,000)	
Operating Profit before Working Capital changes	4,97,000	
Increase in Inventories	(2,80,000)	
Decrease in Trade receivables	2,80,000	
Decrease in Trade payables	(1,68,000)	
Cash generated from operations	3,29,000	
Income tax paid	(70,000)	
Net Cash from operating activities		2,59,000
Cash Flow from Investing Activities		
Purchase of plant & machinery	(4,48,000)	
Expenses on building	(2,80,000)	
Increase in investments	(1,40,000)	
Sale of old machine	49,000	
Net Cash used in investing activities		(8,19,000)
Cash Flow from Financing activities		
Proceeds from issue of shares	2,80,000	
Proceeds from issue of debentures	2,80,000	
Net cash from financing activities		5,60,000
Net increase in cash or cash equivalents		NIL
Cash and Cash equivalents at the beginning of the year		2,80,000
Cash and Cash equivalents at the end of the year		2,80,000

Working Notes:

Provision for taxation account

	Rs.		Rs.
To Cash (Tax Paid)	70,000	By Balance b/d	98,000
To Balance c/d	1,40,000	By Profit and Loss A/c (balancing figure)	1,12,000
	2,10,000		**2,10,000**

Plant and Machinery account

	Rs.		Rs.
To Balance b/d	7,00,000	By Depreciation	1,40,000
To Profit and Loss A/c (profit on sale of machine)	21,000		
To Cash (Balancing figure)	4,48,000	By Cash (sale of machine)	49,000
		By Balance c/d	9,80,000
	11,69,000		11,69,000

Q18. CF Full (Indirect Method) (RTP May 2023) **REG. PAGE NO.**

Following is the Balance Sheet of Fox Ltd. You are required to prepare cash flow statement using Indirect Method.

PARTICULARS	NOTE REF.	31.3.2021 (Rs.)	31.3.2020 (Rs.)
I. EQUITY & LIABILITIES			
1. Shareholder's Funds			
(a) Share Capital	1	5,60,000	3,00,000
(b) Reserve and Surplus	2	35,000	25,000
3. Current Liabilities			
Trade Payables		1,50,000	60,000
Short-term provisions (Provision for taxation)		8,000	5,000
		7,53,000	**3,90,000**
II. ASSETS			
1. Non-Current Assets			
Property, Plant and Equipment		3,50,000	1,80,000
2. Current Assets			
(a) Inventories		1,20,000	50,000
(b) Trade Receivables		1,00,000	25,000
(c) Cash & Cash Equivalents		1,05,000	90,000
(d) Other current assets		78,000	45,000
		7,53,000	3,90,000

Notes to Accounts

PARTICULARS	31.3.2021 (Rs.)	31.3.2020 (Rs.)
1. Share Capital		
(a) Equity share capital	4,10,000	2,00,000
(b) Preference share capital	1,50,000	1,00,000
	5,60,000	3,00,000
2. Reserve and Surplus		
Surplus in statement of profit and loss at the beginning of the year	25,000	
Add: Profit of the year	20,000	
Less: Dividend	(10,000)	
Surplus in statement of profit and loss at the end of the year	35,000	25,000

Additional Information:

1. Dividend paid during the year Rs. 10,000

2. Depreciation charges during the year Rs. 40,000.

Solution:

Fox Ltd.

Cash Flow Statement for the year ended 31st March, 2021

	Rs.	Rs.
Cash flows from operating activities		
Net Profit (35,000 less 25,000)	10,000	
Add: Dividend	10,000	
Provision for tax	8,000	
Net profit before taxation and extraordinary items	28,000	
Adjustments for:		
Depreciation	40,000	
Operating profit before working capital changes		68,000
Increase in trade receivables	(75,000)	
Increase in inventories	(70,000)	
Increase in other current assets	(33,000)	
Increase in trade payables	90,000	(88,000)
Cash used in operating activities		(20,000)
Less: Tax paid*		(5,000)
Net cash used in operating activities		(25,000)
Cash flows from investing activities		
Purchase of PPE	(2,10,000)	
Net cash used in investing activities		(2,10,000)
Cash flows from financing activities		
Issue of equity shares for cash	2,10,000	
Issue of preference shares	50,000	
Dividends paid	(10,000)	
Net cash generated from financing activities		2,50,000
Net increase in cash and cash equivalents		15,000
Cash and cash equivalents at beginning of period		90,000
Cash and cash equivalents at end of period		1,05,000

*Provision for tax of last year considered to be paid in the current year.

Working Note:

	Rs.
Property, plant and equipment acquisitions	
W.D.V. at 31.3.2021	3,50,000
Add back:	
Depreciation for the year	40,000
	3,90,000
Less: W.D.V. at 31.12.2020	1,80,000
Acquisitions during 2020-2021	2,10,000

CHAPTER – 2

AMALGAMATION OF COMPANIES

Q1. Calculation Based Question (ICAI New July 2021 Q5(a) 10M) REG. PAGE NO

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

PARTICULARS	NOTE REF.	Black LTD. (Rs. 000)	White LTD. (Rs. 000)
I. EQUITY & LIABILITIES			
1. Shareholder's Funds			
(A) Share Capital	1	6,000	3,600
(B) Reserves & Surplus	2	1,080	660
2. Current Liabilities			
(A)Trade Payables		600	360
TOTAL		**7,680**	**4,620**
II. ASSETS			
1. Non-Current Assets			
(A) Property, Plant & Equipments		3,600	2,400
2. Current Assets			
(A) Inventories		960	720
(B) Trade Receivables		1,680	1,080
(C) Cash & Cash Equivalents		1,440	420
TOTAL		**7,680**	**4,620**

PARTICULARS	Black LTD. (Rs. 000)	White LTD. (Rs. 000)
1. Share Capital		
Equity shares of Rs. 100 each	6,000	3,600
2. Reserve & Surplus		
General reserve	360	180
Profit & loss account	720	480
TOTAL	**1,080**	**660**

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

No Balance Sheet of White Limited is available as on that date. It is, however estimated that White Limited earned profit of Rs. 2,40,000 after charging proportionate depreciation @ 10% p.a. on Property Plant and Equipment, during April-June, 2020. Estimated profit of Black Limited during these 3 months was Rs. 4,80,000 after charging proportionate depreciation @ 10% p.a. on Property Plant and Equipment. Both the companies have declared and paid 10% dividend within this 3 months' period. Goodwill of White Limited is valued at Rs. 2,40,000 and Property Plant and Equipment are valued at Rs. 1,20,000 above the depreciated book value on the date of takeover. Purchase consideration is to be satisfied by Black Limited by issuing shares at par.

Ignore income tax. You are required to:

a) Calculate the number of shares issued by Black Ltd.
b) Calculate the balance of Net Current Assets of Black Limited and White Limited as on 1st July, 2020.
c) Give balance of Profit or Loss of Black Limited as on 1st July, 2020.

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 [24,00,000x10%x3/12]	(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 x 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. @ Rs. 100 each		45,000 shares

(ii) Calculation of Net Current Assets as on 01.07.2020

		Black Ltd.		White Ltd.
	Rs.	Rs.	Rs.	Rs.
Current Assets:				
Inventory		9,60,000		7,20,000
Trade receivables		16,80,000		10,80,000
Cash and Bank	14,40,000		4,20,000	
Less: Dividend	(6,00,000)		(3,60,000)	
Add: Profit after depreciation	4,80,000		2,40,000	
Add: Depreciation being non Cash	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

Q2. Accounting in the Books of T'ree Co. (Pur.) (ICAI New May 2022) REG. PAGE NO

The summarized balance sheet of A Ltd. And B Ltd. As at 31st March, 2022 are as under:

PARTICULARS	A LTD. (Rs)	B LTD. (Rs)
I. EQUITY & LIABILITIES		
(A) Equity Shares of Rs. 10 each, fully paid up	30,00,000	24,00,000
(B) Share premium account	4,00,000	--
(C) General reserve	6,20,000	5,00,000
(D)Profit & loss account	3,60,000	3,20,000

(E) Retirement gratuity fund account	1,00,000	--
(F) 10% Debentures	20,00,000	--
(G) Unsecured loan (including loan from A ltd.)	6,00,000	8,20,000
(H) Trade Payables	1,00,000	3,40,000
TOTAL	**71,80,000**	**43,80,000**
II. ASSETS		
(A) Land and buildings	28,00,000	21,00,000
(B) Plant and machinery	20,00,000	7,60,000
(C) Long term advance to B Ltd.	2,20,000	--
(D) Inventory	10,40,000	7,00,000
(E) Trade Receivables	8,20,000	5,20,000
(F) Cash at Bank	3,00,000	3,00,000
TOTAL	**71,80,000**	**43,80,000**

B Ltd. is to declare and pay 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 60 lakhs divided into 6 lakhs equity shares of 10 each.

(b) As per Registered Valuer the value of equity shares of A Ltd. is 18 per share and of B Ltd. is Rs.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 10 each at a premium of 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.**

PARTICULARS		Dr. (Rs.)	Cr. (Rs.)
Business Purchase A/c Dr. To Liquidator of A Ltd. A/c		54,00,000	 54,00,000
Land & Building Dr. Plant & Machinery A/c Dr. Long term advance to B Ltd. A/c Dr. Inventories A/c Dr. Trade Receivables A/c Dr. Cash and Bank A/c Dr. Goodwill A/c Dr. To Retirement Gratuity Fund A/c To 10% Debentures A/c To Unsecured Loan A/c To Trade Payables A/c To Other liabilities A/c To Business Purchase A/c		28,00,000 20,00,000 2,20,000 10,40,000 8,20,000 3,00,000 12,20,000	 1,00,000 20,00,000 6,00,000 1,00,000 2,00,000 54,00,000
10% Debentures A/c Dr. To 12% Debentures A/c		20,00,000	 20,00,000
Liquidator of A Ltd. A/c Dr. To Equity Share Capital A/c To Securities Premium A/c		54,00,000	 27,00,000 27,00,000
Business Purchase A/c Dr. To Liquidator of B Ltd. A/c		28,80,000	 28,80,000
Land and Building A/c Dr.		21,00,000	

Plant & Machinery A/c Inventories A/c Trade Receivables A/c Cash and Bank (less dividend) A/c To Unsecured Loan A/c To Trade Payables A/c To Business Purchase A/c To Capital Reserve A/c	Dr. Dr. Dr. Dr.		7,60,000 7,00,000 5,20,000 60,000	 8,20,000 3,40,000 28,80,000 1,00,000
Liquidators of B Ltd. A/c To Equity Share Capital A/c To Securities Premium A/c	Dr.		28,80,000	 14,40,000 14,40,000
Unsecured Loans A/c To Long term Advance to B Ltd. A/c	Dr.		2,20,000	 2,20,000
*Capital Reserve A/c To Cash and Bank A/c (Liquidation expenses) To Goodwill A/c	Dr.		1,00,000	 80,000 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:

Goodwill A/c To Cash & Bank A/c (Liquidation expenses of A Ltd.)	Dr.		50,000	 50,000
Capital Reserve A/c To Cash and Bank A/c (Liquidation expenses of B Ltd.)	Dr.		30,000	 30,0000
Capital Reserve A/c To Goodwill A/c	Dr.		70,000	 70,000

Balance Sheet of Z Ltd. as at 31st March, 2022

PARTICULARS	NOTE REF.	AMOUNT
I. EQUITY & LIABILITIES		
1. Shareholder's Funds		
(A) Share Capital	1	41,40,000
(B) Reserves & Suplus	2	41,40,000
2. Non Current Liabilities		
Long Term Borrowings	3	20,00,000
Long Term Provisions	4	1,00,000
3. Current Liabilities		
Short-term borrowings	5	12,00,000
Trade Payables	6	4,40,000
Other Liability		2,00,000
TOTAL		**1,22,20,000**
II. ASSETS		
1. Non-Current Assets		
(A) Property, Plant & Equipments	7	76,60,000
(B) 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 & Cash Equivalents	10	2,80,000
TOTAL		**1,22,20,000**

Notes to Accounts

PARTICULARS		AMOUNT
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 & Surplus		
Securities Premium Account (4,14,000 shares × Rs. 10)		41,40,000
TOTAL		**41,40,000**
3. Long Term Borrowings		
14% Debentures		20,00,000
TOTAL		**20,00,000**
4. Long Term Provisions		
Retirement gratuity fund		1,00,000
TOTAL		**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
TOTAL		**12,00,000**
6. Trade Payables		
A Ltd.	1,00,000	
B Ltd.	3,40,000	4,40,000
TOTAL		**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
TOTAL		**76,60,000**
8. Inventories		
A Ltd.	10,40,000	
B Ltd .	7,00,000	17,40,000
TOTAL		**17,40,000**
9. Trade Receivables		
A Ltd.	8,20,000	
B Ltd.	5,20,000	13,40,000
TOTAL		**13,40,000**
10. Cash & cash equivalent		
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
TOTAL		**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

Q3. Accounting in the Books of T'ror & T'ree Co. (RTP Nov 2019) REG. PAGE NO

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

PARTICULARS	A LTD. (Rs)
I. EQUITY & LIABILITIES	
(A) 8,000 Equity Shares of Rs. 100 each	8,00,000
(C) 10% debentures	4,00,000
(D) Loans	1,60,000
(E) Trade payables	3,20,000
(F) General reserve	80,000
TOTAL	**17,60,000**
II. ASSETS	
(A) Buildings	3,40,000
(B) Machinery	6,40,000
(C) Inventory	2,20,000
(D) Trade receivables	2,60,000
(E) Bank	1,36,000
(F) Patent	1,30,000
(G) Share issue expenses	34,000
TOTAL	**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 Ltd.
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 % Debenture 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	NOTE REF.	AMOUNT
I. EQUITY & LIABILITIES		
1. Shareholder's Funds		
(A) Share Capital	1	4,88,000
(B) Reserves & Suplus	2	1,07,000
2. Current Liabilities		
Trade Payables	3	2,80,000

Bank Overdraft		6,00,000
TOTAL		**14,75,000**
II. ASSETS		
1. Non-Current Assets		
(A) Property, Plant & Equipments		
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 Account

PARTICULARS		AMOUNT
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 & 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
TOTAL		**2,16,000**
6. Inventories		
Opening balance	1,98,000	
Less: Cancellation of profit upon amalgamation	(15,000)	1,83,000
TOTAL		**1,83,000**
7. Trade receivables		
Opening balance	2,34,000	
Less: Intercompany transaction cancelled upon Amalgamation	(40,000)	1,94,000
TOTAL		**1,94,000**

Working Notes:

	Rs
1. Valuation of Goodwill	
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

	Rs.
3. Unrealized Profit on Inventory	
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 $\frac{40,000 \times 1,00,000}{1,60,000}$	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

Q4. Accounting in the Books of T'ror Co. (RTP May 2020) REG. PAGE NO

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:

PARTICULARS	P LTD. (Rs)	Q LTD. (Rs)
I. EQUITY & LIABILITIES		
(A) Equity Shares of Rs. 100 each	8,20,000	3,20,000
(B) 9% Pref. shares of Rs. 100 each	3,80,000	2,80,000
(C) 8% debentures	2,00,000	1,00,000
(D) General reserve	1,50,000	50,000
(E) Profit & loss A/c	3,52,000	2,05,000
(F) Unsecured loan	--	1,75,000
(G) Trade Payables	88,000	1,60,000
TOTAL	**19,90,000**	**12,90,000**
II. ASSETS		
(A) Land and buildings	4,50,000	3,40,000
(B) Furniture & fittings	1,00,000	50,000
(B) Plant and machinery	6,20,000	4,50,000
(C) Trade receivables	3,25,000	1,50,000
(D) Inventory	2,33,000	1,05,000
(E) Cash at bank	2,08,000	1,75,000
(F) Cash in hand	54,000	20,000
TOTAL	**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:

1) 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.
2) 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.
3) 6% Debentures to discharge the 8% debentures of both the companies.
4) 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 and Building	4,50,000	By 8% Debentures	2,00,000
To Plant and Machinery	6,20,000	By Trade Payables	88,000
To Furniture & Fitting	1,00,000	By PQ Ltd. (PC)	16,02,100
To Trade receivables	3,25,000	By Equity Shareholders (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	8,20,000
To Equity Shares in PQ Ltd	10,82,400	By Profit & Loss A/c	3,52,000
To Cash	1,01,700	By General Reserve	1,50,000
	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% Debentureholders Account

	Rs.		Rs.
To 6% Debentures.	2,00,000	By 8% Debentures	2,00,000
	2,00,000		**2,00,000**

Books of Q Ltd.

Realization Account

	Rs.		Rs.
To Land and Building	3,40,000	By 8% Debentures	1,00,000
To Plant and Machinery	4,50,000	By Trade Payables	1,60,000
To Furniture & Fitting	50,000	By Unsecured loan	1,75,000
To Trade receivables	1,50,000	By PQ Ltd. (PC)	7,92,250
To Inventory/Stock	1,05,000	By Equity Shareholders (Loss)	90,750
To Cash at Bank	1,75,000		
To Cash in Hand	20,000		
To Preference shareholders (excess payment)	28,000		
	13,18,000		**13,18,000**

Equity Shareholders Account

	Rs.		Rs.
To Realization A/c (loss)	90,750	By Share capital	3,20,000
To Equity Shares in PQ Ltd	4,22,400	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 Pref. Share capital	2,80,000
		By Realization A/c	28,000
	3,08,000		**3,08,000**

PQ Ltd. Account

	Rs.			Rs.
To Realization A/c	7,92,250	By Shares in PQ Ltd.		
		For Equity	4,22,400	
		For Pref.	3,08,000	7,30,400
		By Cash		61,850
	7,92,250			**7,92,250**

8% Debentures holders Account

	Rs.		Rs.
To 6% Debentures.	1,00,000	By 8% Debentures	1,00,000
	1,00,000		**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
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.	Q Ltd
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.

Q5. Accounting in the Books of T'ror Co. & T'ree Co. (RTP May'21) REG. PAGE NO.

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

PARTICULARS	(Rs)
Share Capital :	
Equity shares of Rs. 10 each	3,00,000
6000, 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 authorized 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.
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 shareholders A/c (W.N.2)	5,400		
	5,60,400		**5,60,400**

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.

Bank Account

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

Balance Sheet as at 31st March, 2020

PARTICULARS	NOTE REF.	AMOUNT
I. EQUITY & LIABILITIES		
1. Shareholder's Funds		
(A) 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 & Equipments		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

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

Working Notes:

1. Calculation of Purchase consideration

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

Q6. Accounting in the Books of T'ree Co. (RTP Nov 21) REG. PAGE NO.

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):

PARTICULARS	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 on 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. (Rs.)	Cr. (Rs.)
Business Purchase Account Dr. To Liquidator of Heera Ltd. account To Liquidator of Rita Ltd. account (Being the amount of purchase consideration payable to liquidator of Heera Ltd. and Rita ltd. for assets taken over)		36,00,000	 21,60,000 14,40,000
Goodwill Dr. PPE account Dr. Inventory account Dr. Trade receivables account Dr. Cash at Bank account Dr. To Trade Payables account To Business Purchase account (Being assets and liabilities of Heera Ltd. take over)		5,40,000 7,20,000 3,60,000 4,80,000 3,00,000	 2,40,000 21,60,000
PPE account Dr. Inventory account Dr. Trade receivables account Dr. To bank overdraft account To Trade Payables account To Business Purchase account (Being assets and liabilities of Rita Ltd. taken over		10,80,000 6,60,000 7,80,000	 5,40,000 5,40,000 14,40,000
Liquidators of Heera Ltd. Account Dr. To Equity Share Capital account (57,600xRs.10) To Securities Premium account (57,600 x Rs. 15) (Being the allotment of shares as per agreement for discharge of purchase consideration)		21,60,000	 8,64,000 12,96,000
Liquidators of Rita Ltd. Account Dr. To Equity Share Capital account (86,400xRs.10) To Securities Premium account (86,400 x Rs. 15) (Being the allotment of shares as per agreement for discharge of purchase consideration)		14,40,000	 5,76,000 8,64,000
Bank account Dr. To Equity share capital account (72,000 x Rs.10) To Securities premium (72,000 x Rs. 15) (Equity share capital issued to raise working capital)		18,00,000	 7,20,000 10,80,000

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

	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

Q7. Accounting in the Books of T'ree Co. (Pur.) (RTP Nov 22) REG. PAGE NO.

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 REF.	Truth LTD.	Myth LTD.
I. EQUITY & LIABILITIES			
1. Shareholder's Funds			
(A) Share Capital	1	10,00,000	4,00,000
(B) Reserves & Surplus	2	11,35,000	4,13,000
2. Non Current Liabilities			
(A)Long Term Borrowings	3	--	1,50,000
3. Current Liabilities			
(A)Trade Payables		90,000	1,42,000
(B) Other Current Liablities		50,000	40,000
TOTAL		**22,75,000**	**11,45,000**
II. ASSETS			
1. Non-Current Assets			
(A) Property, Plant & Equipments		15,75,000	6,80,000
(B) Investment		1,87,500	1,00,000
2. Current Assets			
(A) Inventories		2,15,000	85,000
(B) Trade Receivables		2,02,500	1,75,000
(C) Cash & Cash Equivalents		95,000	1,05,000
TOTAL		**22,75,000**	**11,45,000**

Notes to Accounts

PARTICULARS	Truth LTD.	Myth LTD.
1. Share Capital		
Equity Share Of Rs. 100 each	10,00,000	4,00,000
TOTAL	**10,00,000**	**4,00,000**
2. Reserves & Surplus		
General Reserve	5.05,000	2,30,000
Profit and Loss	4,45,000	1,58,000
Export Profit Reserve	1,85,000	25,000
TOTAL	**11,35,000**	**4,13,000**
3. Non- Current Liablities		
14% Debentures		1,50,000

Truth Limited would issue 12% debentures to discharge the claim of the debenture holders of Myth Limited so as to maintain their present annual interest income. Non -trade investment, which constitute

80% of their respective total investments yielded income of 20% to Truth Limited and 15% to Myth Limited. This income is to be deducted from profits while computing average profit for the purpose of calculating goodwill. Profit before tax of both the companies during the last 3 years were as follows:

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

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

Prepare Balance Sheet of Truth Limited after the amalgamation

Solution :-

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

PARTICULARS	NOTE REF.	AMOUNT
I. EQUITY & LIABILITIES		
1. Shareholder's Funds		
(A) Share Capital	1	13,13,750
(B) Reserves & Suplus	2	20,76,250
2. Non Current Liabilities		
12% Debentures	3	1,75,000
3. Current Liabilities		
Trade Payables	4	2,32,000
Other current liabilities	5	90,000
TOTAL		**38,87,000**
II. ASSETS		
1. Non-Current Assets		
(A) Property, Plant & Equipments	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

PARTICULARS			AMOUNT
1. Share Capital			
1,31,375 Equity Shares of Rs. 10 each [1,00,000 + 31,375] (of the above shares, 31,375 shares were issued to the vendors otherwise than for cash)			13,13,750
2. Reserves & 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
TOTAL			**20,76,250**
3. Long Term Borrowings			

12% Debentures issued to Myth Ltd.		1,75,000
TOTAL		**1,75,000**
4. Trade Payables		
Trade payables.	90,000	
Add: Taken over	1,42,000	2,32,000
TOTAL		**2,32,000**
5. Other Current Liabilities		
Truth Ltd.	50,000	
Myth Ltd.	40,000	90,000
TOTAL		**90,000**
6. Property, plant & equipment		
Truth Ltd	15,75,000	
Myth Ltd.	6,80,000	22,55,000
TOTAL		**22,55,000**
7. Investment		
Truth Ltd.	1,87,500	
Myth Ltd.	1,00,000	2,87,500
TOTAL		**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.
		Rs.		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
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.	Rs.	Rs.
Goodwill [W.N. 1]	18,65,000		4,67,000	
Other Assets	22,75,000	41,40,000	11,45,000	16,12,000

Less: Liabilities:				
12% Debentures	-		1,75,000**	
Trade payables	90,000		1,42,000	
Provision for Tax	50,000	(1,40,000)	40,000	(3,57,000)
Net Assets		40,00,000		12,55,000
Intrinsic value per share [Net Assets / No. of Shares]		40,00,000 / 1,00,000 = Rs. 40		12,55,000 / 40,000 = Rs. 31.375

** 1,50,000 x14%
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

Q8. Accounting in the Books of T'ree Co. (RTP May 2018) REG. PAGE NO

P Ltd. and Q Ltd. agreed to amalgamate their business. The scheme envisaged a share capital, equal to the combined capital of P Ltd. and Q Ltd. for the purpose of acquiring the assets, liabilities and undertakings of the two companies in exchange for share in PQ Ltd. The Summarized Balance Sheets of P Ltd. and Q Ltd. as on 31st March, 2017 (the date of amalgamation) are given below:

PARTICULARS	P LTD. (Rs)	Q LTD. (Rs)
I. EQUITY & LIABILITIES		
1. Shareholder's Funds		
(A) Share Capital	6,00,000	8,40,000
(B) Reserves & Surplus	10,20,000	6,00,000
2. Current Liabilities		
(A)Bank overdraft	--	5,40,000
(B)Trade Payables	2,40,000	5,40,000
TOTAL	**18,60,000**	**25,20,000**
II. ASSETS		
1. Non-Current Assets		
(A)Fixed assets (excluding goodwill)	7,20,000	10,80,000
2. Current Assets		
(A) Inventories	3,60,000	6,60,000
(B) Trade Receivables	4,80,000	7,80,000
(C) Cash at bank	3,00,000	--
TOTAL	**18,60,000**	**25,20,000**

The consideration was to be based on the net assets of the companies as shown in the above Balance Sheets, but subject to an additional payment to P Ltd. for its goodwill to be calculated as its weighted average of net profits for the three years ended 31st March, 2017. The weights for this purpose for the years 2014-15, 2015-16 and 2016-17 were agreed as 1, 2 and 3 respectively.

The profit had been:

2014-15 Rs. 3,00,000; 2015-16 Rs. 5,25,000 and 2016-17 Rs. 6,30,000.

The shares of PQ Ltd. were to be issued to P Ltd. and Q Ltd. at a premium and in proportion to the agreed net assets value of these companies.

In order to raise working capital, PQ Ltd proceeded to issue 72,000 shares of Rs. 10 each at the same rate of premium as issued for discharging purchase consideration to P Ltd. And Q Ltd.

You are required to:

(i) **Calculate** the number of shares issued to P Ltd. and Q Ltd; and

(ii) **Prepare** required journal entries in the books of PQ Ltd.; and

(iii) **Prepare** the Balance Sheet of PQ Ltd. as per Schedule III after recording the necessary journal entries.

Solution :-

(i) Calculation of number of shares issued to P Ltd. and Q Ltd.:

Amount of Share Capital as per balance sheet	Rs.
P Ltd.	6,00,000
Q Ltd.	8,40,000
	14,40,000

Share of P 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 Q 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

(ii) Journal Entries in the books of PQ Ltd.

PARTICULARS		Dr. (Rs.)	Cr. (Rs.)
Business Purchase Account Dr.		36,00,000	
To Liquidator of P Ltd. account			21,60,000
To Liquidator of Q Ltd. account			14,40,000
(Being the amount of purchase consideration payable to liquidator of P Ltd. and Q 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 account Dr.		3,00,000	
To Trade Payables account			2,40,000
To Business Purchase account			21,60,000
(Being assets and liabilities of P Ltd. take 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 Q Ltd. taken over			
Liquidators of P Ltd. Account Dr.		21,60,000	
To Equity Share Capital account (86,400xRs.10)			8,64,000
To Securities Premium account (86,400x Rs. 15)			12,96,000
(Being the allotment of shares as per agreement for discharge of purchase consideration)			
Liquidators of Q Ltd. Account Dr.		14,40,000	
To Equity Share Capital account (57,600xRs.10)			5,76,000
To Securities Premium account (57,600x Rs. 15)			8,64,000
(Being the allotment of shares as per agreement for discharge of purchase consideration)			
Bank account 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)			

(iii) Balance Sheet of PQ Ltd. on 31st March, 2017 (after amalgamation)

PARTICULARS	NOTE REF.	AMOUNT
I. EQUITY & LIABILITIES		
1. Shareholder's Funds		
(A) Share Capital	1	21,60,000
(B) Reserves & Suplus	2	32,40,000
2. Current Liabilities		
Trade Payables (2,40,000 + 5,40,000)		7,80,000
TOTAL		**61,80,000**
II. ASSETS		
1. Non-Current Assets		
(A) Fixed assets		
Tangible assets (7,20,000 + 10,80,000)		18,00,000
Intangible assets (Goodwill)	4	5,40,000
2. Current Assets		
(A) Inventories (3,60,000 + 6,60,000)		10,20,000
(B) Trade Receivables (4,80,000 +7,80,000)		12,60,000
(C) Cash & Cash Equivalents	3	15,60,000
E		**61,80,000**

Notes to Accounts

	Rs.
1 Share Capital	
Issued, subscribed and paid up share capital 2,16,000 Equity shares of Rs.10 each (Out of the above 1,44,000 shares issued for non-cash consideration under scheme of amalgamation)	21,60,000
2 Reserves and Surplus	
Securities premium (@Rs.15 for 2,16,000 shares)	32,40,000
3 Cash and cash equivalents	
Cash at Bank	15,60,000
4 Intangible Assets	
Goodwill	5,40,000

Working Notes:

1. Calculation of goodwill of P Ltd

Particulars	Amount (Rs.)	Weight	Weighted Amount (Rs.)
2014-15	3,00,000	1	3,00,000
2015-16	5,25,000	2	10,50,000
2016-17	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

	P Ltd. Rs.	Q 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

3. New authorized capital

= Rs. 14,40,000 + Rs. 12,00 000 = Rs. 26,40,000

4. Cash and Cash equivalents

	Rs.
P Ltd. Balance	3,00,000
Cash received from Fresh issue (72,000 X Rs. 25)	18,00,000
	21,00,000
Less: Bank Overdraft	5,40,000
	15,60,000*

*The balance of cash and cash equivalents has been shown after setting off overdraft amount

Q9. Accounting in the Books of T'ree Co. (Merger & Pur.) (RTP May 2022) REG. PAGE NO

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

PARTICULARS	NOTE REF.	Aakash LTD. (Rs)	Ganga LTD. (Rs)
I. EQUITY & LIABILITIES			
1. Shareholder's Funds			
(A) Share Capital	1	80,00,000	20,00,000
(B) Reserves & 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			
(A) Property, Plant & Equipments		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:

PARTICULARS	Aakash LTD (Rs)	Ganga LTD (Rs)
1. Share Capital		
(a) Authorized, issued, subscribed & paid up		
6,00,000 equity shares of Rs. 10 each	60,00,000	--
20,000 Pref. shares of Rs. 100 each	20,00,000	--
2,00,000 equity shares of Rs. 10 each	--	20,00,000
TOTAL	**80,00,000**	**20,00,000**
2. Reserves & Surplus		
General Reserve	8,00,000	56,00,000
Surplus	(3,32,00,000)	--
TOTAL	**(3,24,00,000)**	**56,00,000**
3. Secured Loans		

(Secured loans of Aakash Ltd. 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
TOTAL	**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:

1) 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.
2) Property, Plant and Equipment of both the companies are taken over at book value by Aakash Ganga Limited.
3) Secured Loans include Rs. 32,00,000 accured interest in case of Ganga Limited.
4) 4,00,000 Equity Shares of Rs. 10 each are allotted by Aakash Ganga 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.
5) Preference Shareholders in Aakash Limited are issued Equity Shares in Aakash Ganga Ltd. worth Rs. 4,00,000 in lieu of their present holdings.
6) Secured Loan agree to continue the balance amount of their loans to Aakash Ganga 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.
7) Unsecured Loans are taken over by Aakash Ganga Limited at 25% of loan amounts.
8) Employees are issued fully paid Equity Shares in Aakash Ganga Limited in full settlement of their dues.
9) Statutory Liabilities are taken over by Aakash Ganga 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 Aakash Ganga Limited as at 1.4.2021.

<u>Solution:-</u>

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

PARTICULARS	NOTE REF.	AMOUNT
<u>I. EQUITY & LIABILITIES</u>		
1. Shareholder's Funds		
(A) Share Capital	1	1,40,00,000
2. Non-Current Liabilities		
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**
<u>II. ASSETS</u>		
1. Non-Current Assets		
(A) Property, Plant & Equipments	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		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.

		Aakash Limited.		Ganga Limited.
	Rs.	Rs.	Rs.	Rs.
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.

	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

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

Q10. Calculation of Purchase Consideration (ICAI New Nov 18 , 22) REG. PAGE NO

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.

Solution:- 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.

Computation of Purchase consideration	Rs.	Form
For Preference Shareholders of Moon Ltd. (25,000 × Rs. 70)	17,50,000	25,000 Preference Shares of Star Ltd.
For equity shareholders of Moon Ltd. (70,000 × Rs. 110)	77,00,000	70,000 Equity shares of Star Ltd.
	1,25,000	Cash
Total Purchase consideration	95,75,000	

Q11. Calculation of Purchase Consideration (ICAI CA-Inter New Dec 2021) REG. PAGE NO.

Moon Limited is absorbed by Sun Limited; the consideration, being the takeover of liabilities, the payment of cost of absorption not exceeding Rs. 10,000 (actual cost Rs. 9000); 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 share of Rs. 10/- each at a premium of 30% fully paid for every three shares in Moon Limited respectively. The number of shares of the vendor company is 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.

Purchase consideration will be:

	Rs.	From
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.

INTERNAL RECONSTRUCTION

Q1. IR Complete Question (RTP May 2021) **REG. PAGE NO.**

Recover Ltd decided to re-organize 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	NOTE REF.	AMOUNT
I. EQUITY & LIABILITIES		
1. Shareholder's Funds		
(A) Share Capital	1	3,50,000
(B) Reserves & Suplus	2	(70,000)
2. Non Current Liabilities		
Long Term Borrowings	3	55,000
3. Current Liabilities		
Trade Payables		80,000
Short Term Borrowings – Bank OD		90,000
TOTAL		**5,05,000**
II. ASSETS		
1. Non-Current Assets		
(A) Property, Plant & Equipments	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
TOTAL		**5,05,000**

Notes to Accounts

PARTICULARS	AMOUNT
1. Shareholder's Funds	
Equity Share Capital	
20,000 Equity Shares of Rs. 10 each	2,00,000
15,000 8% Pref. Shares of Rs. 10 each (Preference dividend has been in arrears for 4 years)	1,50,000
TOTAL	**3,50,000**
2. Reserves & Surplus	
Securities Premium	10,000
Debit Balance of Profit & Loss Account	(80,000)
TOTAL	**(70,000)**
3. Long Term Borrowings	
Secured – 9% Debentures (Secured on the freehold Property)	50,000
Accured Interest on 9% Debentures	5,000
TOTAL	**55,000**
4. Property, Plant & Equipments	
Freehold Property	1,20,000
Leasehold Property	85,000
Plant and Machinery	1,30,000
TOTAL	**3,35,000**
5. Intangible Assets	
Goodwill	50,000
6. Non Current Investments	
Non Trade Investments at Cost	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. To 8% Cumulative Preference share capital (Rs.2.5) A/c To Capital reduction (Rs. 7.5) A/c (Preference shares being reduced to shares of Rs. 2.5 per share and remaining transferred to capital reduction account as per capital reduction scheme)		1,50,000	 37,500 1,12,500
Equity Share Capital Account (Rs. 10) Dr. To Equity Share Capital Account (Rs. 1) To Capital Reduction Account (Rs. 9) (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.)		2,00,000	 20,000 1,80,000
Capital reduction A/c Dr. To Equity share capital A/c (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)		48,000	 48,000
Securities Premium A/c Dr. To Capital reduction A/c (Amount from the securities premium utilized towards the capital reduction a/c as a part of the internal reconstruction scheme)		10,000	 10,000
9% Debentures A/c Dr. Accrued interest on debentures A/c Dr. Bank A/c Dr. Capital reduction A/c Dr. To Freehold Property A/c (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.)		50,000 5,000 20,000 45,000	 1,20,000
Capital reduction A/c Dr. To Plant and Machinery Ac To Goodwill A/c To Inventory A/c		90,000	 30,000 50,000 10,000

(The assets written off as a part of the internal reconstruction scheme)			
Bank A/c Dr. Capital reduction A/c Dr. To Investments A/c (Investments sold at a loss debited to capital reduction account as a part of the internal reconstruction scheme)		32,000 8,000	 40,000
Contingent Liability A/c Dr. To Bank A/c (Contingent liability paid as a part of the internal reconstruction scheme)		7,000	 7,000
Bank A/c Dr. Capital reduction A/c Dr. To Contingent Liability A/c (The insurance company remitting part of the contingency payment amount)		6,300 700	 7,000
Capital reduction A/c Dr. To Profit and loss A/c (Accumulated losses written off to capital reduction account as a part of the internal reconstruction scheme).		80,000	 80,000
Capital reduction A/c Dr. To Capital reserve A/c (The balance in capital reduction account transferred to capital reserve as a part of the internal reconstruction scheme)		30,800	 30,800

Balance sheet of Recover Ltd. as at 31st March 2020 (and reduced)

PARTICULARS	NOTE REF.	AMOUNT
I. EQUITY & LIABILITIES		
1. Shareholder's Funds		
(A) Share Capital	1	1,05,500
(B) Reserves & Suplus	2	30,800
2. Non Current Liabilities		
Long Term Borrowings		
3. Current Liabilities		
(A) Trade Payables		80,000
(B) Bank Overdraft		90,000
TOTAL		**3,06,300**
II. ASSETS		
1. Non-Current Assets		
(A) Property, Plant & Equipments	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:

PARTICULARS	AMOUNT
1. Shareholder's Funds	
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
TOTAL	**1,05,500**
2. Reserves & Surplus	
Capital reserve	30,800

TOTAL	**30,800**
3. Property, Plant & Equipments	
Leasehold Property	85,000
Plant and Machinery	1,00,000
TOTAL	**1,85,000**
4.Cash and cash equivalents	
Bank A/c (20,000+32,000-7000+6,300)	51,300
TOTAL	**51,300**

Q2. IR Complete Question (RTP Nov 2021) **REG. PAGE NO.**

Shine Ltd. provides the following information as on 31st March, 2021:

PARTICULARS	AMOUNT (Rs. In 000)
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 of 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.

PARTICULARS		Dr. (Rs. In 000)	Cr. (Rs. In 000)
Equity share capital (Rs. 10) A/c Dr. To Equity Share Capital (Rs. 4) A/c To Capital Reduction A/c (Being conversion of equity share capital of Rs. 10 each into Rs. 4 each as per reconstruction scheme)		35,000	 14,000 21,000
8% Cumulative Preference Share capital (Rs. 100) A/c Dr. To 8% Cumulative Preference Share Capital (Rs. 60) A/c To Capital Reduction A/c (Being conversion of 6% cumulative preference shares capital of Rs. 100 each into Rs. 60 each as per reconstruction scheme)		17,500	 10,500 7,000
6% Debentures (Rs. 100) A/c Dr. To 9% Debentures (Rs. 80) A/c To Capital Reduction A/c (Being 9% debentures of Rs. 80 each issued to existing 6%		14,000	 11,200 2,800

debenture holders. The balance transferred to capital reduction account as per reconstruction scheme)			
Sundry Creditors A/c Dr. To Equity Share Capital (Rs. 4) A/c To Capital Reduction A/c (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)		7,000	 3,500 3,500
Provision for Taxation A/c Dr. Capital Reduction A/c Dr. To Liability for Taxation A/c (Being conversion of the provision for taxation into liability for taxation for settlement of the amount due)		350 175	 525
Liability for Taxation A/c Dr. To Current Assets (Bank A/c) (Being the payment of tax liability)		525	 525
Capital Reduction A/c Dr. To P & L A/c To PPE A/c To Current Assets A/c To Investments A/c To Capital Reserve A/c (Bal. fig.) (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)		34,125	 2,100 8,750 18,725 175 4,375

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**

Q3. IR Complete Question (RTP May 2020) **REG. PAGE NO.**

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

PARTICULARS	AMOUNT
I. EQUITY & LIABILITIES	
1. Shareholder's Funds	
(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) Reserves & Suplus	
Profit and 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	
(a) Workmen's Compensation Fund:	
Bombay Works	10,000
Chennai Works	5,000
(b)Trade Payables	1,25,000

TOTAL	**24,90,000**
II. ASSETS	
1. Non-Current Assets	
Property, Plant & Equipments	
Bombay Works	9,50,000
Chennai Works	7,75,000
2. Investments	
Investments for Workman's Compensation Fund	15,000
3. Current Assets	
(A) Inventories	4,50,000
(B) Trade Receivables	2,50,000
(C) Cash at Bank	50,000
TOTAL	**24,90,000**

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

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		Debit (Rs.)	Credit (Rs.)
7% Preference share capital (Rs. 100) Dr. To 9% Preference share capital (Rs. 80) To Capital reduction A/c (Being preference shares reduced to Rs. 80 and also rate of dividend raised from 7% to 9%)		9,00,000	 7,20,000 1,80,000
Equity share capital A/c (Rs. 100 each) Dr. To Equity share capital A/c (Rs. 10 each) To Capital reduction A/c (Being reduction of nominal value of one share of Rs. 100 each to Rs. 10 each)		10,00,000	 1,00,000 9,00,000
Bank A/c Dr. To Capital reduction A/c (Being directors refunded the fee amount)		50,000	 50,000
Trade payables A/c (Interest on debentures) Dr.		26,000	

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

Q4. IR Complete Question (RTP May 2019, N22) **REG. PAGE NO.**

The Balance Sheet of Lion Limited as on 31-03-2018 is given below:

PARTICULARS	NOTE REF.	AMOUNT (Rs. In Lakhs)
I. EQUITY & LIABILITIES		
1. Shareholder's Funds		
(A) Share Capital	1	1,400
(B) Reserves & Suplus	2	(522)
2. Non Current Liabilities		
Long Term Borrowings	3	700
3. Current Liabilities		
Trade Payables	4	102
Other Liabilities	5	24
TOTAL		**1,704**

II. ASSETS		
1. Non-Current Assets		
Property, Plant & Equipments	6	750
2. Current Assets		
(A) Current Investments	7	200
(B) Inventories	8	300
(C) Trade Receivables	9	450
(D) Cash and Cash Equivalents	10	4
TOTAL		**1,704**

Notes to Accounts

PARTICULARS	AMOUNT (Rs. In Lakhs)
1. Shareholder's Funds	
Equity Share Capital	
Authorized Share Capital	
200 lakhs Equity Shares of Rs. 10 each	2,000
8 lakhs 8% Pref Shares of Rs. 100 each	800
TOTAL	**2,800**
Issued, Subscribed & Paid Up Capital	
100 lakhs Equity Shares of Rs. 10 each	1,000
4 lakhs 8% Pref shares of Rs. 100 each, fully paid up	400
TOTAL	**1,400**
2. Reserves & Surplus	
Debit Balance of Profit & Loss Account	(522)
TOTAL	**(522)**
3. Long Term Borrowings	
6% Debentures (Secured by Freehold Property)	400
Director's Loan	300
TOTAL	**700**
4. Trade Payables	
Trade Payables for Goods	102
TOTAL	**102**
5. Other Current Liabilities	
Interest Accured and Due on 6% Debentures	24
TOTAL	**24**
6. Property, Plant & Equipments	
Freehold Property	550
Plant and Machinery	200
TOTAL	**750**
7. Current Investments	
Investments in Equity Instruments	200
TOTAL	**200**
8. Inventories	
Finished Goods	300
TOTAL	**300**
9. Trade Receivables	
Trade Receivables for Goods	450
TOTAL	**450**
10. Cash and Cash Equivalents	
Balance with Bank	4
TOTAL	**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:-

Journal Entries in the books of Lion Ltd.

PARTICULARS		Debit (Rs. In lakhs)	Credit (Rs. in lakhs)
8% Preference share capital (Rs. 100) Dr. To 8% Preference share capital (Rs. 80) To Capital reduction A/c (Being the preference shares of Rs.100 each reduced to Rs.80 each as per the approved scheme)		400	 320 80
Equity share capital A/c (Rs. 100 each) Dr. To Equity share capital A/c (Rs. 2 each) To Capital reduction A/c (Being the equity shares of Rs.10 each reduced to Rs.2 each)		1,000	 200 800
Capital Reduction A/c Dr. To Equity share capital A/c (Rs. 2 each) (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)		32	 32
6% Debentures A/c Dr. To Freehold property A/c (Being claim of Debenture holders settled in part by transfer of freehold property)		300	 300
Accrued debenture interest A/c Dr. To Bank A/c (Being accrued debenture interest paid)		24	 24
Freehold property A/c Dr. To Capital Reduction A/c (Being appreciation in the value of freehold property)		150	 150
Bank A/c Dr. To Investments A/c To Capital Reduction A/c (Being investment sold at profit)		250	 200 50
Director's loan A/c Dr. To Equity share capital A/c (Rs. 2 each) To Capital Reduction A/c (Being director's loan waived by 70% and balance being discharged by issue of 45 lakhs equity shares of Rs.2 each)		300	 90 210

Capital Reduction A/c Dr. To Profit and loss A/c To Trade receivables A/c (450 x 40%) To Inventories-in-trade A/c (300x 80%) To Bank A/c (600 x 5%) (Being certain value of various assets, penalty on cancellation of contract, profit and loss account debit balance written off through Capital Reduction Account)		972	 522 180 240 30
Capital Reduction A/c Dr. To Capital reserve A/c (Being balance transferred to capital reserve account as per the scheme)		286	 286

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**

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

Q5. IR Complete Question (ICAI New Nov 2022) **REG. PAGE NO.**

The following is the Balance Sheet of Purple Limited as at 31st March, 2022:

PARTICULARS	NOTE REF.	AMOUNT
I. EQUITY & LIABILITIES		
1. Shareholder's Funds		
(A) Share Capital	1	15,00,000
(B) Reserves & Suplus	2	(3,00,000)
2. Current Liabilities		
Trade Payables		2,20,000
Short Term Borrowings – Bank Overdraft		2,00,000
TOTAL		**16,20,000**
II. ASSETS		
1. Non-Current Assets		

(A)Property, Plant & Equipments	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**

Notes to Accounts:

PARTICULARS	AMOUNT
1. Share Capital	
90,000 Equity Shares of Rs. 10 each, fully paid up	9,00,000
6% Preference Share Capital	6,00,000
TOTAL	**15,00,000**
2. Reserves & Surplus	
Debit Balance of Profit & Loss Account	(3,00,000)
TOTAL	**(3,00,000)**
3. Property, Plant & Equipments	
Land and Building	5,40,000
Plant and Machinery	4,80,000
TOTAL	**10,20,000**
4. Intangible Assets	
Goodwill	84,600
Patents	36,000
TOTAL	**1,20,600**

1) Dividends on preference shares are in arrears for 3 years.
2) On the above date, the company adopted the following scheme of reconstruction:
3) The preference shares are converted from 6% to 8% but revalued in a manner in which the total return on them remains unaffected.
4) The value of equity shares is brought down to Rs. 8 per share.
5) The arrears of dividend on preference shares are cancelled.
6) The debit balance of Goodwill account is written off entirely.
7) Land and Building and Plant and Machinery are revalued at 85% and 80% of their respective book values.
8) Book debts amounting to Rs. 14,400 are to be treated as bad and hence to be written off.
9) 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.
10) The balance of total capital reduction is to be utilized in writing down Patents.
11) 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.

Solution:-

Journal Entries in the books of Purple Ltd.

PARTICULARS		Dr. (Rs.)	Cr. (Rs.)
6% Preference share capital A/c Dr. To 8% Preference share capital A/c To Capital reduction A/c (Being 6% preference shares converted to 8% preference shares so that return to pref. shareholders remains unaffected)		6,00,000	 4,50,000 1,50,000
Equity share capital A/c (Rs. 10) Dr. To Equity share capital A/c (Rs. 8) To Capital reduction A/c		9,00,000	 7,20,000 1,80,000

(Being equity capital reduced to nominal value of Rs. 8 each)			
Capital Reduction A/c Dr. To Goodwill A/c To Land and Building A/c To Plant and Machinery A/c To Trade Receivables A/c (Book debts) To Patents A/c (Bal. fig.) To Profit and loss A/c (Being losses and assets written off to the extent required)		3,30,000	 84,600 81,000 96,000 14,400 24,000 30,000
Bank A/c Dr. To Bank Loan A/c (Being Loan taken)		4,80,000	 4,80,000
Bank overdraft A/c Dr. To Bank A/c (Being Bank overdraft repaid)		2,00,000	 2,00,000

Capital Reduction Account

	Rs.		Rs.
To Goodwill A/c	84,600	By Equity Share Capital A/c	1,80,000
To Land & Building A/c	81,000	By 6% Preference Share Capital A/c	1,50,000
To Plant and Machinery A/c	96,000		
To Trade receivables (Book Debts) A/c	14,400		
To Profit & Loss A/c	30,000		
To Patents A/c (Bal. fig.)	24,000		
	3,30,000		3,30,000

Balance Sheet of Purple Ltd. (and reduced)
as at 31.3.2022

PARTICULARS	NOTE REF.	AMOUNT
I. EQUITY & LIABILITIES		
1. Shareholder's Funds		
(A) Share Capital	1	11,70,000
(B) Reserves & Surplus	2	(2,70,000)
2. Current Liabilities		
Short Term Borrowings (Secured Bank Loan)		4,80,000
Trade Payables		2,20,000
TOTAL		**16,00,000**
II. ASSETS		
1. Non-Current Assets		
(A)Property, Plant & Equipments	3	8,43,000
(B)Intangible Assets	4	12,000
2. Current Assets		
(A) Inventories		1,70,000
(B) Trade Receivables	5	2,87,400
(C) Cash and Cash Equivalents (7,600+4,80,000-2,00,000)		2,87,600
TOTAL		**16,00,000**

Notes to Accounts:

PARTICULARS		AMOUNT
1. Share Capital		
Authorized		
Issued, subscribed and paid up:		

90,000 Equity Shares of Rs. 8 each, fully paid up	7,20,000	
8% Preference Share Capital	4,50,000	11,70,000
TOTAL		**11,70,000**
2. Reserves & Surplus		
Debit Balance of Profit & Loss Account		(2,70,000)
TOTAL		**(2,70,000)**
3. Property, Plant & Equipments		
Land and Building	4,59,000	
Plant and Machinery	3,84,000	8,43,000
TOTAL		**8,43,000**
4. Intangible Assets		
Patent Rs. (36,000 - 24,000)		12,000
TOTAL		**12,000**
5. Trade Receivables		
Sundry Debtors	3,01,800	
Less: Bad debts	(14,400)	2,87,400
TOTAL		**2,87,400**

Note: *Face value of preference share is not given in the question (pre and post reconstruction) and hence any suitable value of preference share may be assumed.

Working Notes:

1. Calculation of new Preference Shares

Rate of return : 6% on Preference Shares

Dividend : (6/100) x Rs. 6,00,000 = Rs. 36,000

Rate of return : 8% on Preference Shares

Dividend : (8/100) x X = Rs. 36,000

X = (36,000/8) x 100 = Rs. 4,50,000

New Preference Share Capital = Rs. 4,50,000

Old Preference Share Capital = Rs. 6,00,000

(6,00,000 – 4,50,000) = Rs. 1,50,000 Amount taken to Capital Reduction A/c.

2. Since the company expects to earn a profit of Rs. 90,000 p.a. consecutively for three years and it shall be used to write-off debit balance of P & L account, hence Rs. 2,70,000 being loss shall be shown in the Balance Sheet under Reserve & Surplus head and Rs. 30,000 shall be written-off from Capital Reduction A/c.

3. Calculation of Amount written off on Land & Building and Plant & Machinery

Land & Building = (85/100) x 5,40,000 = Rs. 4,59,000

Plant & Machinery = (80/100) x 4,80,000 = Rs. 3,84,000

Reduced by:

Land & Building = (5,40,000 - 4,59,000) = Rs. 81,000

Plant & Machinery = (4,80,000 - 3,84,000) = Rs. 96,000

Q6. Calculation of Purchase Consideration (ICAI New July 2021) **REG. PAGE NO.**

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. 250,000.

(ii) Goodwill which stood at Rs. 2,70,000 is to be completely written off.

(iii) Plant & 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 & 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 Sapra Limited of the above reconstruction scheme considering that balance in General Reserve is utilized to write off the losses.

Solution:-

Journal Entries

PARTICULARS		Debit (Rs.)	Credit (Rs.)
Equity Share Capital (old) A/c Dr.		75,00,000	
To Equity Share Capital (Rs. 10) A/c			45,00,000
To 6% Preference Share Capital (Rs. 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 (Being general reserve utilized to write off the balance in Capital reduction A/c)			3,000

Q7. Calculation of Purchase Consideration (ICAI New Nov 2019) **EG. PAGE NO.**

Following is the summarized Balance Sheet of Fortunate Ltd. as on 31st March, 2019

PARTICULARS	AMOUNT
I. LIABILITIES	
Authorized and Issued Share Capital	
(A)15,000 8% Pref 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**
II. 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
Inventories	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			Debit (Rs.)	Credit (Rs.)
Equity Share Capital (Rs. 50 each) A/c	Dr.		9,37,500	
To Equity Share Capital (Rs. 5 each) A/c				93,750
To Capital Reduction A/c				8,43,750
(Being equity capital reduced to nominal value of Rs. 5 each)				
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)				
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)				
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)				
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)				
Equity share application A/c	Dr.		1,25,000	
To Equity share capital A/c				1,25,000
(Being application money transferred to capital A/c)				
Loan A/c	Dr.		2,50,000	
To Bank A/c				2,50,000

(Being loan repaid)			
Capital reduction A/c Dr.		7,68,750	
To Profit and loss A/c			5,63,750
To Plant A/c			43,750
To Trademarks and Goodwill A/c (Bal. fig.)			1,61,250
(Being losses and assets written off to the extent required)			

Balance sheet of Fortunate Ltd. (and reduced) as on 31.3.2019

PARTICULARS	NOTES REF	AMOUNT
I. EQUITY & LIABILITIES		
1. Shareholders' funds		
(A) Share capital	1	15,12,500
2. Non-current liabilities		
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**
II. 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 each	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**

Q8. IR Complete Question (ICAI New Nov 2018) **REG. PAGE NO.**

The summarized Balance Sheet of SK Ltd. as on 31 st March, 2018 is given below.

PARTICULARS	AMOUNT (000)
I. LIABILITIES	
Equity Shares of Rs. 10 each	35,000
8% Pref 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**
II. ASSETS	
Fixed Assets	43,750
Investments(Market Value Rs.3325000	3,500
Current Assets (incl 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 31 st 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		Rs. In '000	Rs. In '000
Equity Share Capital (Rs. 10 each) A/c Dr. To Equity Share Capital (Rs. 4 each) A/c To Capital ReductionA/c (Being conversion of equity share capital of Rs. 10 each into Rs. 4 each as per reconstruction scheme)		35,000	 14,000 21,000
8% Preference Share Capital (Rs. 100 each) A/c Dr. To 8% Preference Share Capital (Rs. 60 each) A/c To Capital Reduction A/c Being conversion of 6% cumulative preference shares capital of Rs. 100 each into Rs. 60 each as per reconstruction scheme.)		17,500	 10,500 7,000
6% Debentures (Rs. 100) A/c Dr. To 9% Debentures (Rs. 80) A/c To Capital Reduction A/c (Being 9% debentures of Rs. 80 each issued to existing 6% debenture holders. The balance transferred to capital reduction account as per reconstruction scheme)		14,000	 11,200 2,800
Sundry Creditors A/c Dr. To Equity Share Capital (Rs. 4) A/c To Capital Reduction A/c (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)		7,000	 3,500 3,500
Provision for Taxation A/c Dr. Capital Reduction A/c Dr.		350 175	

To Liability for Taxation A/c (Being conversion of the provision for taxation into liability for taxation for settlement of the amount due)			525
Liability for Taxation A/c Dr. To Current Assets (Bank A/c) (Being the payment of tax liability)		525	 525
Capital Reduction A/c Dr. To P & L A/c To Fixed Assets A/c To Current Assets A/c To Investments A/c To Capital Reserve A/c (Bal. fig.) (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)		34,125	 2,100 8,750 18,725 175 4,375

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**

Q9. IR Complete Question (RTP Nov 2018, M22, N20) **REG. PAGE NO.**

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

PARTICULARS	NOTE REF.	AMOUNT
fal. EQUITY & LIABILITIES		
1. Shareholder's Funds		
(A) Share Capital	1	70,00,000
(B) Reserves & Suplus	2	(14,60,000)
2. Non Current Liabilities		
10% Secured Debentures	3	16,00,000
3. 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
TOTAL		**81,00,000**
II. ASSETS		
1. Non-Current Assets		
(A) Property, Plant & Equipments	4	45,00,000
(B) Intangible Assets	5	15,00,000
2. Current Assets		
(A) Trade Investments		5,00,000
(B) Trade Receivables		5,00,000
(C) Inventories		10,00,000
(D) Discount on Issue of Debentures		1,00,000
TOTAL		**81,00,000**

Notes to Accounts

PARTICULARS	AMOUNT
1. Shareholder's Funds	
Equity Share Capital	
5,00,000 Equity Shares of Rs. 10 each	50,00,000
20,000 9% Pref. Shares of Rs. 100 each	20,00,000
TOTAL	**70,00,000**
2. Reserves & Surplus	
Debit Balance of Profit & Loss Account	(14,60,000)
TOTAL	**(14,60,000)**
3. Long Term Borrowings	
10% Secured Debentures	16,00,000
TOTAL	**16,00,000**
4. Property, Plant & Equipments	
Land and Building	30,00,000
Plant and Machinery	12,50,000
Furniture and Fixtures	2,50,000
TOTAL	**45,00,000**
5. Intangible Assets	
Goodwill	10,00,000
Patents	5,00,000
TOTAL	**15,00,000**

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

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

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

(i) All the equity shares to be converted into fully paid equity shares of Rs. 5.00 each.

(ii) The Preference shares be reduced to Rs. 50 each and the preference shareholders agreed to forego their arrears of preference dividends, in consideration of which 9% preference shares are to be converted into 10% preference shares.

(iii) Mr. Y and Mr. Z agreed to cancel 50% each of their respective total debt including interest on debentures. Mr. Y and Mr. Z also agreed to pay Rs. 1,00,000 and Rs. 60,000 respectively in cash and to receive new 12% debentures for the balance amount.

(iv) Persons relating to trade payables, other than Mr. Y and Mr. Z also agreed to forgo their 50% claims.

(v) Directors also waived 60% of their loans and accepted equity shares for the balance.

(vi) Capital commitments of Rs. 3.00 lacs were cancelled on payment of Rs. 15,000 as penalty.

(vii) Directors refunded Rs. 1,00,000 of the fees previously received by them.

(viii) Reconstruction expenses paid Rs. 15,000.

(ix) The taxation liability of the company was settled for Rs. 75,000 and was paid immediately.

(x) The Assets were revalued as under

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

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

Solution:

Journal Entries in the Books of Z Ltd.

PARTICULARS		Dr. (Rs.)	Cr. (Rs.)
Equity Share Capital (Rs. 10 each) A/c Dr. To Equity Share Capital (Rs. 5 each) A/c To Reconstruction A/c (Being conversion of 5,00,000 equity shares of Rs. 10 each fully paid into same number of fully paid equity shares of Rs. 5 each as per scheme of reconstruction.)		50,00,000	 25,00,000 25,00,000
9% Preference Share Capital (Rs. 100 each) A/c Dr. To 10% Preference Share Capital (Rs. 50 each) A/c To Reconstruction A/c (Being conversion of 9% preference share of Rs. 100 each into same number of 10% preference share of Rs. 50 each and claims of preference dividends settled as per scheme of reconstruction.)		20,00,000	 10,00,000 10,00,000
10% Secured Debentures A/c Dr. Trade payables A/c Dr. Interest on Debentures Outstanding A/c Dr. Bank A/c Dr. To 12% Debentures A/c To Reconstruction A/c (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.)		9,60,000 1,00,000 96,000 1,00,000	 6,78,000 5,78,000
10% Secured Debentures A/c Dr. Trade Payables Dr. Interest on debentures outstanding A/c Dr. Bank A/c Dr. To 12% debentures A/c To Reconstruction A/c (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.)		6,40,000 60,000 64,000 60,000	 4,42,000 3,82,000
Trade payables A/c Dr. To Reconstruction A/c (Being remaining trade payables sacrificed 50% of their claim.)		1,70,000	 1,70,000
Directors' Loan A/c Dr. To Equity Share Capital (Rs. 5) A/c To Reconstruction A/c (Being Directors' loan claim settled by issuing 12,000 equity shares of Rs. 5 each as per scheme of reconstruction.)		1,00,000	 40,000 60,000
Reconstruction A/c Dr. To Bank A/c (Being payment made towards penalty of 5% for cancellation of capital commitments of Rs. 3 Lakhs.)		15,000	 15,000
Bank A/c Dr. To Reconstruction A/c (Being refund of fees by directors credited to reconstruction A/c)		1,00,000	 1,00,000

Reconstruction A/c Dr. To Bank A/c (Being payment of reconstruction expenses)		15,000	 15,000
Provision for Tax A/c Dr. To Bank A/c To Reconstruction A/c (Being payment of tax liability in full settlement against provision for tax)		1,00,000	 75,000 25,000
Land and Building A/c Dr. To Reconstruction A/c (Being appreciation in value of Land & Building recorded)		2,00,000	 2,00,000
Reconstruction A/c Dr. To Goodwill A/c To Patent A/c To Profit and Loss A/c To Discount on issue of Debentures A/c To Plant and Machinery A/c To Furniture & Fixture A/c To Trade Investment A/c To Inventory A/c To Trade Receivables A/c To Capital Reserve (bal. fig.) (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.)		49,85,000	 10,00,000 5,00,000 14,60,000 1,00,000 6,50,000 1,00,000 50,000 2,50,000 1,00,000 7,75,000

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	15,000
To Reconstruction A/c	1,00,000	(capital commitment penalty paid)	
(refund of earlier fees by directors)		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	By Equity Share Capital A/c	25,00,000
To Bank (reconstruction expenses)	15,000	By 9% Pref. Share Capital A/c	10,00,00
To Goodwill	10,00,000	By Mr. Y (Settlement)	5,78,000
To Patent	5,00,000	By Mr. Z (Settlement)	3,82,000
To P & L A/c	14,60,000	By Trade Payables A/c	1,70,000
To Discount on issue of Debentures	1,00,000	By Director's loan	60,000
To P & M	6,50,000	By Bank	1,00,000
To Furniture and Fixtures	1,00,000	By Provision for tax	25,000
To Trade investment	50,000	By Land and Building	2,00,000

To Inventory	2,50,000		
To Trade Receivables	1,00,000		
To Capital Reserve (bal. fig.)	7,75,000		
	50,15,000		**50,15,000**

BUY BACK OF SECURITIES

Q1. Advanced Question (ICAI New Dec'21) **REG. PAGE NO.**

Mohan Ltd. furnishes the following summarised Balance Sheet on 31st March 2021:

PARTICULARS	AMOUNT (Lakhs)
EQUITY & LIABILITIES	
Shareholder's Funds	
Share Capital	
Equity Share of Rs. 10 each fully paid up	780
6% Red. Pref. Share of Rs. 50 each fully paid up	240
Reserves & Surplus	
Capital Reserve	58
General Reserve	625
Securities Premium	52
Profit & Loss	148
Revaluation Reserve	34
Infrastructure Development Fund	16
Non Current Liabilities	
7% Debentures	268
Unsecured Loans	36
Current Liabilities	395
TOTAL	**2652**
ASSETS	
Non-Current Assets	
Plant & Equipments less Depreciation	725
Investments (Cost)	720
Current Assets	1207
TOTAL	**2652**

Other Information:

(1) The company redeemed preference shares at a premium of 10% on 1st April,2021.

(2) It also offered to 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). These debentures were cancelled on 2nd April 2021.

(5) On 4th April 2021 company issued one fully paid-up equity share of Rs. 10 each by way of bonus for every five equity shares held by the shareholders.

You are required to:

(a) Calculate maximum possible number of equity shares that can be bought back as per the Companies Act, 2013 and

(b) Record the Journal Entries for the above-mentioned information.

Solution:-

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 As per the provisions of the Companies Act, 2013, Company	29.725 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	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 As per the provisions of the Companies Act, 2013, company	24.7875 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	Dr.	Cr.
2021 1st April	6% Redeemable preference share capital A/c Dr. Premium on redemption of preference shares A/c Dr. To Preference shareholders A/c (Being preference share capital transferred to shareholders account)	240 24	 264
	Preference shareholders A/c Dr. To Bank A/c (Being payment made to shareholders)	264	 264
	General Reserve or P&L A/c* Dr. To Premium on redemption of preference shares A/c (Being premium on redemption of preference shares adjusted though securities premium)	24	 24
2nd April	Equity shares buy-back A/c Dr. To Bank A/c (Being 11.175 lakhs equity shares of Rs 10 each bought back @ Rs 30 per share)	335.25	 335.25
	Equity share capital A/c Dr. Securities Premium A/c Dr. General Reserve or P&L A/c Dr. To Equity Shares buy-back A/c (Being cancellation of shares bought back)	111.75 52 171.50	 335.25
	General reserve A/c Dr. To Capital redemption reserve A/c (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 i.e., 240+ 111.75 lakhs))	351.75	 351.75
2nd April	7% Debentures A/c Dr. To Investment (own debentures) A/c To Profit on cancellation of own debentures A/c (Being cancellation of own debentures costing Rs 60 lakhs, face value being Rs 75 lakhs and the balance being profit on cancellation of debentures)	75	 60 15

4th April	Capital Redemption A/c Dr. To Bonus Shares A/c (Being issue of one bonus equity share for every five equity shares held)	133.65	133.65
	Bonus shares A/c Dr. To Equity share capital A/c (Being bonus shares issued)	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.

Q2. Basic Question on buy Back (ICAI New Jan'21) REG. PAGE NO.

The Directors of Umang Ltd. passed a resolution to buyback 5,00,000 of its fully paid equity shares of Rs. 10 each at Rs. 15 per share. This buyback is 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.

S.No.	PARTICULARS	Dr. Rs.	Cr. Rs.
1.	Bank A/c Dr. Profit and Loss A/c Dr. To Investment A/c (Being investment sold for the purpose of buy-back of Equity Shares)	25,00,000 5,00,000	30,00,000
2.	Bank A/c Dr. To 12% Pref. Share capital A/c (Being 12% Pref. Shares issued for Rs 20,00,000)	20,00,000	20,00,000
3.	Equity share capital A/c Dr. Premium payable on buy-back A/c Dr. To Equity shares buy-back A/c/ Equity shareholders A/c (Being the amount due on buy-back of equity shares)	50,00,000 25,00,000	75,00,000
4.	Equity shares buy-back A/c/ Equity shareholders A/c Dr. To Bank A/c (Being payment made for buy-back of equity shares)	75,00,000	75,00,000
5.	Securities Premium A/c Dr. General Reserve A/c Dr. To Premium payable on buy-back A/c (Being premium payable on buy-back charged from Securities premium)	15,00,000 10,00,000	25,00,000
6.	General Reserve A/c Dr. To Capital Redemption Reserve A/c (Being creation of capital redemption reserve to the extent of the equity shares bought back after deducting fresh pref. shares issued)	30,00,000	30,00,000

Q3. Buy Back (RTPMay'22) **REG. PAGE NO.**

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

S.No.	PARTICULARS	Dr. (Rs.)	Cr. (Rs.)
(a)	Equity shares buy-back account Dr. To Bank account (Being buy back of 25,000 equity shares of Rs 10 each @ Rs 15 per share)	3,75,000	 3,75,000
(b)	Equity share capital account Dr. Premium payable on buyback account Dr. To Equity shares buy-back account (Being cancellation of shares bought back)	2,50,000 1,25,000	 3,75,000
(c)	Securities premium account Dr. To Premium payable on buyback account (Being Premium payable on buyback adjusted against securities premium account)	1,25,000	 1,25,000
(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

PARTICULARS	Note No	AMOUNT (Lakhs)
EQUITY & LIABILITIES		
1. Shareholder's Funds		
a) Share Capital	1	11,00,000

b) Reserves & 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:

PARTICULARS		AMOUNT	AMOUNT
1. Share Capital			
Equity share capital			
1,10,000 Equity shares of Rs10 each			11,00,000
2. Reserves & 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	
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

Q4. Advanced Question (RTP Nov'21, ICAI New Nov 2019) **REG. PAGE NO.**

Rohan Ltd. furnishes the following information as on 31st March 2021:

PARTICULARS	AMOUNT	AMOUNT
Share Capital		
Equity Share of Rs. 20 each fully paid up	50,00,000	
6% Red. Pref. Share of Rs. 50 each fully paid up	10,00,000	60,00,000
Reserves & Surplus		
Capital Reserve	1,00,000	
Securities Premium	12,00,000	
Revenue Reserve	5,00,000	
Profit & Loss	25,50,000	43,50,000
12% Debentures		12,50,000
Current Liabilities & Provisions		5,50,000
Property, Plant & Equipment		1,00,75,000
Investments	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

S.No.	PARTICULARS	Dr. (Rs.)	Cr. (Rs.)
1.	Bank A/c Dr. To 14 % Debenture A/c To Securities Premium A/c (Being 14 % debentures issued to finance buy back)	3,60,000	 3,00,000 60,000
2.	Bank A/c Dr. To 10% preference share capital A/c (Being 10% preference share issued to finance buy back)	2,50,000	 2,50,000
3.	Bank A/c Dr. To Investment A/c To Profit on sale of investment (Being investment sold on profit)	1,50,000	 1,00,000 50,000
4.	Equity share capital A/c (62,500 x Rs20) Dr. Premium on buyback or Securities premium A/c Dr. (62,500 x Rs16) To Equity shares buy back A/c (62,500 x Rs36) (Being the amount due to equity shareholders on buy back)	12,50,000 10,00,000	 22,50,000
5.	Equity shares buy back A/c Dr. To Bank A/c (Being the payment made on account of buy back of 62,500 Equity Shares as per the Companies Act)	22,50,000	 22,50,000
6.	Revenue reserve A/c Dr. Securities premium A/c Dr. Profit and Loss A/c Dr. To Capital redemption reserve A/c (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]	3,00,000 2,60,000 4,40,000	 10,00,000
7	Capital redemption reserve A/c Dr. To Bonus shares A/c (Being the utilization of capital redemption reserve to issue 37,500 bonus shares)	7,50,000	 7,50,000
8	Bonus shares A/c Dr. To Equity share capital A/c (Being issue of 3 bonus equity share for every 15equity shares held)	7,50,000	 7,50,000

Q5. Basic Question (ICAI New May 2018) **REG. PAGE NO.**

Alpha Ltd. furnishes the following summarized Balance Sheet as at 31st March, 2017:

PARTICULARS	NOTE REF.	AMOUNT (Rs. In Lakhs)
I. EQUITY & LIABILITIES		
1. Shareholder's Funds		
(A) Share Capital	1	2,400
(B) Reserves & Suplus	2	1,620
2. Non Current Liabilities		
Long Term Borrowings	3	1,500
3. Current Liabilities		
Trade Payables		1,490
Other current Liabilites		390
TOTAL		**7,400**
II. ASSETS		
1. Non-Current Assets		
Fixed Assets		4,052
2. Current Assets		
(A) Current Investments		148
(B) Inventories		1,200
(C) Trade Receivables		520
(D) Cash & Bank		1,480
TOTAL		**7,400**

Notes to Accounts:

PARTICULARS	AMOUNT
1. Share Capital	
Authorized, Issued & Subscribed Share Capital	
Equity share capital (fully paid up shares of Rs. 10 each)	2,400
TOTAL	**2,400**
2. Reserves & Surplus	
Securities Premium	350
General Reserve	530
Capital Redemption Reserve	400
Profit and Loss Account	340
TOTAL	**1,620**
3. Long Term Borrowings	
12% Debentures	1,500
TOTAL	**1,500**

(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

In Lakhs

Date	Particulars		Dr.	Cr.
April 1	Bank A/c	Dr.	150	
	To Investment A/c			148
	To Profit on sale of investment			2
	(Being investment sold on profit)			
April 10	Equity share capital A/c	Dr.	600	

	Securities premium A/c Dr. To Equity shares buy back A/c (Being the amount due to equity shareholders on buy back)	300	900
	Equity shares buy back A/c Dr. To Bank A/c (Being the payment made on account of buy back of 60 Lakh Equity Shares)	900	900
April 10	General reserve A/c Dr. Profit and Loss A/c Dr. To Capital redemption reserve (CRR) A/c (Being amount equal to nominal value of buy back shares from free reserves transferred to capital redemption reserve account as per the law)	530 70	 600
April 30	Capital redemption reserve A/c Dr. To Bonus shares A/c (W.N.1) (Being the utilization of capital redemption reserve to issue bonus shares)	450	450
	Bonus shares A/c Dr. To Equity share capital A/c (Being issue of one bonus equity share for every four equity shares held)	450	450
	Profit on sale of Investment Dr. To Profit and Loss A/c (Profit on sale transfer to Profit and Loss A/c)	2	2

Q6. Basic Question (ICAI New May 2019) **REG. PAGE NO.**

Following is the summarized Balance Sheet of Super Ltd. as on 31st March, 2018

PARTICULARS	NOTE REF.	AMOUNT (Rs.)
I. EQUITY & LIABILITIES		
1. Shareholder's Funds		
(A) Share Capital	1	17,00,000
(B) Reserves & Suplus	2	29,50,000
2. Non Current Liabilities		
Long Term Borrowings	3	46,50,000
TOTAL		**93,00,000**
II. ASSETS		
1. Non-Current Assets		
Fixed Assets		58,50,000
2. Current Assets		
Current Assets		34,50,000
TOTAL		**93,00,000**

Notes to Accounts:

PARTICULARS	AMOUNT
1. Share Capital	
Authorized, Issued & Subscribed Share Capital	
Equity Shares of Rs. 10 each fully paid up	17,00,000
TOTAL	**17,00,000**
2. Reserves & Surplus	
Revenue Reserve	23,50,000
Securities Premium	2,50,000
Profit and Loss Account	2,00,000
Infrastructure Development Reserve	1,50,000
TOTAL	**29,50,000**
3. Long Term Borrowings	

9% Debentures	22,50,000
Unsecured Loans	8,50,000
Current Maturities of Long Term Borrowings	15,50,000
TOTAL	**46,50,000**

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, whether 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	17,00,000
Free reserves	28,00,000
Shareholders' funds	**45,00,000**
25% of Shareholders fund	11,25,000
Buy-back price per share	30
Number of shares that can be bought back	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 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

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)

(y/30 × 10) = x Or 3x = y (2)

by solving the above equation, we get

x = Rs 5,43,750

y = Rs 16,31,250

Q7. Basic Question (ICAI New Nov 2022) **REG. PAGE NO.**

PG Limited furnishes the following Balance Sheet as at 31st March,2022:

PARTICULARS	NOTE REF.	AMOUNT (Rs. In Lakhs)
I. EQUITY & LIABILITIES		
1. Shareholder's Funds		
(A) Share Capital	1	12,000
(B) Reserves & Suplus	2	8,100
2. Current Liabilities		
Trade Payables		7,450
Other current Liabilites		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 & cash Equivalents		7,400
TOTAL		**29,500**

Notes to Accounts:

PARTICULARS	AMOUNT (Rs.In Lakhs)
1. Share Capital	
Authorized, Issued & Subscribed Share Capital	
Equity share capital (fully paid up shares of Rs. 10 each)	12,000
TOTAL	**12,000**
2. Reserves & Surplus	
Securities Premium	1,750
General Reserve	2,650
Capital Redemption Reserve	2,000
Profit and Loss Account	1,700
TOTAL	**8,100**

On 1stApril, 2022, the company announced the buy-back of 25% of its Equity Shares @ Rs. 15 per share. For this purpose, it sold all of is investments for Rs. 750 lakhs.

On 5thApril, 2022, the company achieved the target of buy-back You are required to pass necessary journal entries for the above transactions.

Solution:-

In the books of PG Limited
Journal Entries

In Lakhs

Date	Particulars		Dr.	Cr.
April 1	Bank A/c	Dr.	750	
	To Investment A/c			740
	To Profit on sale of investment			10
	(Being investment sold on profit)			
April 5	Equity share capital A/c	Dr.	3000	
	Premium payable on buy-back A/c	Dr.	1500	

	To Equity shares buy back A/c (Being the amount due to equity shareholders on buy back)		4500
	Securities Premium A/c Dr. To Premium payable on buy-back A/c (Being the amount of premium charged from securities premium account)	1,500	1,500
	Equity shares buy back A/c Dr. To Bank A/c (Being the payment made on account of buy back of 60 Lakh Equity Shares)	4500	4500
April 5	General reserve A/c Dr. Profit and Loss A/c Dr. To Capital redemption reserve (CRR) A/c (Being amount equal to nominal value of buy back shares from free reserves transferred to capital redemption reserve account as per the law)	1300 1700	3000

Note:

1. In the last entry given in the solution, it is possible to adjust transfer to Capital Redemption Reserve Account from different combinations of amounts from Securities Premium, General Reserve and Profit and Loss Account to the extent available.
2. Calculation of amount of Buy Back of Share: Rs12,000/10 X 25% X Rs 15 = Rs 4,500 Lakhs

Q8. Buy Back (RTPNov'18) **REG. PAGE NO.**

The following summarized Balance Sheet Pee Limited (a non-listed company) furnishes as at 31st March,2017.

PARTICULARS	AMOUNT	
Equity & Liabilities		
Share capital:		
Authorised capital		
2,50,000 Equity shares of Rs. 10 each fully paid up	25,00,000	
5,000, 10% Preference shares of Rs. 100 each	5,00,000	30,00,000
Issued and subscribed capital:		
2,40,000 Equity shares of Rs. 10 each fully paid up	24,00,000	
3,000, 10% Preference shares of Rs. 100 each (Issued two months back for the purpose of buy back)	3,00,000	27,00,000
Reserves & Surplus		
Capital Reserve	10,00,000	
Revenue Reserve	25,00,000	
Securities Premium	27,00,000	
Profit & Loss	35,00,000	97,00,000
Current Liabilities		
Trade Payables	13,00,000	
Other current Liabilities	3,00,000	16,00,000
TOTAL		**1,40,00,000**
Assets		
Tangible Assets		
Building	25,00,000	
Machinery	31,00,000	
Furniture	20,00,000	76,00,000
Non-current Investments		30,00,000
Current Assets		
Inventory	12,00,000	
Trade Receivables	7,00,000	
Cash and Bank balance	15,00,000	34,00,000
TOTAL		**1,40,00,000**

On 1st April, 2017, the company passed a resolution to buy back 20% of its equity capital @ Rs. 60 per share. For this purpose, it sold all of its investment for Rs. 25,00,000. The company achieved its target of buy-back. You are required to:
(a) Give necessary journal entries and
(b) Give the Balance Sheet of the company after buy back of shares.

Solution:-

In the books of Pee Ltd.
Journal Entries

Date	PARTICULARS		Dr. (Rs.)	Cr. (Rs.)
1	Bank A/c Profit on sale of investment To Investment A/c (Being investment sold on profit)	Dr. Dr.	25,00,000 5,00,000	 30,00,000
2	Equity share capital A/c Premium payable on buy-back A/c To Equity shares buy back A/c (Being the amount due to equity shareholders on buy back)	Dr. Dr.	4,80,000 24,00,000	 28,80,000
3	Securities Premium A/c To Premium payable on buy-back A/c (Being the amount of premium charged from securities premium account)	Dr.	24,00,000	 24,00,000
4	Equity shares buy back A/c To Bank A/c (Being the payment made on account of buy back of 60 Lakh Equity Shares)	Dr.	28,80,000	 28,80,000
April 5	Revenue reserve A/c To Capital redemption reserve (CRR) A/c (Being amount equal to nominal value of buy back shares from free reserves transferred to capital redemption reserve account as per the law)	Dr.	1,80,000	 1,80,000

Balance Sheet of Pee Limited as on 1st April, 2017
(After buy back of shares)

PARTICULARS	NOTE REF.	AMOUNT (Rs. In Lakhs)
I. EQUITY & LIABILITIES		
1. Shareholder's Funds		
(A) Share Capital	1	22,20,000
(B) Reserves & Suplus	2	68,00,000
2. Current Liabilities		16,00,000
TOTAL		**1,06,20,000**
II. ASSETS		
1. Non-Current Assets		
(A) Fixed Assets		76,00,000
2. Current Assets		30,20,000
TOTAL		**1,06,20,000**

Notes to Accounts:

PARTICULARS		AMOUNT
1. Share Capital		
Authorized Capital		30,00,000
1,92,000 Equity share capital(fully paidup shares of Rs.10 each)	1,92,000	
3,000 10% Preference shares of Rs 100 each fully paid up	3,00,000	22,20,000
Reconciliation of share capital		

Opening no. of shares		2,40,000	
Buy back of shares during the year		48,000	1,92,000
During the year the company has buy back of 48,000 shares			
2. Reserves & Surplus			
Capital reserve		10,00,000	
Capital redemption reserve		1,80,000	
Securities Premium	27,00,000		
Less: Premium payable on buy back of shares	24,00,000	3,00,000	
Revenue reserve	25,00,000		
Less: Transfer to Capital redemption reserve	1,80,000	23,20,000	
Profit and loss A/c	35,00,000		
Less: Loss on investment	5,00,000	30,00,000	68,00,000

Q9. Buy Back (RTPNov'19 N22) REG. PAGE NO.

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:-

In the books of Umesh Ltd.
Journal Entries

S.No.	PARTICULARS	Dr. (Rs.)	Cr. (Rs.)
1.	Bank A/c Dr. To 11% Preference share application & allotment A/c (Being receipt of application money on preference shares)	10,00,000	 10,00,000
2.	11% Preference share application & allotment A/c Dr. To 11% Preference share capital A/c (Being allotment of 1 lakh preference shares)	10,00,000	 10,00,000
3.	General reserve A/c Dr. To Capital redemption reserve A/c (Being creation of capital redemption reserve for buy back of shares)	30,00,000	 30,00,000
4.	Equity share capital A/c Dr. Premium payable on buyback A/c Dr. To Equity shareholders/Equity shares buy back A/c (Amount payable to equity shareholder on buy back)	40,00,000 48,00,000	 88,00,000
5.	Equity shareholders/ Equity shares buy back A/c Dr. To Bank A/c (Being payment made for buy back of shares)	88,00,000	 88,00,000
6.	Securities Premium A/c Dr. General reserve A/c 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

PARTICULARS	AMOUNT (Rs.In Lakhs)
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 Rs10)		(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

PARTICULARS	AMOUNT (Rs.In Lakhs)
Nominal value of shares bought back (4,00,000 shares x Rs10)	40,00,000
Less: Nominal value of Preference Shares issued for such buy back (1,00,000 shares x Rs10)	(10,00,000)
Amount transferred to Capital Redemption Reserve Account	**30,00,000**

Q10. Buy Back (RTPMay'21) **REG. PAGE NO.**

M/s. Vriddhi Infra Ltd. (a non-listed company) provide the following information as on 31.3.2020:

PARTICULARS	AMOUNT
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 and Loss Account (Surplus)	1,50,000
10% Debentures (Secured by floating charge on all assets)	20,00,000
Unsecured Loans	8,00,000
Trade 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	PARTICULARS		Dr.	Cr.
2020			₹	₹
April 21	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)			
April 25	Equity share capital A/c	Dr.	1,50,000	
	Securities premium A/c	Dr.	75,000	
	To Equity shares buy back A/c			2,25,000
	(Being the amount due to equity shareholders on buy back)			

	Equity shares buy back A/c Dr. To Bank A/c (Being the payment made on account of buy back of 15,000 Equity Shares)	2,25,000	2,25,000
	General reserve A/c or P&L A/c Dr. To Capital redemption reserve (CRR) A/c (Being amount equal to nominal value of buy back shares from free reserves transferred to capital redemption reserve account as per the law)	1,50,000	1,50,000
May 1	Capital redemption reserve A/c Dr. To Bonus shares A/c (W.N.1) (Being the utilization of capital redemption reserve to issue bonus shares)	1,06,250	1,06,250
	Bonus shares A/c Dr. To Equity share capital A/c (Being issue of one bonus equity share for every ten equity shares held)	1,06,250	1,06,250

Working Note:

Amount of bonus shares = [(1,00,000 - 15,000) ×1/8] × 10

= Rs 1,06,250

CHAPTER – 5

FINANCIAL STATEMENTS OF A COMPANY

Q1. Complete Financial Statements (RTP M19) REG. PAGE NO.

Swetha Ltd. has an authorized share capital of Rs. 15,00,000 consisting of 6,000 6% Preference Shares of Rs. 100 each and 90,000 Equity Shares of Rs. 10 each. The following was the Trial Balance of the company as on 31st March 2018:

PARTICULARS	DR. (Rs.)	CR. (Rs.)
Investment in Shares (at Cost)	1,50,000	
Purchases	14,71,500	
Selling Expenses	2,37,300	
Inventory as at the Beginning of the year	4,35,600	
Salaries and Wages	1,56,000	
Cash on Hand	36,000	
Interim Preference Dividend for the Half year to 30th September	18,000	
Bills Receivables	1,24,500	
Interest on Bank Overdraft	29,400	
Interest on Debentures for the Half year up to 30th September	11,250	
Debtors	1,50,300	
Trade Payables		2,63,550
Freehold Property at Cost	10,50,000	
Furniture at cost less depreciation of Rs. 45,000	1,05,000	
6% Preference Share Capital		6,00,000
Equity Share Capital fully paid up		6,00,000
5% Mortgaged Debentures secured on Freehold Properties		4,50,000
Income Tax paid in Advance for the current year	30,000	
Dividends		12,750
Profit & Loss A/c (Opening Balance)		85,500
Sales (Net)		20,11,050
Bank Overdraft secured by Hypothecation of stocks & receivables		4,50,000
Technical know-how fees at cost paid during the year	4,50,000	
Audit Fees	18,000	
TOTAL	**44,72,850**	**44,72,850**

You are required to prepare the Profit and Loss Statement for the year ended 31st March, 2018 and the Balance Sheet as on 31st March, 2018 as per Schedule III of the Companies Act, 2013 after taking into account the following –

1. Closing Stock was valued at Rs. 4,27,500.
2. Purchases include Rs. 15,000 worth of goods and articles distributed among valued customers.
3. Salaries and Wages include Rs. 6,000 being Wages incurred for installation of Electrical Fittings which were recorded under "Furniture".
4. Bills Receivable include Rs.4,500 being dishonoured bills. 50% of which had been considered irrecoverable.
5. Bills Receivable of Rs. 6,000 maturing after 31st March were discounted.
6. Depreciation on Furniture to be charged at 10% on Written Down Value.
7. Investment in shares is to be treated as non-current investments.
8. Interest on Debentures for the half year ending on 31st March was due on that date.
9. Provide Provision for taxation Rs. 12,000.
10. Technical Knowhow Fees is to be written off over a period of 10 years.
11. Salaries and Wages include Rs. 30,000 being Director's Remuneration.
12. Trade receivables include Rs. 18,000 due for more than six months.

Solution:- Statement of Profit and Loss of Shweta Ltd. for the year ended 31st March, 2018

	PARTICULARS	NOTE REF	Rs. (Rs.)
I	Revenue from Operations		20,11,050
II	Other income (Divided income)		12,750
III	Total Revenue (I &+ II)		20,23,800
IV	Expenses:		
	(a) Purchases (14,71,500 – Advertisement Expenses 15,000)		14,56,500
	(b) Changes in Inventories of finished Goods / Work in progress (4,35,600 – 4,27,500)		8,100
	(c) Employee Benefits expense	9	1,20,000
	(d) Finance costs	10	51,900
	(e) Depreciation & Amortization Expenses [10% of (1,05,000 + 6,000)]		11,100
	(f) Other Expenses	11	3,47,550
	Total Expenses		19,95,150
V	Profit before exceptional, extraordinary items and tax (III-IV)		28,650
VI	Exceptional items		-
VII	Profit before extra ordinary items and tax (V-IV)		28,650
VIII	Extraordinary items		-
IX	Profit before tax (VII-VIII)		28,650
X	Tax expense:		
	Current Tax		12,000
XI	Profit/Loss for the period (after tax)		16,650

Balance sheet of Shweta Ltd. as on 31 st March, 2018

	PARTICULARS as on 31st March	NOTE REF	Rs.
I	**EQUITY&LIABILITIES**		
(1)	**Shareholders' funds:**		
	(a) Share capital	1	12,00,000
	(b) Reserves and surplus	2	66,150
(2)	**Non current liabilities:**		
	Long term borrowings	3	4,50,000
(3)	**Current liabilities:**		
	(a) Short term borrowings	4	4,50,000
	(b) Trade payables		2,63,550
	(c) Other current liabilities	5	29,250
	TOTAL		**24,58,950**
II	**ASSETS**		
(1)	**Non-current Assets**		
	(a) Property, Plant & Equipment		
	(i) Tangible assets	6	11,49,900
	(ii) Intangible assets	7	4,05,000
	(b) Non current investments (Shares at cost)		1,50,000
(2)	**Current Assets:**		
	(a) Inventories		4,27,500
	(b) Trade receivables	8	2,72,550
	(c) Cash and Cash equivalents – Cash on hand		36,000
	(d) Short term loans and advances –Income tax (paid 30,000-Provision 12,000)		18,000
	TOTAL		**24,58,950**

Note: There is a Contingent liability for Bills receivable discounted with Bank Rs. 6,000.

Notes to accounts

			Rs.
1.	**Share Capital**		
	Authorized		
	90,000 Equity Shares of Rs. 10 each	9,00,000	
	6,000 6% Preference shares of Rs. 100 each	6,00,000	15,00,000
	Issued, subscribed & called up		
	60,000, Equity Shares of Rs. 10 each	6,00,000	
	6,000 6% Redeemable Preference Shares of 100 each	6,00,000	12,00,000
2.	**Reserves and Surplus**		
	Balance as on 1st April, 2017	85,500	
	Add: Surplus for current year	16,650	1,02,150
	Less: Preference Dividend		36,000
	Balance as on 31st March, 2018		66,150
3.	**Long Term Borrowings**		
	5% Mortgage Debentures (Secured against Freehold Properties)		4,50,000
4.	**Short Term Borrowings**		
	Secured Borrowings: Loans Repayable on Demand Overdraft from Banks (Secured by Hypothecation of Stocks & Receivables)		4,50,000
5.	**Other Current liabilities**		
	Interest Accrued and due on Borrowings (5% Debentures)	11,250	
	Unpaid Preference Dividends	18,000	29,250
6.	**Tangible Fixed assets**		
	Furniture		
	Furniture at Cost Less depreciation Rs. 45,000 (as given in Trial Balance	1,05,000	
	Add: Depreciation	45,000	
	Cost of Furniture	1,50,000	
	Add: Installation charge of Electrical Fittings wrongly included under the heading Salaries and Wages	6,000	
	TOTAL Gross block of Furniture A/c	1,56,000	
	Accumulated Depreciation Account: Opening Balance-given in Trial Balance 45,000		
	Depreciation for the year:		
	On Opening WDV at 10% i.e. (10% x 1,05,000) 10,500		
	On additional purchase during the year at 10% i.e. (10% x 6,000) 600		
	Less: Accumulated Depreciation	56,100	99,900
	Freehold property (at cost)		10,50,000
			11,49,900
7.	**Intangible Fixed Assets**		
	Technical knowhow	4,50,000	
	Less: Written off	45,000	4,05,000
8.	**Trade Receivables**		
	Sundry Debtors (a) Debt outstanding for more than six months	18,000	
	(b) Other Debts (refer Working Note)	1,34,550	
	Bills Receivable (1,24,500 -4,500)	1,20,000	2,72,550
9.	**Employee benefit expenses**		
	Amount as per Trial Balance	1,56,000	
	Less: Wages incurred for installation of electrical		

	fittings to be capitalized	6,000	
	Less: Directors' Remuneration shown separately	30,000	
	Balance amount		1,20,000
10.	**Finance Costs**		
	Interest on bank overdraft	29,400	
	Interest on debentures	22,500	51,900
11.	**Other Expenses**		
	Payment to the auditors	18,000	
	Director's remuneration	30,000	
	Selling expenses	2,37,300	
	Technical knowhow written of (4,50,000/10)	45,000	
	Advertisement (Goods and Articles Distributed)	15,000	
	Bad Debts (4,500 x50%)	2,250	3,47,550

Working Note

Calculation of Sundry Debtors-Other Debts

Sundry Debtors as given in Trial Balance	1,50,300
Add Back: Bills Receivables Dishonoured	4,500
	1,54,800
Less: Bad Debts written off – 50% Rs. 4,500	(2,250)
Adjusted Sundry Debtors	1,52,550
Less: Debts due for more than 6 months (as per information given	(18,000)
TOTAL of other Debtors i.e. Debtors outstanding for less than 6 months	1,34,550

Q2. Complete Financial Statements (RTP N19) **REG. PAGE NO.**

The following balances appeared in the books of Oliva Company Ltd. as on 31st March 2019.

PARTICULARS	DR.	PARTICULARS	CR.
Inventory on 01-04-18		Sales	17,10,000
Raw Material 30,000		Interest	3,900
Finished Good 46,500	76,500	Profit & Loss A/c	48,000
Purchases	12,15,000	Share Capital	3,15,000
Manufacturing Expenses	2,70,000	Secured Loans -	
Salaries & Wages	40,200	Short Term 4,500	
General Charges	16,500	Long Term 21,000	45,500
Interim Dividend paid (Incl. DDT)	27,000	Fixed Deposit (Unsecured) -	
Building	1,01,000	Short Term 1,500	
Plant & Machinery	70,400	Long Term 3,300	4,800
Furniture	10,200	Trade Payables	3,27,000
Motor Vehicles	40,800		
Stores & Spare Parts Consumed	45,000		
Investments -			
Current 4,500			
Non-Current 7,500	12,000		
Trade Receivables	2,38,500		
Cash in Bank	2,71,100		
TOTAL	**24,34,200**	**TOTAL**	**24,34,200**

From the above balance and the following information, prepare the company's Profit and Loss Account for the year ended 31st March, 2019 and Company's Balance Sheet as on that date:

1.Inventoryon 31st March, 2019 Raw material Rs. 25,800 & finished goods Rs. 60,000.
2.Outstanding Expenses: Manufacturing Expenses Rs. 67,500& Salaries & Wages Rs. 4,500.
3.Interest accrued on Securities Rs. 300.
4.General Charges prepaid Rs. 2,490.
5.Depreciate Building @ 2% p.a., Machinery @ 10% p.a., Furniture @ 10% p.a. & Motor Vehicles @ 20%p.a.
6. Current maturity of long term loan is Rs. 1,000.

7. The taxation provision of 40% on Net Profit is considered.

Solution:-

Oliva Company Ltd.
Statement of Profit and loss for the year ended 31.03.2019

	PARTICULARS	NOTE REF	Rs.
I	Revenue from Operations		17,10,000
II	Other income (3,900 +300)		4,200
III	Total Revenue (I &+ II)		17,14,200
IV	Expenses:		
	Cost of materials consumed	10	12,64,200
	Purchases of inventory-in-trade		-
	Changes in inventories of finished goods, work-in-progress and inventory-in-Trade	11	(13,500)
	Employee benefit expenses	12	44,700
	Finance costs		-
	Depreciation and amortization expenses		18,240
	Other expenses	13	3,51,510
	Total Expenses		16,65,150
V	Profit before exceptional, extraordinary items and tax		49,050
VI	Exceptional items		-
VII	Profit before extra ordinary items and tax		49,050
VIII	Extraordinary items		-
IX	Profit before tax (VII-VIII)		49,050
X	Tax expense: (40% of 49,050)		19,620
XI	Profit/Loss for the period (after tax)		29,430

Oliva Company Ltd.
Balance Sheet for the year ended 31.03.2019

	PARTICULARS as on 31st March	NOTE REF	Rs.
I	**EQUITY&LIABILITIES**		
(1)	**Shareholders' funds:**		
	(a) Share capital		3,15,000
	(b) Reserves and surplus	1	50,430
(2)	**Non current liabilities:**		
	Long term borrowings	2	23,300
(3)	**Current liabilities:**		
	(a) Short term borrowings	3	6,000
	(b) Trade payables		3,27,000
	(c) Other current liabilities	4	73,000
	(d) Short term provision	5	19,620
	TOTAL		**8,14,350**
II	**ASSETS**		
(1)	**Non-current Assets**		
	(a) Property, Plant & Equipment		
	(i) Tangible assets	6	2,04,160
	(b) Non current investments (Shares at cost)		7,500
(2)	**Current Assets:**		
	(a) Current Investments		4,500
	(b) Inventories	7	85,800
	(c) Trade receivables		2,38,500
	(d) Cash and Cash equivalents – Cash on hand		2,71,100
	(e) Short term loans and advances	8	2,490
	(f) Other current assets	9	300
	TOTAL		**8,14,350**

Notes to accounts

				Rs.
1.	**Reserve & Surplus**			
	Profit & Loss Account: Balance b/f		48,000	
	Net Profit for the year		(27,000)	
	Less: Interim Dividend including DDT		(27,000)	50,430
2.	**Long term borrowings**			
	Secured loans (21,000 less current maturities 1,000)		20,000	
	Fixed Deposits: Unsecured		3,300	23,300
3.	**Short term borrowings**			
	Secured loans		4,500	
	Fixed Deposits -Unsecured		1,500	6,000
4.	**Other current liabilities**			
	Expenses Payable (67,500 + 4,500)		72,000	
	Current maturities of long term borrowings		1,000	73,000
5.	**Short term provisions**			
	Provision for Income tax			19,620
6.	**Tangible Assets**			
	Building	1,01,000		
	Less: Depreciation @ 2%	(2,020)	98,980	
	Plant & Machinery	70,400		
	Less: Depreciation @10%	(7,040)	63,360	
	Furniture	10,200		
	Less: Depreciation @10%	(1,020)	9,180	
	Motor vehicles	40,800		
	Less: Depreciation @20%	(8,160)	32,640	2,04,160
7.	**Inventory:**			
	Raw Material		25,800	
	Finished goods		60,000	85,800
8.	**Short term Loans & Advances**			
	General Charges prepaid			2,490
9.	**Other Current Assets:**			
	Interest accrued			300
10.	**Cost of material consumed**			
	Opening inventory of raw Material & Stores	30,000		
	Add: Purchases	12,15,000		
	Add: Stores & Spare parts consumed	45,000	12,90,000	
	Less: Closing inventory		(25,800)	12,64,200
11.	**Changes in inventory of Finished Goods & WIP**			
	Closing Inventory of Finished Goods		60,000	
	Less: Opening Inventory of Finished Goods		46,500	13,500
12.	**Employee Benefit expenses**			
	Salary & Wages (40,200 + 4,500)			44,700
13.	**Other Expenses:**			
	Manufacturing Expenses (2,70,000 + 67,500)		3,37,500	
	General Charges (16,500 – 2,490)		14,010	3,51,510

Q3. Complete Financial Statements (RTP N20) **REG. PAGE NO.**

On 31st March, 2020, Om Ltd. provides to you the following ledger balances after preparing its Profit and Loss Account for the year ended 31st March, 2020:

Credit Balances

	Rs.
Equity shares capital (fully paid shares of Rs. 10 each)	1,05,00,000
General Reserve	21,84,000
Loan from State Finance Corporation	15,75,000
(Secured by hypothecation of Plant & Machinery – Repayable within one year Rs. 3,00,000)	
Loans: Unsecured (Long term)	12,70,500
Sundry Creditors for goods & expenses	
(Payable within 6 months)	21,00,000
Profit & Loss Account	10,50,000
Provision for Taxation	12,25,350
	199,04,850

Debit Balances :

	Rs.
Calls in arrear	10,500
Land	21,00,000
Buildings	30,75,000
Plant and Machinery	55,12,500
Furniture & Fixture	5,25,000
Inventories : Finished goods	21,00,000
Raw Materials	5,25,000
Trade Receivables	21,00,000
Advances: Short-term	4,48,350
Cash in hand	3,15,000
Balances with banks	25,93,500
Patents & Trade marks	6,00,000
	199,04,850

The following additional information is also provided in respect of the above balances:

(i) 6,30,000 fully paid equity shares were allotted as consideration for land & buildings.

(ii) Cost of Building Rs. 42,00,000

Cost of Plant & Machinery Rs. 73,50,000

Cost of Furniture & Fixture Rs. 6,56,250

(iii) Trade receivables for Rs. 5,70,000 are due for more than 6 months.

(iv) The amount of Balances with Bank includes Rs. 27,000 with a bank which is not a scheduled Bank and the deposits of Rs. 7,50,000 are for a period of 9 months.

(v) Unsecured loan includes Rs. 3,00,000 from a Bank and Rs. 1,50,000 from related parties.

You are not required to give previous year figures. You are required to prepare the Balance Sheet of the Company as on 31st March, 2020 as required under Schedule III of the Companies Act, 2013.

Solution:-

Om Ltd.

Balance Sheet as on 31st March, 2020

	PARTICULARS as on 31st March	NOTE	Figures at the end of current reporting period
I	**EQUITY&LIABILITIES**		
(1)	**Shareholders' funds:**		
	(a) Share capital	1	1,04,89,500
	(b) Reserves and surplus	2	32,34,000
(2)	**Non current liabilities:**		
	Long term borrowings	3	25,45,500
(3)	**Current liabilities:**		
	(a) Trade payables		21,00,000
	(b) Other current liabilities	4	3,00,000
	(c) Short term provision	5	12,25,350

	TOTAL		**1,98,94,350**
II	**ASSETS**		
(1)	**Non-current Assets**		
	(a) Property, Plant & Equipment	6	1,12,12,500
	(b) Intangible assets (Patents & Trade Marks)		6,00,000
(2)	**Current Assets:**		
	(a) Inventories	7	26,25,000
	(b) Trade receivables	8	21,00,000
	(c) Cash and Cash equivalents – Cash on hand	9	29,08,500
	(d) Short term loans and advances		4,48,350
	TOTAL		**1,98,94,350**

Notes to accounts

			Rs.
1.	**Share Capital**		
	Equity share capital		
	Issued, subscribed and called up		
	10,50,000 Equity Shares of Rs. 10 each (Out of the above 6,30,000 shares have been issued for consideration other than cash)	1,05,00,000	
	Less: Calls in arrears	(10,500)	1,04,89,500
	TOTAL		**1,04,89,500**
2.	**Reserves and Surplus**		
	General Reserve		21,84,000
	Surplus (Profit & Loss A/c)		10,50,000
	TOTAL		**32,34,000**
3.	**Long-term borrowings**		
	Secured		
	Term Loans		
	Loan from State Finance Corporation (Rs. 15,75,000 less Rs. 3,00,000) (Secured by hypothecation of Plant and Machinery)		12,75,000
	Unsecured		
	Bank Loan	3,00,000	
	Loan from related parties	1,50,000	
	Others	8,20,500	12,70,500
	TOTAL		**25,45,500**
4.	**Other current liabilities**		
	Loan Instalment repayable within one Year		**3,00,000**
5.	**Short-term provisions**		
	Provision for taxation		**12,25,350**
6.	**Property, Plant and Equipment**		
	Land		21,00,000
	Buildings	42,00,000	
	Less: Depreciation	(11,25,000)	30,75,000
	Plant & Machinery	73,50,000	
	Less: Depreciation	(18,37,500)	55,12,500
	Furniture & Fittings	6,56,250	
	Less: Depreciation	(1,31,250)	5,25,000
	TOTAL		**1,12,12,500**
7.	**Inventories**		
	Raw Material		5,25,000
	Finished goods		21,00,000
	TOTAL		**26,25,000**
8.	**Trade receivables**		

	Debts outstanding for a period exceeding six months		5,70,000
	Other Debts		15,30,000
	TOTAL		**21,00,000**
9.	**Cash and cash equivalents**		
	Cash at bank with Scheduled Banks including Bank deposits for period of 9 months amounting Rs. 7,50,000	25,66,500	
	with others	27,000	25,93,500
	Cash in hand		3,15,000
	TOTAL		**29,08,500**

Q4. Complete Financial Statements (RTP M18,RTP M21) REG. PAGE NO.

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

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

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

Charge depreciation on closing written down amount of Plant & Machinery @ 5%, Engineering Tools @ 20%; Patterns @ 10%; and Furniture & Fixtures @10%. Provide 25,000 as doubtful debts after writing off Rs.16,000 as bad debts. Provide for income tax @ 30%. Corporate Dividend Tax Rate @ 17.304 (wherein Base Rate is 15%).

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

Solution:-

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

	PARTICULARS as on 31st March	NOTE REF	Rs.
I	**EQUITY&LIABILITIES**		
(1)	**Shareholders' funds:**		
	(a) Share capital	1	19,90,000
	(b) Reserves and surplus	2	59,586
(2)	**Current liabilities:**		
	(a) Trade payables		2,40,500
	(b) Other current liabilities	3	13,28,000
	(c) Short term provision	4	4,07,414
	TOTAL		**40,25,500**
II	**ASSETS**		

(1)	**Non-current Assets**		
	(a) Property, Plant & Equipment		
	(i) Tangible assets	5	29,30,000
(2)	**Current Assets:**		
	(a) Inventories		7,08,000
	(b) Trade receivables	6	3,59,500
	(c) Cash and Cash equivalents	7	28,000
	TOTAL		**40,25,500**

Kapil Ltd.

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

	PARTICULARS	**NOTE REF**	**Rs.**
I	Revenue from Operations		36,17,000
II	Other income	8	36,500
III	Total Revenue (I &+ II)		36,53,500
IV	Expenses:		
	Cost of purchases		12,32,500
	Changes in Inventories [6,65,000-7,08,000]		(43,000)
	Employee benefit expenses	9	13,93,000
	Finance costs	10	1,11,000
	Depreciation and amortization expenses		1,20,000
	Other expenses	11	4,40,000
	Total Expenses		32,53,500
V	Profit before tax (III-IV)		4,00,000
VI	Tax expense: @ 30%		(1,20,000)
VII	Profit/Loss for the period (after tax)		2,80,000

Notes to Accounts:

1. Share Capital

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

2. Reserves and Surplus

General Reserve		7,000
Surplus i.e. Balance in Statement of Profit & Loss:		
Opening Balance	67,000	
Add: Profit for the period	2,80,000	
Less: Transfer to Reserve @ 2.5%	(7,000)	
Less: Equity Dividend [12% of (20,00,000-10,000)]	(2,38,800)	
Less: Corporate Dividend Tax (Working note)	(48,614)	52,586
	40,000	**59,586**

3. Other Current Liabilities

Bank Overdraft	12,67,000
Outstanding Expenses [25,000+36,000]	61,000
	13,28,000

4. Short-term Provisions

Provision for Tax	1,20,000
Equity Dividend payable	2,38,800
Corporate Dividend Tax	48,614
	4,07,414

5. Tangible Assets

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

6. Trade Receivables

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

7. Cash & Cash Equivalent

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

8. Other Income

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

9. Employee benefits expenses

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

10. Finance Cost

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

11. Other Expenses

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

Working Note

Calculation of grossing-up of dividend:

	Rs.
Dividend distributed by Company	2,38,800
Add: Increase for the purpose of grossing up of dividend 2,38,800 x [15/(100-15)]	42,141
Gross dividend	2,80,941
Dividend distribution tax @ 17.304%	48,614

Q5. Complete Financial Statements (RTP N18) REG. PAGE NO.

You are required to prepare a Balance Sheet as at 31st March 2018, as per Schedule III of the Companies Act, 2013, from the following information of Mehar Ltd .

PARTICULARS	Rs.	PARTICULARS	Rs.
Term Loans (Secured)	40,00,000	Investments (Non- current)	9,00,000
Trade payables	45,80,000	Profit for the year	32,00,000
Other advances	14,88,000	Trade receivables	49,00,000
Cash and Bank Balances	38,40,000	Miscellaneous Expenses	2,32,000
Staff Advances	2,20,000	Loan from other parties	8,00,000

Provision for Taxation	10,20,000	Provision for Doubtful Debts	80,000
Securities Premium	19,00,000	Stores	16,00,000
Loose Tools	2,00,000	Fixed Assets (WDV)	2,26,00,000
General Reserve	62,00,000	Finished Goods	30,00,000
Capital Work-in- progress	8,00,000		

Additional Information:-

1. Share Capital consist of-

(a) 1,20,000 Equity Shares of Rs. 100 each fully paid up.

(b) 40,000, 10% Redeemable Preference Shares of Rs. 100 each fully paid up.

2. The company declared dividend @ 5% of equity share capital. The dividend distribution tax rate is 17.304%. (15% CDT, surcharge 12%, Education Cess 2% and SHEC @ 1%)

3. Depreciate Assets by Rs. 20,00,000

Solution:-

Balance Sheet of Mehar Ltd. as at 31st March, 2018

	PARTICULARS as on 31st March	NOTE REF	Rs.
I	**EQUITY&LIABILITIES**		
(1)	**Shareholders' funds:**		
	(a) Share capital	1	1,60,00,000
	(b) Reserves and surplus	2	98,64,424
(2)	Non-current Liabilities		
	Long term Borrowings- Terms Loans (Secured)		40,00,000
(3)	**Current liabilities:**		
	(a) Trade payables		45,80,000
	(b) Other current liabilities	3	20,03,576
	(c) Short term provision(Provision for taxation)		10,20,000
	TOTAL		**3,74,68,000**
II	**ASSETS**		
(1)	**Non-current Assets**		
	(a) Fixed Assets:		
	(i) Tangible assets	4	2,06,00,000
	(ii) Capital WIP		8,00,000
	(b) Non- current Investments		9,00,000
(2)	**Current Assets:**		
	(a) Inventories	5	48,00,000
	(b) Trade receivables	6	48,20,000
	(c) Cash and Cash equivalents		38,40,000
	(d) Short-term Loans and Advances	7	17,08,000
	TOTAL		**3,74,68,000**

Notes to accounts

			Rs.
1.	**Share Capital**		
	Authorized, issued, subscribed & called up		
	1,20,000, Equity Shares of Rs. 100 each	1,20,00,000	
	40,000 10% Redeemable Preference Shares of 100 each	40,00,000	**1,60,00,000**
2.	**Reserves and Surplus**		
	Securities Premium Account	19,00,000	
	General reserve	62,00,000	
	Profit & Loss Balance		
	Opening balance		
	Profit for the period 32,00,000		
	Less: Miscellaneous Expenditure written off (2,32,000)		

		29,68,000		
	Less: Appropriations			
	Dividend	(10,00,000)		
	Dividend distribution tax	(2,03,576)	17,64,424	**98,64,424**
3.	**Other current liabilities**			
	Loan from other parties		8,00,000	
	Dividend		10,00,000	
	Dividend Distribution tax [W.N]		2,03,576	**20,03,576**
4.	**Tangible assets**			
	Fixed Assets			
	Opening balance		2,26,00,000	
	Less: Depreciation		(20,00,000)	
	Closing balance			**2,06,00,000**
5.	**Inventories**			
	Finished Goods		30,00,000	
	Stores		16,00,000	
	Loose Tools		2,00,000	**48,00,000**
6.	**Trade Receivables**			
	Trade Receivables		49,00,000	
	Less: Provision for Doubtful Debts		(80,000)	**48,20,000**
7.	**Short term loans & Advances**			
	Staff Advances		2,20,000	
	Other Advances		14,88,000	**17,08,000**

Working Note:

Calculation of Dividend distribution tax

(i) Grossing-up of dividend:

Dividend distributed by Mehar Ltd.		
Equity shares dividend	6,00,000	
Preference share dividend	4,00,000	10,00,000
Add: Increase for the purpose of grossing up of dividend 10,00,000 x [15 /(100-15)]		1,76,470
Gross dividend		11,76,470

(ii) Dividend distribution tax @ 17.304% 2,03,576

Q6. Complete Financial Statements (RTP M20,M23) REG. PAGE NO.

On 31st March 2019, Gaurav Ltd. provides you the following particulars:

Particulars		**Debit Rs.**	**Credit Rs.**
Equity Share Capital (Face value of Rs. 100 each)			12,50,000
Call in Arrears		1,250	
Land & Building		6,87,500	
Plant & Machinery		6,56,250	
Furniture		62,500	
General Reserve			2,62,500
Loan from State Financial Corporation			1,87,500
Inventory:			
Raw Materials	62,500		
Finished Goods	2,50,000	3,12,500	
Provision for Taxation			1,60,000
Trade receivables		2,50,000	
Advances		53,375	
Profit & Loss Account			1,08,375
Cash in Hand		37,500	
Cash at Bank		3,08,750	
Unsecured Loan			1,51,250

Trade payables 2,50,000

The following additional information is also provided:

(i) 2,500 Equity shares were issued for consideration other than cash.

(ii) Debtors of Rs. 65,000 (included in trade receivables) are due for more than 6 months.

(iii) The cost of the Assets were:

Building Rs. 7,50,000, Plant & Machinery Rs. 8,75,000 and Furniture Rs. 78,125

(iv) The balance of Rs. 1,87,500 in the Loan Account with State Finance Corporation is inclusive of Rs. 9,375 for Interest accrued but not due. The loan is secured by hypothecation of Plant & Machinery.

(v) Balance at Bank includes Rs. 2,500 with Global Bank Ltd., which is not a Scheduled Bank.

You are required to prepare the Balance sheet of Gaurav Ltd. as on 31st March, 2019 as per Schedule III to the Companies Act, 2013.

Solution:-

Gaurav Ltd.
Balance Sheet as on 31st March, 2019

	PARTICULARS as on 31st March	NOTE REF	Rs.
I	**EQUITY&LIABILITIES**		
(1)	**Shareholders' funds:**		
	(a) Share capital	1	12,48,750
	(b) Reserves and surplus	2	3,70,875
(2)	**Non current liabilities:**		
	Long term borrowings	3	3,29,375
(3)	**Current liabilities:**		
	(a) Trade payables		2,50,000
	(b) Other current liabilities	4	9,375
	(c) Short term provision	5	1,60,000
	TOTAL		**23,68,375**
II	**ASSETS**		
(1)	**Non-current Assets**		
	(a) Property, Plant & Equipment	6	14,06,250
(2)	**Current Assets:**		
	(a) Inventories	7	3,12,500
	(b) Trade receivables	8	2,50,000
	(c) Cash and Cash equivalents - Cash on hand	9	3,46,250
	(d) Short term loans and advances		53,375
	TOTAL		**23,68,375**

Notes to accounts

			Rs.
1.	**Share Capital**		
	Equity share capital		
	Issued & subscribed & called up		
	12,500 Equity Shares of Rs. 100 each		
	(of the above 2,500 shares have been issued for consideration other than cash)	12,50,000	
	Less: Calls in arrears	(1,250)	12,48,750
	TOTAL		**12,48,750**
2.	**Reserves and Surplus**		
	General Reserve		2,62,500
	Surplus (Profit & Loss A/c)		1,08,375
	TOTAL		**3,70,875**
3.	**Long-term borrowings**		
	Secured Term Loan		
	State Financial Corporation Loan (1,87,500 –9,375) (Secured by hypothecation of Plant and Machinery)		1,78,125

	Unsecured Loan		1,51,250
	TOTAL		**3,29,375**
4.	**Other current liabilities**		
	Interest accrued but not due on loans (SFC)		**9,375**
5.	**Short-term provisions**		
	Provision for taxation		**1,60,000**
6.	**PPE**		
	Land and Building	7,50,000	
	Less: Depreciation	(62,500)	6,87,500
	Plant & Machinery	8,75,000	
	Less: Depreciation	(2,18,750)	6,56,250
	Furniture & Fittings	78,125	
	Less: Depreciation	(15,625)	62,500
	TOTAL		**14,06,250**
7.	**Inventories**		
	Raw Materials		62,500
	Finished goods		2,50,000
	TOTAL		**3,12,500**
8.	Trade receivables		
	Outstanding for a period exceeding six months		65,000
	Other Amounts		1,85,000
	TOTAL		**2,50,000**
9.	**Cash and cash equivalents**		
	Cash at bank		
	with Scheduled Banks	3,06,250	
	with others (Global Bank Ltd.) Cash in hand	2,500	3,08,750
	Cash in hand		37,500
	TOTAL		**3,46,250**

Q7. Financial Stat. of a Non-Going Concern entity (CA-Inter New M19,RTP M22,N22) REG. PAGE NO.

Summarised Balance Sheet of a Cloth Trader as on 31st March 2017 is given below:

LIABILITIES	**AMT.**	**ASSETS**	**AMT.**
Proprietor's Capital	3,00,000	Fixed Assets	3,60,000
Profit & Loss A/c	1,25,000	Closing Stock	1,50,000
10% Loan Account	2,10,000	Sundry Debtors	1,00,000
Sundry Creditors	50,000	Deferred Expenses	50,000
		Cash and Bank	25,000
TOTAL	**6,85,000**	**TOTAL**	**6,85,000**

Additional Information is as follows:

(1) The remaining life of fixed assets is 8 years. The pattern of use of the asset is even. The net realisable value of fixed assets on31.03.2018 was Rs. 3,25,000.

(2) Purchases & Sales in 2017-18 amounted to Rs. 22,50,000 and Rs. 27,50,000 respectively.

(3) The cost & net realizable value of stock on 31.03.2018 were Rs. 2,00,000 & Rs. 2,50,000 respectively.

(4)Expenses for the year amounted to Rs. 78,000.

(5) Deferred Expenses are amortized equally over 5years.

(6) Sundry Debtors on 31.03.2018 are Rs. 1,50,000 of which Rs. 5,000 is doubtful Collection of another Rs. 25,000 depends on successful re-installation of certain product supplied to the customer;

(7) Closing Sundry Creditors are Rs. 75,000, likely to be settled at10% discount.

(8)Cash balance as on 31.03.2018 is Rs. 4,22,000.

(9)There is an early repayment penalty for the loan of Rs. 25,000.

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

(1)Profit & Loss Account for the year 2017-18.

(2) Balance Sheet as on 31stMarch, 2018.

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

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

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

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

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

Q8. Declaration of Dividend (RTP M21) **REG. PAGE NO.**

XYZ Ltd. is having inadequacy of profits in the year ending 31-03-2021 and it proposes to declare 10% dividend out of General Reserves.
From the following particulars ascertain the amount that can be utilized from general reserves, according to the Companies (Declaration of Dividend out of Reserves)
Rules, 2014:
5,00,000 Equity Shares of Rs. 10 each fully paid up 50,00,000
General Reserves 25,00,000
Revaluation Reserves 6,50,000
Net profit for the year 1,42,500
Average rate of dividend during the last five years has been 12%.

Solution:- Amount that can be drawn from reserves for (10% dividend on Rs. 50,00,000 i.e. Rs. 5,00,000)
Profits available
Current year profit Rs. 1,42,500
Amount which can be utilized from reserves (Rs. 5,00,000 – 1,42,500) Rs. 3,57,500
Conditions as per Companies (Declaration of dividend out of Reserves) Rules, 20X1:

Condition I
Since 10% is lower than the average rate of dividend (12%), 10% dividend can be declared.

Condition II
Maximum amount that can be drawn from the accumulated profits and reserves should not exceed 10% of paid up capital plus free reserves ie. Rs. 7,50,000 [10% of (50,00,000 + 25,00,000)]

Condition III
The balance of reserves after drawl Rs. 21,42,500 (Rs. 25,00,000 - Rs. 3,57,500) should not fall below 15 % of its paid up capital ie. Rs. 7,50,000 (15% of Rs. 50,00,000]
Since all the three conditions are satisfied, the company can withdraw Rs. 3,57,500 from accumulated reserve (as per Declaration and Payment of Dividend Rules, 2014).

Q9. (CA-Inter New N19) **REG. PAGE NO.**

From the following particulars furnished by Prashant Ltd., prepare the Balance Sheet as on 31st March 2019 as required by Schedule III of the Companies Act, 2013.

Particulars	Debit Rs.	Credit Rs.
Equity Share Capital (Face value of Rs. 10 each)		15,00,000
Call in Arrears	5,000	
Land	5,50,000	
Building	4,85,000	
Plant & Machinery	5,60,000	

General Reserve		2,70,000
Loan from State Financial Corporation		2,10,000
Inventories	3,15,000	
Provision for Taxation		72,000
Trade receivables	2,95,000	
Short term Loans and Advances	58,500	
Profit & Loss Account		1,06,800
Cash in Hand	37,300	
Cash at Bank	2,85,000	
Unsecured Loan		1,65,000
Trade payables		2,67,000
TOTAL	**25,90,800**	**25,90,800**

The following additional information is also provided:

(i) 10,000 Equity shares were issued for consideration other than cash.

(ii) Trade receivables of Rs. 55,000 are due for more than 6 months.

(iii) The cost of Building and Plant & Machinery is Rs. 5,50,000 and Rs. 6,25,000.

(iv) The loan from State Financial Corporation is secured by hypothecation of Plant & Machinery. The balance of Rs. 2,10,000 in his accounts is inclusive of Rs. 10,000 for interest accrued but not due.

(v) Balance at Bank included Rs. 15,000 with Aakash Bank Ltd., which is not a scheduled bank.

Solution:-

Prashant Ltd.
Balance Sheet as on 31st March, 2019

	PARTICULARS as on 31st March	NOTE REF	Rs.
I	**EQUITY&LIABILITIES**		
(1)	**Shareholders' funds:**		
	(a) Share capital	1	14,95,000
	(b) Reserves and surplus	2	3,76,800
(2)	**Non current liabilities:**		
	Long term borrowings	3	3,65,000
(3)	**Current liabilities:**		
	(a) Trade payables		2,67,000
	(b) Other current liabilities	4	10,000
	(c) Short term provision	5	72,000
	TOTAL		**25,85,800**
II	**ASSETS**		
(1)	**Non-current Assets**		
	(a) Property, Plant & Equipment	6	15,95,000
(2)	**Current Assets:**		
	(a) Inventories		3,15,000
	(b) Trade receivables	7	2,95,000
	(c) Cash and bank balances	8	3,22,300
	(d) Short term loans and advances		58,500
	TOTAL		**25,85,800**

Notes to accounts

			Rs.
1.	**Share Capital**		
	Equity share capital		
	Issued & subscribed & fully paid up		
	1,50,000 Equity Shares of Rs. 10 each		
	(of the above 10,000 shares have been issued for consideration other than cash)	15,00,000	
	Less: Calls in arrears	(5,000)	**14,95,000**
2.	**Reserves and Surplus**		

	General Reserve		2,70,000
	Profit & Loss balance		1,06,800
	TOTAL		**3,76,800**
3.	**Long-term borrowings**		
	Secured		
	Loan from State Financial Corporation (2,10,000-10,000) (Secured by hypothecation of Plant and Machinery)		2,00,000
	Unsecured Loan		1,65,000
	TOTAL		**3,65,000**
4.	**Other current liabilities**		
	Interest accrued but not due on loans (SFC)		**10,000**
5.	**Short-term provisions**		
	Provision for taxation		**72,000**
6.	**Property, Plant & Equipment**		
	Land		5,50,000
	Building	5,50,000	
	Less: Depreciation(b.f.)	(65,000)	4,85,000
	Plant & Machinery	6,25,000	
	Less: Depreciation (b.f.)	(65,000)	5,60,000
	TOTAL		**15,95,000**
7.	**Trade receivables**		
	Outstanding for a period exceeding six months		55,000
	Other Amounts		2,40,000
	TOTAL		**2,95,000**
8.	**Cash and bank balances**		
	Cash and cash equivalents		
	Cash at bank		2,85,000
	Cash in hand		37,300
	Other bank balances		Nil
	TOTAL		**3,22,300**

AS-2 VALUATION OF INVENTORIES

Q1. ICAI RTP May 18 **REG. PAGE NO.**

A private limited company manufacturing fancy terry towels had valued its closing inventory of inventories of finished goods at the realizable value, inclusive of profit and the export cash incentives. Firm contracts had been received and goods were packed for export, but the ownership in these goods had not been transferred to the foreign buyers.

You are required to advise the company on the valuation of the inventories in line with the provisions of AS 2.

Ans. Accounting Standard 2 "Valuation of Inventories" states that inventories should be valued at lower of historical cost and net realizable value. The standard states, "at certain stages in specific industries, such as when agricultural crops have been harvested or mineral ores have been extracted, performance may be substantially complete prior to the execution of the transaction generating revenue. In such cases, when sale is assured under forward contract or a government guarantee or when market exists and there is a negligible risk of failure to sell, the goods are often valued at net realizable value at certain stages of production."

Terry Towels do not fall in the category of agricultural crops or mineral ores. Accordingly, taking into account the facts stated, the closing inventory of finished goods (Fancy terry towel) should have been valued at lower of cost and net realizable value and not at net realizable value. Further, export incentives are recorded only in the year the export sale takes place. Therefore, the policy adopted by the company for valuing its closing inventory of inventories of finished goods is not correct.

Q2. ICAI RTP May 21 **REG. PAGE NO.**

The inventory of Rich Ltd. as on 31st March, 2020 comprises of Product – A: 200 units and Product – B: 800 units.

Details of cost for these products are:

Product – A: Material cost, wages cost and overhead cost of each unit are Rs. 40, Rs. 30 and Rs. 20 respectively, Each unit is sold at Rs. 110, selling expenses amounts to 10% of selling costs.

Product – B: Material cost and wages cost of each unit are Rs. 45 and Rs. 35 respectively and normal selling rate is Rs. 150 each, however due to defect in the manufacturing process 800 units of Product-B were expected to be sold at Rs. 70.

You are requested to value closing inventory according to AS 2 after considering the above.

Ans. According to AS 2 'Valuation of Inventories', inventories should be valued at the lower of cost and net realizable value.

Product – A

Material cost	Rs. 40 x 200 = 8,000	
Wages cost	Rs. 30 x 200 = 6,000	
Overhead	Rs. 20 x 200 = 4,000	
Total cost		Rs. 18,000
Realizable value [200 x (110-11)]		Rs. 19,800
Hence inventory value of Product -A		Rs. 18,000

Product – B

Material cost	Rs. 45 x 800 = 36,000	
Wages cost	Rs. 35 x 800 = 28,000	
Total cost		Rs. 64,000
Realizable value (800 x 70)		Rs. 56,000
Hence inventory value of Product -A		Rs. 56,000
Total Value of closing inventory i.e. Product A + Product B (18,000+ 56,000)		Rs. 74,000

Q3. ICAI RTP Nov 21 **REG. PAGE NO.**

On 31st March 2020, a business firm finds that cost of a partly finished unit on that date is Rs. 430. The unit can be finished in 2020-21 by an additional expenditure of Rs. 310. The finished unit can be sold for Rs. 750 subject to payment of 2% brokerage on selling price.

The firm seeks your advice regarding the amount at which the unfinished unit should be valued as at 31st March, 2020 for preparation of final accounts. Assume that the partly finished unit cannot be sold in semi-finished form and its NRV is zero without processing it further.

Ans. Valuation of unfinished unit

	Rs.
Net selling price	750
Less: Estimated cost of completion	(310)
	440
Less: Brokerage (2% of 750)	(15)
Net Realisable Value	425
Cost of inventory	430
Value of inventory (Lower of cost and net realisable value)	**425**

Q4. ICAI RTP Nov 22 **REG. PAGE NO.**

The closing stock of finished goods (at cost) of a company amounted to Rs. 4,50,000. The following items were included at cost in the total:

(a) 100 coats, which had cost Rs. 2,200 each and normally sold for Rs. 4,000 each. Owing to a defect in manufacture their NRV was determined at 50% of their normal selling price.

(b) Shirts which had cost Rs. 50,000, their net realizable value at Balance sheet date was Rs. 55,000. Commission @ 10% on sales is payable to agents.

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

Ans. Valuation of closing stock

	Rs.
Closing stock at cost	4,50,000
Less: Adjustment for 100 coats (Working Note 1)	(20,000)
Value of inventory	4,30,000

Working Notes:

1. Adjustment for Coats	Rs.
Cost included in Closing Stock	2,20,000
NRV of Coats	2,00,000
Adjustment to be made as NRV is less than Cost	20,000

2. No adjustment required for shirts as their NRV is more than their cost which was included in value of inventory.

Q5. ICAI RTP May 23 **REG. PAGE NO.**

An enterprise ordered 20,000 KG of certain material at Rs. 110 per unit. The purchase price includes GST Rs. 12 per KG, in respect of which full input tax credit (ITC) is admissible. Freight incurred amounted to Rs. 1,17,600. Normal transit loss is 2%. The enterprise actually received 19,500 KG and consumed 18,000 KG of the material.

(i) You are required to calculate cost of material per KG;

(ii) Allocation of material cost

Ans. Calculation of Normal cost per Kg.

	Rs.
Purchase price (20,000 Kg. x Rs. 110)	22,00,000
Less: Input Tax Credit (20,000 Kg. x Rs. 12)	(2,40,000)
	19,60,000
Add: Freight	1,17,600
A. Total material cost	20,77,600
B. Number of units normally received = 98% of 20,000 Kg.	Kg. 19,600
C. Normal cost per Kg. (A/B)	106

Allocation of material cost

	Kg	Rs./kg	Rs,
Materials consumed	18,000	106	19,08,000
Cost of inventory	1,500	106	1,59,000
Abnormal loss	100	106	10,600
Total material cost	19,600	106	20,77,600

Note: Abnormal losses are recognized as separate expense

Q6. ICAI RTP Nov 23 **REG. PAGE NO.**

Alpha Ltd. sells flavored milk to customers; some of the customers consume the milk in the shop run by Alpha Limited. While leaving the shop, the consumers leave the empty bottles in the shop and the company takes possession of these empty bottles. The company has laid down a detailed internal record procedure for accounting for these empty bottles which are sold by the company by calling for tenders. Keeping this in view:

Decide whether the inventory of empty bottles is an asset of the company; If so, whether the inventory of empty bottles existing as on the date of Balance Sheet is to be considered as inventories of the company and valued as per AS 2 or to be treated as scrap and shown at realizable value with corresponding credit to 'Other Income'?

Ans. As per the 'Framework on Presentation and Preparation of Financial Statements': Tangible objects or intangible rights carrying probable future benefits, owned by an enterprise are called assets. Alpha Ltd. sells these empty bottles by calling tenders. It means further benefits are accrued on its sale.

Therefore, empty bottles are assets for the company.

As per AS 2, inventories are assets held for sale in the ordinary course of business. Inventory of empty bottles existing on the Balance Sheet date is the inventory and Alpha Ltd. has detailed controlled recording and accounting procedure which duly signify its materiality.

Thus, inventory of empty bottles cannot be considered as scrap and should be valued as inventory in accordance with AS 2.

Q7. ICAI New Nov 19 **REG. PAGE NO.**

Mr. Rakshit gives the following information relating to items forming part of inventory as on 31st March, 2019. His factory produces product X using raw material A.

(i) 800 units of raw material A (purchased @ Rs. 140 per unit). Replacement cost of raw material A as on 31st March, 2019 is Rs. 190 per unit.

(ii) 650 units of partly finished goods in the process of producing X and cost incurred till date Rs. 310 per unit. These units can be finished next year by incurring additional cost of Rs. 50 per unit.

(iii) 1,800 units of finished product X and total cost incurred Rs. 360 per unit. Expected selling price of product X is Rs. 350 per unit.

In the context of AS-2, determine how each item of inventory will be valued as on 31st March, 2019. Also, calculate the value of total inventory as on 31st March, 2019.

Ans. As per AS 2 (Revised) "Valuation of Inventories", materials and other supplies held for use in the production of inventories are not written down below cost if the finished products in which they will be incorporated are expected to be sold at cost or above cost. However, when there has been a decline in the price of materials and it is estimated that the cost of the finished products will exceed net realizable value, the materials are written down to net realizable value. In such circumstances, the replacement cost of the materials may be the best available measure of their net realizable value. In the given case, selling price of product X is Rs. 350 and total cost per unit for production is Rs. 360.

Hence the valuation will be done as under:

(i) 800 units of raw material will be valued at cost 140.

(ii) 650 units of partly finished goods will be valued at 300 per unit* i.e. lower of cost (Rs. 310) or Net realizable value Rs. 300 (Estimated selling price Rs. 350 per unit less additional cost of Rs. 50).

(iii) 1,800 units of finished product X will be valued at NRV of Rs. 350 per unit since it is lower than cost Rs. 360 of product X.

Valuation of Total Inventory as on 31.03.2019:

	Units	Cost (Rs.)	NRV / Replacement cost Rs.	Value = units x cost or NRV whichever is less (Rs.)	Rs.
Raw material A	800	140	190	1,12,000	(800 x 140)
Partly finished goods	650	310	300	1,95,000	(650 x 300)
Finished goods X	1,800	60	350	6,30,000	(1,800 x 350)
Value of Inventory				**9,37,000**	

Q8. ICAI New Jan 21, MTP Nov 23 Sr. I **REG. PAGE NO.**

Mr. Jatin gives the following information relating to the items forming part of the inventoryas on 31.03.2019. His enterprise produces product P using Raw Material X.

(i) 900 units of Raw Material X (purchases @ Rs. 100 per unit). Replacement cost of Raw Material X as on 3103.2019 is Rs. 80 per unit

(ii) 400 units of partly finished goods in the process of producing P. Cost incurred till date is Rs. 245 per unit. These units can be finished next year by incurring additional cost of Rs. 50 per unit.

(iii) 800 units of Finished goods P and total cost incurred is Rs. 295 per unit. Expected selling price of product P is Rs.280 per unit, subject to a payment of 5% brokerage on selling price.

Determine how each item of inventory will be valued as on 31.03.2019.

Also calculate the value of total Inventory as on 31.03.2019.

Ans. As per AS 2 (Revised) "Valuation of Inventories", materials and other supplies held for use in the production of inventories are not written down below cost if the finished products in which they will be incorporated are expected to be sold at cost or above cost.

However, when there has been a decline in the price of materials and it is estimated that the cost of the finished products will exceed net realizable value, the materials are written down to net realizable value. In such circumstances, the replacement cost of the materials may be the best available measure of their net realizable value. In the given case, selling price of product P is Rs. 266 and total cost per unit for production is Rs. 295.

Hence the valuation will be done as under:

(i) 900 units of raw material X will be written down to replacement cost as market value of finished product is less than its cost, hence valued at Rs. 80 per unit.

(ii) 400 units of partly finished goods will be valued at 216 per unit i.e., lower of cost (Rs. 245) or Net realizable value Rs. 216 (Estimated selling price Rs. 266 per unit less additional cost of Rs. 50).

(iii) 800 units of finished product P will be valued at NRV of Rs. 266 per unit since it is lower than cost Rs. 295.

Valuation of Total Inventory as on 31.03.2019:

	Units	Cost (Rs.)	NRV / Replacement cost Rs.	Value = units x cost or NRV whichever is less (Rs.)
Raw material X	900	100	80	72,000
Partly finished goods	400	245	216	86,400
Finished goods P	800	295	266	2,12,800
Value of Inventory				**3,71,200**

Q9. ICAI New May 21 **REG. PAGE NO.**

Joy Ltd. purchased 20,000 kilograms of Raw Material @ Rs. 20 per kilogram during the year 2020-21. They have furnished you with the following further information for the year ended 31st March, 2021:

Particulars	Units	Amount (Rs.)
Opening Inventory:		
Finished Goods	2,000	1,00,000
Raw Materials	2,200	44,000
Direct Labour		3,06,000
Fixed Overheads		3,00,000
Sales	20,000	11,20,000

Closing Inventory:		
Finished Goods	2,400	
Raw Materials	1,800	

The plant has a capacity to produce 30,000 units of finished product per annum. However, the actual production of finished products during the year 2020-21 was 20,400 units. Due to a fall in the market demand, the price of the finished goods in which the raw material has been utilized is expected to be sold @ Rs. 40 per unit. The replacement cost of the raw material was Rs. 19 per kilogram.

You are required to ascertain the value of closing inventory as at 31st March, 2021 as per AS 2.

Ans. Statement Showing the Computation of Value of Closing Inventory

Value of Closing Finished Goods

Particulars	Amount (Rs.)
Cost of Raw Material consumed (20,400 units X Rs. 20 per kg)	4,08,000
Direct Labour	3,06,000
Fixed Overheads (Rs. 3,00,000/30,000 x 20,400)	2,04,000
Cost of Production	**9,18,000**
Cost of Closing Inventory of Finished Goods per unit (Rs. 9,18,000/20,400)	45
Net Realizable Value (NRV) per unit	40

Since net realizable value is less than cost, closing inventory of Finished Goods will be valued at Rs. 40 per unit

Value of Closing Raw Materials

As NRV of finished goods is less than its cost, the relevant raw material will be valued at its replacement cost, which is the best available measure of its NRV i.e. @ Rs. 19 per kg. Therefore, value of closing inventory would be as under:

Finished Goods 2,400 units @ Rs. 40 per unit	Rs. 96,000
Raw Materials 1,800 kg @ Rs. 19 per kg	Rs. 34,200
Total	Rs. 1,30,200

Working Note:

Calculation of raw material consumed during the year

Particulars	Units (Kg)
Opening Inventory	2,200
Purchases	20,000
Less: Closing Inventory	(1,800)
Raw Material Consumed	20,400

AS-4 CONTINGENCIES AND EVENTS OCCURRING AFTER BALANCE SHEET DATE

Q10. ICAI RTP Nov'21 **REG. PAGE NO.**

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.

Ans. 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.

Q11. ICAI RTP May'22, MTP Dec'21 Series 1 **REG. PAGE NO.**

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 10 th 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.
Ans. 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.

Q12. ICAI New Nov'18 **REG. PAGE NO.**

The accounting year of Dee Limited ended on 31st March, 2018 but the accounts were approved on 30th April, 2018. On 15th April, 2018 a fire occurred in the factory and office premises. The loss by fire is of such a magnitude that it was not possible to expect the enterprise Dee Limited to start operation again.

State with reasons, whether the loss due to fire is an adjusting or non- adjusting event and how the fact of loss is to be disclosed by the company in the context of the provisions of AS-4 (Revised).

Ans. As per AS 4 (Revised) "Contingencies and Events occurring after the Balance Sheet Date", an event occurring after the balance sheet date should be an adjusting event even if it does not reflect any condition existing on the balance sheet date, if the event is such as to indicate that the fundamental accounting assumption of going concern is no longer appropriate. The fire occurred in the factory and office premises of an enterprise after 31 March, 2018 but before approval of financial statement of 30.4.18. The loss by fire is of such a magnitude that it is not reasonable to expect the Dee Ltd. to start operations again, i.e.,the going concern assumption is not valid. Since the fire occurred after 31/03/18, the loss on fire is not a result of any condition existing on 31/03/18. But the loss due to fire is an adjusting event the entire accounts need to be prepared on a liquidation basis with adequate disclosures by the company by way of note in its financial statements in the following manner:

"Major fire occurred in the factory and office premises on 15th April, 2018 which has made impossible for the enterprise to start operations again. Therefore, the financial statements have been prepared on liquidation basis."

Q13. ICAI New May'19,MTP Nov 20,May 22 Series I REG. PAGE NO.

The financial statements of PQ Ltd. for the year 2017-18 approved by the Board of Directors on 15th July, 2018. The following information was provided :

(i) A suit against the company's advertisement was filed by a party on 20th April, 2018, claiming damages of Rs. 25 lakhs.

(ii) The terms and conditions for acquisition of business of another company have been decided by March, 2018. But the financial resources were arranged in April, 2018 and amount invested was Rs. 50 lakhs.

(iii) Theft of cash of Rs. 5 lakhs by the cashier on 31st March, 2018 but was detected on 16th July, 2018.

(iv) Company sent a proposal to sell an immovable property for Rs. 40 lakhs in March, 2018. The book value of the property was Rs. 30 lakhs on 31st March, 2018. However, the deed was registered on 15th April, 2018.

(v) A, major fire has damaged the assets in a factory on 5th April, 2018. However, the assets are fully insured.

With reference to AS-4 "Contingencies and events occurring after the balance sheet date", state whether the above mentioned events will be treated as contingencies, adjusting events or non-adjusting events occurring after the balance sheet date.

Ans. i) Suit filed against the company is a contingent liability but it was not existing as on balance sheet date as the suit was filed on 20th April after the balance Sheet date. As per AS 4, '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. Hence, it will have no effect on financial statements and will be a non-adjusting event.

(ii) In the given case, terms and conditions for acquisition of business were finalised and carried out before the closure of the books of accounts but transaction for payment of financial resources was effected in April, 2018. This is clearly an event occuring after the balance sheet date. Hence, necessary adjustment to assets and liabilities for acquisition of business is necessary in the financial statements for the year ended 31st March 2018.

(iii) Only those significant events which occur between the balance sheet date and the date on which the financial statements are approved, may indicate the need for adjustment to assets and liabilities existing on the balance sheet date or may require disclosure. In the given case, theft of cash was detected on 16th July, 18 after approval of financial statements by the Board of Directors, hence no treatment is required.

(iv) 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. In the given case, sale of immovable property was under proposal stage (negotiations also not started) on the balance sheet date. Therefore, no adjustment to assets for sale of immovable property is required in the financial statements for the year ended 31st March, 2018.

(v) The condition of fire occurrence was not existing on the balance sheet date. Only the disclosure regarding event of fire and loss being completely insured may be given in the report of approving authority.

Q14. ICAI New July'21 **REG. PAGE NO.**

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.

Ans. (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 financi al statements, no adjustment is required. Hence it is non-adjusting event.

Q15. ICAI New Dec'21 **REG. PAGE NO.**

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 23.05.221. Loss was estimated to be Rs. 81,00,000.

Ans. (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 31 st 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.

Q16. ICAI New Nov'22 **REG. PAGE NO.**

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.

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

(i) 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 ex tent 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 note in the financial statements.

(ii) On the basis of evidence provided, the claim against the company will not succeed. Thus, 12 crores should not be provided in the account but should be disclosed by means of a contingent liability with full details of the facts as per AS 29. Provision can be made for legal fee expected to be incurred to the extent that they are not expected to be recovered if the amount can be ascertained.

(iii) The sale of property should be treated as an adjusting event since contracts had been exchanged prior to the year-end. The effect of the sale would be reflected in the financial statements ended on 31.3.2022 and the profit on sale of property Rs. 2,25,000 would be considered.

Q17. ICAI RTP Nov'22 **REG. PAGE NO.**

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

Ans. 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.

Q18. ICAI MTP Dec'21 Series II **REG. PAGE NO.**

An earthquake destroyed a major warehouse of PQR Ltd. on 30.4.2019. The accounting year of the company ended on 31.3.2019. The accounts were approved on 30.6.2019. The loss from earthquake is estimated at Rs. 25 lakhs. State with reasons, whether the loss due to earthquake is an adjusting or non-adjusting event and how the fact of loss is to be disclosed by the company.

Ans. AS 4 "Contingencies and Events Occurring after the Balance Sheet Date", 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 destruction of warehouse due to earthquake did not exist on the balance sheet date i.e. 31.3.2019. Therefore, loss occurred due to earthquake is not to be recognized in the financial year 2018-2019.

However, according to para 8.6 of 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 earthquake has caused major destruction; therefore, fundamental accounting assumption of going concern is called upon.

Hence, the fact of earthquake together with an estimated loss of Rs. 25 lakhs should be disclosed in the Report of the Directors for the financial year 2018-2019.

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

Q19. ICAI RTP May 18, Nov 22, MTP May 20, Dec 21 **REG. PAGE NO.**

Bela Ltd. has a vacant land measuring 20,000 sq. mts, which it had no intention to use in the future. The Company decided to sell the land to tide over its liquidity problems and made a profit of Rs.10 Lakhs by selling the said land. Moreover, there was a fire in the factory and a part of the unused factory shed valued at Rs. 8 Lakhs was destroyed. The loss from fire was set off against the profit from sale of land and profit of Rs. 2 lakhs was disclosed as net profit from sale of assets. You are required to examine the treatment and disclosure done by the company and advise the company in line with AS 5.

Ans. 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.

Q20. ICAI RTP Nov 18 , Nov 19, May 22 **REG. PAGE NO.**

The Accountant of Mobile Limited has sought your opinion with relevant reasons, whether the following transactions will be treated as change in Accounting Policy or not for the year ended 31st March, 2017. You are required to advise him in the following situations in accordance with the provisions of AS 5

(i) Provision for doubtful debts was created @ 2% till 31st March, 2016. From the Financial year 2016-2017, the rate of provision has been changed to 3%.

(ii) During the year ended 31st March, 2017, the management has introduced a formal gratuity scheme in place of ad-hoc ex-gratia payments to employees on retirement.

(iii) Till the previous year the furniture was depreciated on straight line basis over a period of 5 years. From current year, the useful life of furniture has been changed to 3 years.

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

(v) During the year ended 31st March, 2017, there was change in cost formula in measuring the cost of inventories.

Ans. (i) In the given case, Mobile limited created 2% provision for doubtful debts till 31st March, 2016. Subsequently in 2016-17, the company revised the estimates based on the changed circumstances and wants to create 3% provision. Thus change in rate of provision of doubtful debt is change in estimate and is not change in accounting policy. This change will affect only current year.

(ii) As per AS 5, the adoption of an accounting policy for events or transactions that differ in substance from previously occurring events or transactions, will not be considered as a change in accounting policy. Introduction of a formal retirement gratuity scheme by an employer in place of ad hoc ex-gratia payments to employees on retirement is a transaction which is substantially different from the previous policy, will not be treated as change in an accounting policy.

(iii) Change in useful life of furniture from 5 years to 3 years is a change in estimate and is not a change in accounting policy.
(iv) Adoption of a new accounting policy for events or transactions which did not occur previously should not be treated as a change in an accounting policy. Hence the introduction of new pension scheme is not a change in accounting policy.
(v) Change in cost formula used in measurement of cost of inventories is a change in accounting policy.

Q21. ICAI RTP May 19 **REG. PAGE NO.**

Goods of Rs. 5,00,000 were destroyed due to flood in September, 2015. A claim was lodged with insurance company, but no entry was passed in the books for insurance claim. In March, 2018, the claim was passed and the company received a payment of Rs. 3,50,000 against the claim. Explain the treatment of such receipt in final accounts for the year ended 31 st March, 2018.
Ans. As per the provisions of 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 error or omissions in the preparation of financial statements of one or more prior periods. Further, the nature and amount of prior period items should be separately disclosed in the statement of profit and loss in a manner that their impact on current profit or loss can be perceived. In the given instance, it is clearly a case of error in preparation of financial statements for the year 2015-16. Hence, claim received in the financial year 2017-18 is a prior period item and should be separately disclosed in the statement of Profit and Loss.

Q22. ICAI RTP May 20, SM Illu.4 **REG. PAGE NO.**

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.
Ans. 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

Q23. ICAI RTP Nov 20 **REG. PAGE NO.**

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.
Ans. (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.

Q24. ICAI RTP May 21 **REG. PAGE NO.**

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.

Ans. 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.

Q25. ICAI RTP Nov 21 REG. PAGE NO.

(a) 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.

(b) 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.

Ans. (a) 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.

(b) 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.

Q26. ICAI New May 18 REG. PAGE NO.

PQR Ltd. is in the process of finalizing its accounts for the year ended 31st March, 2018. The company seeks your advice on the following:

(i) Goods worth Rs. 5,00,000 were destroyed due to flood in September, 2015. A claim was lodged with insurance company. But no entry was passed in the books for insurance claim in the financial year 2015-16. In March, 2018, the claim was passed and the company received a payment of Rs. 3,50,000 against the claim. Explain the treatment of such receipt in final account for the year ended 31st March, 2018.

(ii) Company created a provision for bad and doubtful debts at 2.5% on debtors in preparing the financial statements for the year 2017-18. Subsequently, on a review of the credit period allowed and financial capacity of the customers, the company decides to increase the provision to 8% on debtors as on 31.03.2018. The accounts were not approved by the Board of Directors till the date of decision. While applying the relevant accounting standard, can this revision be considered as an extra ordinary item or prior period item?

Ans. (i) As per the provisions of 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 error or omissions in the preparation of financial statements of one or more prior periods. Further, the nature and amount of prior period items should be separately disclosed in the statement of profit and loss in a manner that their impact on current profit or loss can be perceived.

In the given instance, it is clearly a case of error/omission in preparation of financial statements for the year 2015-16. Hence, claim received in the financial year 2017- 18 is a prior period item and should be separately disclosed in the statement of Profit and Loss.

(ii) In the given case, a limited company created 2.5% provision for doubtful debts for the year 2017-2018. Subsequently, the company revised the estimates based on the changed circumstances and wants to create 8% provision.
As per AS 5, the revision in rate of provision for doubtful debts will be considered as change in estimate and is neither a prior period item nor an extraordinary item. The effect of such change should be shown in the profit and loss account for the year ending 31st March, 2018.

Q27. ICAI New May 22 **REG. PAGE NO.**

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.

Ans. 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 statem ents 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.

Q28. ICAI New Nov 22 **REG. PAGE NO.**

The Accountant of Shiva Limited had 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.

Ans. (i) In the given case, company has created 3cer% provision for doubtful debts till 31st March, 2020. Subsequently from 1st April, 2020, the company revised the estimates based on the changed circumstances and wants to create 4% provision. Thus, change in rate of provision of doubtful debt is change in estimate and is not change in accounting policy. This change will affect only current year.

(ii) As per AS 5 "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. 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 transaction, will neither be treated as change in an accounting policy nor change in accounting estimate.
(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 neither a change in accounting policy nor a change in accounting estimate.
(v) Change in cost formula used in measurement of cost of inventories is a change in accounting policy.

Q29. ICAI RTP May 23 **REG. PAGE NO.**

State whether the following items are examples of change in Accounting Policy / Change in Accounting Estimates / Extraordinary items / Prior period items / O rdinary Activity:
(i) Actual bad debts turning out to be more than provisions.
(ii) Change from Cost model to Revaluation model for measurement of carrying amount of PPE.
(iii) Government grant receivable as compensation for expenses incurred in previous accounting period.
(iv) Treating operating lease as finance lease.
(v) Capitalisation of borrowing cost on working capital.
(vi) Legislative changes having long term retrospective application.
(vii) Change in 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.

Ans. 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

Q30. ICAI MTP July 21, May 21, May 22 Series II **REG. PAGE NO.**

A company created a provision of Rs. 7,50,000 for staff welfare while preparing the financial statements for the year 2020-21. On 31st March 2021, in a meeting with staff welfare association, it was decided to increase the amount of provision for staff welfare to Rs. 10,00,000. The accounts were approved by Board of Directors on 15th April, 2021.
You are required to explain the treatment of such revision in financial statements for the year ended 31st March 2021 in line with the provisions of AS 5?

Ans. As per AS 5 "Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies", the change in amount of staff welfare provision amounting Rs. 2,50,000 is neither a prior period item nor an extraordinary item. It is a change in es timate, which has been occurred in the year 2020-21. As per the provisions of the standard, normally, all items of income and expense which are recognized in a period are included in the determination of the net profit or loss for the period. This includes extraordinary items and the effects of changes in accounting estimates. However, the effect of such change in accounting estimate should be classified using the same classification in the statement of profit and loss, as was used previously, for the estimate.

AS-7 CONSTRUCTION CONTRACTS

Q31. ICAI New Nov 20, MTP Nov 23 Sr. II **REG. PAGE NO.**

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

In Year 1, the amounts expended were Rs. 8,60,000, the work was certified for Rs. 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 expended were Rs. 4,75,000. Three-fourth of the work under 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, the amounts 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 A/c of Mr. Rajendra each year.

Ans. Year 1

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

% of work completed = $\frac{8,60,000}{18,60,000}$ x 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.

Q32. ICAI New July 21, MTP Nov 22 Sr. II **REG. PAGE NO.**

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.

Ans. Computation of contract cost

	Rs. In Lakhs	Rs. In Lakhs
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

Q33. ICAI New May 22 **REG. PAGE NO.**

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 Price Contract 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	
Progress Payment Received	17,325
Payment to be Received	14,000
Escalation in cost is by 8% and accordingly the contract price is increased by 8%	4,900

From the above information, you are required to:
(i) Compute the contract revenue to be recognized.
(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.

Ans. Calculation of total estimated cost of construction

		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**

Q34. ICAI RTP May 18, Nov 18, RTP Nov 20 REG. PAGE NO.

Uday Constructions undertake to construct a·bridge for the Government of Uttar Pradesh. The construction commenced during the financial year ending 31.03.2016 and is likely to be completed by the next financial year. The contract is for a fixed price of Rs. 12 crores with an escalation clause. The costs to complete the whole contract are estimated at Rs. 9.50 crores of rupees. You are·given the following information for the year ended 31.03.2016: Cost incurred upto 31.03.2016 Rs. 4 crores. Cost estimated to complete the contract Rs. 6 crores Escalation in cost by 5% and accordingly the contract price· is increased by 5%.
You are required to identify the state of completion and calculate the revenue and profit to be recognized for the year as per AS 7.

Ans.

	Rs. In crores
Cost of construction of bridge incurred 31.3.16	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)x100 = 40%
Revenue and Profit to be recognized for the year ended 31st March, 2016 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, 2016 = Rs. 5.04 crore less Rs. 4 crore = 1.04 crore

Q35. ICAI RTP May 19 REG. PAGE NO.

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?

Ans. 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.

Q36. ICAI RTP Nov 19, Nov 22 **REG. PAGE NO.**

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."

Ans. 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.

AS- 9 REVENUE RECOGNITION

Q37. ICAI RTP Nov 19 **REG. PAGE NO.**

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.

Ans. 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.

Q38. ICAI RTP Nov 21 **REG. PAGE NO.**

(a) How will you recognize revenue in the following cases:
1. Installation Fees;
2. Advertising and insurance agency commissions;
3. Subscriptions for publications.

(b) 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.

Ans. a) 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.

(b) 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.

Q39. ICAI RTP May 22 REG. PAGE NO.

(a) 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

(b) 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.

Ans. (a) 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.

(b) (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.

Q40. ICAI RTP Nov 22 REG. PAGE NO.

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.

Ans. (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.

Q41. ICAI RTP May 23 **REG. PAGE NO.**

PQR Ltd., sells agriculture products to dealers. One of the conditions of sale is that interest is at the rate of 2% p.m., for delayed payments. Percentage of interest recovery is only 10% on such overdue outstanding due to various reasons. During the year 2021-22 the company wants to recognize the entire interest receivable. Do you agree?

Ans. As per AS 9 'Revenue Recognition', where the ability to assess the ultimate collection with reasonable certainty is lacking at the time of raising any claim, e.g. for escalation of price, export incentives, interest etc., revenue recognition is postponed to the extent of uncertainty involved. In such cases, it may be appropriate to recognise revenue only when it is reasonably certain that the ultimate collection will be made. Where there is no uncertainty as to ultimate collection, revenue is recognised at the time of sale or rendering of service even though payments are made by instalments.

Thus, PQR Ltd. cannot recognise the interest amount unless the company actually receives it. 10% rate of recovery on overdue outstanding is also an estimate based on previous record and is not certain. Hence, the company is advised to recognise interest receivable only on receipt basis.

AS-10 PROPERTY, PLANT AND EQUIPMENT

Q42. ICAI RTP Nov 22

RS Ltd. has acquired a heavy plant at a cost of Rs. 2,00,00,000. The estimated useful life is 10 years. At the end of the 2nd year, one of the major components i.e. the Boiler has become obsolete (which was acquired at price of Rs. 50,00,000) and requires replacement, as further maintenance is uneconomical. The remainder of the plant is perfect and is expected to last for next 8 years. The cost of a new boiler is Rs. 60,00,000.

Can the cost of the new boiler be recognised as an asset, and, if so, what should be the carrying value of the plant at the end of second year?

Ans. Recognition of Asset: The new boiler will produce economic benefits to RS Ltd., and the cost is measurable. Hence, the item should be recognized as an asset. The cost old boiler should be de-recognized and the new boiler will be added .

Statement showing cost of new boiler and machine after year 2

Original cost of plant	Rs. 2,00,00,000
Less: Accumulated depreciation [(2,00,00,000 /10) x 2]	Rs. 40,00,000
Carrying value of the plant after two years	Rs. 1,60,00,000
Less: Current Cost of Old Boiler to be derecognized	40,00,000
Less: WDV of Boiler (replaced) after 2 years (50,00,000/10 x 8)	
	1,20,00,000
Add: Cost of new Boiler to be recognized	60,00,000
Revised carrying amount of Plant	1,80,00,000

Q43. ICAI RTP May 22

A Ltd. has incurred the following costs. Determine if the following costs can be added to the invoiced purchase price and included in the initial recognition of the cost of the item of property, plant and equipment:

1. Import duties paid
2. Shipping costs and cost of road transport for taking the machinery to factory
3. Insurance for the shipping
4. Inauguration costs for the factory
5. Professional fees charged by consulting engineer for the installation process
6. Costs of advertising and promotional activities
7. Administration and other general overhead costs
8. Cost of site preparation.

Ans. Included in Cost:
Point no. 1,2,3,5,8
Excluded from Cost:
Point no. 4,6,7

Q44. ICAI RTP Nov 21

A property costing Rs. 10,00,000 is bought on 1.4.2020. Its estimated total physical life is 50 years. However, the company considers it likely that it will sell the property after 25 years.
The estimated residual value in 25 years' time, based on current year prices, is:
Case (a) Rs. 10,00,000
Case (b) Rs. 9,00,000
You are required to compute the amount of depreciation charged for the year ended 31.3.2021.
Ans. Case (a)
The company considers that the residual value, based on prices prevailing at the balance sheet date, will equal the cost.
There is, therefore, no depreciable amount and depreciation is zero.
Case (b)
The company considers that the residual value, based on prices prevailing at the balance sheet date, will be Rs. 9,00,000 and the depreciable amount is, therefore, Rs. 1,00,000.
Annual depreciation (on a straight line basis) will be Rs. 4,000 [{10,00,000 – 9,00,000} ÷ 25].

Q45. ICAI RTP May 21

You are required to give the correct accounting treatment for the following in line with provisions of AS 10:
(a) Trozen Ltd. operates a major chain of supermarkets all over India. It acquires a new store in Pune which requires significant renovation expenditure. It is expected that the renovations will be done in 2 months during which the store will be closed. The budget for this period, including expenditure related to construction and remodelling costs (Rs. 18 lakhs), salaries of staff (Rs. 2 lakhs) who will be preparing the store before its opening and related utilities costs (Rs. 1.5 lakhs), is prepared. The cost of salaries of the staff and utilities are operating expenditures that would be incurred even after the opening of the supermarket. What will the treatment of all these expenditures in the books of accounts?
(b) ABC Ltd is setting up a new refinery outside the city limits. In order to facilitate the construction of the refinery and its operations, ABC Ltd. is required to incur expenditure on the construction/development of railway siding, road and bridge.
Though ABC Ltd. incurs the expenditure on the construction/development, it will not have ownership rights on these items and they are also available for use to other entities and public at large. Can ABC Ltd. capitalize expenditure incurred on these items as property, plant and equipment (PPE)?
Ans. (a) Trozen Ltd. should capitalize the costs of construction and remodelling the supermarket, because they are necessary to bring the store to the condition necessary for it to be capable of operating in the manner intended. The supermarket cannot be opened without incurring the remodelling expenditure. Therefore, this construction and remodelling expenditure of Rs. 18 lakh should be considered as part of the cost of the asset. However, the cost of salaries of the staff Rs. 2 lakh and utilities cost Rs. 1.5 lakh are operating expenditures that would be incurred even after the opening of the supermarket. Therefore, these costs are not necessary to bring the store to the condition necessary for it to be capable of operating in the manner intended by the management and should be expensed.

AS 10 states that the cost of an item of property, plant and equipment shall be recognized as an asset if, and only if:

(a) it is probable that future economic benefits associated with the item will flow to the entity; and
(b) the cost of the item can be measured reliably.
Further, the standard provides that the standard does not prescribe the unit of measure for recognition, i.e., what constitutes an item of property, plant and equipment. Thus, judgement is required in applying the recognition criteria to an entity's specific circumstances. The cost of an item of property, plant and equipment comprise any costs directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management.
In the given case, railway siding, road and bridge are required to facilitate the construction of the refinery and for its operations. Expenditure on these items is required to be incurred in order to get future economic benefits from the project as a whole which can be considered as the unit of measure for the purpose of capitalization of the said expenditure even though the company cannot restrict the access of others for using the assets individually. It is apparent that the aforesaid expenditure is directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management.
In view of this, even though ABC Ltd. may not be able to recognize expenditure incurred on these assets as an individual item of property, plant and equipment in many cases (where it cannot restrict others from using the asset), expenditure incurred may be capitalized as a part of overall cost of the project. From this, it can be concluded that, in the given case the expenditure incurred on these assets, i.e., railway siding, road and bridge, should be considered as the cost of constructing the refinery and accordingly, expenditure incurred on these items should be allocated and capitalized as part of the items of property, plant and equipment of the refinery.

Q46. ICAI RTP Nov 20, MTP Nov 20 , May 22

Omega Ltd. contracted with a supplier to purchase machinery which is to be installed in its one department 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. 1,40,000. These activities were supervised by a technician during the entire period, who is employed for this purpose at Rs. 45,000 per month.
The machine was purchased at Rs. 1,58,00,000 and Rs. 50,000 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.
You are required to ascertain the amount at which the Machinery should be capitalized under AS 10.
Ans. Calculation of Cost of Machinery

Particulars		Rs.
Purchase Price	Given	1,58,00,000
Add: Site Preparation Cost	Given	1,40,000
Technician's Salary	Specific/Attributable overheads for 3months (45,000 x3)	1,35,000
Initial Delivery Cost	Transportation	50,000
Professional Fees for Installation	Architect's Fees	30,000
Total Cost of Asset		1,61,55,000

Q47. ICAI RTP May 20

(a) Entity A has a policy of not providing for depreciation on PPE capitalized in the year until the following year, but provides for a full year's depreciation in the year o disposal of an asset. Is this acceptable?
(b) Entity A purchased an asset on 1st January 2016 for Rs. 1,00,000 and the asset ha an estimated useful life of 10 years and a residual value of nil. On 1st January 2020 the directors review the estimated life and decide that the asset will probably be useful for a further 4 years. Calculate the amount of depreciation for each year, if company charges depreciation on Straight Line basis.
(c) The following items are given to you:
ITEMS
(1) Costs of testing whether the asset is functioning properly, after deducting the net proceeds from selling any items produced while bringing the asset to that location and condition (such as samples produced when testing equipment);
(2) Costs of conducting business in a new location or with a new class of customer (including costs of staff training);

(3) Any costs directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management
(4) Costs of opening a new facility or business, such as, inauguration costs;
(5) Purchase price, including import duties and non–refundable purchase taxes, after deducting trade discounts and rebates.
With reference to AS 10 "Property, Plant and Equipment", classify the above items under the following heads:
HEADS
(i) Purchase Price of PPE
(ii) Directly attributable cost of PPE or
(iii) Cost not included in determining the carrying amount of an item of PPE.

Ans. (a) The depreciable amount of a tangible fixed asset should be allocated on a systematic basis over its useful life. The depreciation method should reflect the pattern in which the asset's future economic benefits are expected to be consumed by the entity.
Useful life means the period over which the asset is expected to be available for use by the entity. Depreciation should commence as soon as the asset is acquired and is available for use. Thus, the policy of Entity A is not acceptable.
(b) The entity has charged depreciation using the straight-line method at Rs. 10,000 per annum i.e (1,00,000/10 years). On 1st January 2020, the asset's net book value is
[1,00,000 – (10,000 x 4)] = Rs. 60,000.
The remaining useful life is 4 years. The company should amend the annual provision for depreciation to charge the unamortized cost over the revised remaining life of four years. Consequently, it should charge depreciation for the next 4 years at Rs. 15,000 per annum i.e. (60,000 / 4 years). Depreciation is recognized even if the Fair value of the Asset exceeds its Carrying Amount. Repair and maintenance of an asset do not negate the need to depreciate it.
(c) (1) Costs of testing whether the asset is functioning properly, after deducting the net proceeds from selling any items produced while bringing the asset to that location and condition (such as samples produced when testing equipment) will be classified as "Directly attributable cost of PPE".
(2) Costs of conducting business in a new location or with a new class of customer (including costs of staff training) will be classified under head (iii)as it will not be included in determining the carrying amount of an item of PPE.
(3) Any costs directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by
management will be included in determination of Purchase Price of PPE
(4) Costs of opening a new facility or business, such as, inauguration costs will be classified under head (iii) as it will not be included in determining the carrying amount of an item of PPE.
(5) Purchase price, including import duties and non–refundable purchase taxes, after deducting trade discounts and rebates will be included in determination of Purchase Price of PPE.

Q48. ICAI New May 22

XYZ Limited provided you the following information for the year ended 31 st March, 2022.
(i) The carrying amount of a property at the end of the year amounted to Rs. 2,16,000 (cost/value Rs. 2,50,000 and accumulated depreciation Rs. 34,000). On this date the property was revalued and was deemed to have a fair value of Rs. 1,90,000. The balance in the revaluation surplus relating to a previous revaluation gain for this property was Rs. 20,000.
You are required to calculate the revaluation loss as per AS 10 (Revised) and give its treatment in the books of accounts.
(ii) An asset that originally cost Rs. 76,000 and had accumulated depreciation of Rs. 62,000 was disposed of during the year for Rs. 4,000 cash.
You are required to explain how the disposal should be accounted for in the financial statements as per AS 10 (Revised).

Ans. (i) As per AS 10, a decrease in the carrying amount of an asset arising on revaluation should be charged to the statement of profit and loss. However, the decrease should be debited directly to owners' interests under the heading of revaluation surplus to the extent of any credit balance existing in the revaluation surplus in respect of that asset.
Calculation of revaluation loss and its accounting treatment

		Rs.
Carrying value of the asset as on 31st March, 2022	a	2,16,000
Revalued amount of the asset	B	(1,90,000)
Total revaluation loss on asset	c= a-b	26,000
Adjustment of previous revaluation reserve	d	(20,000)
Net revaluation loss to be charged to the Profit and loss account	e=c-d	6,000

(ii) AS 10 states that the carrying amount of an item of property, plant and equipment is derecognized on disposal of the asset. It further states that the gain or loss arising from the derecognition of an item of property, plant and equipment should be included in the statement of profit and loss when the item is derecognized. Gains should also not be classified as revenue.

Calculation of loss on disposal of the asset and its accounting treatment

		Rs.
Original cost of the asset	a	76,000
Accumulated depreciation till date	B	62,000
Carrying value of the asset as on 31st March, 2022	c= a-b	14,000
Cash received on disposal of the asset	d	4,000
Loss on disposal of asset charged to the Profit and loss account	e=c-d	10,000

AS-11 THE EFFECTS OF CHANGES IN FOREIGN EXCHANGE RATES (REVISIED)

Q49. ICAI New November 2018

i) ABC Ltd. a Indian Company obtained long term loan from WWW private Ltd., a U.S. company amounting to Rs.30,00,000. It was recorded at US $1 = Rs.60.00, taking exchange rate prevailing at the date of transaction. The exchange rate on balance sheet date (31.03.2018) was US $1 = Rs.62.00.

(ii) Trade receivable includes amount receivable from Preksha Ltd.Rs.10,00,000 recorded at the prevailing exchange rate on the date of sales, transaction recorded at US $1 = Rs.59.00. The exchange rate on balance sheet date (31.03.2018) was US $1 = Rs.62.00.

You are required to calculate the amount of exchange difference and also explain the accounting treatment needed in the above two cases as per AS 11 in the books of ABC Ltd.

Ans.

	Long term Loan	**Foreign currency rate**	**Rs.**
i)	Initial recognition US $50,000 Rs. (30,00,000/60) Rate on Balance Sheet date Exchange Difference Loss US $50,000 × Rs. (62-60) **Treatment:** Credit Loan A/c and Debit Profit and Loss A/c by Rs.1,00,000	1 US $= Rs.60 1 US $= Rs.62	30,00,000 1,00,000
ii)	**Trade receivables** Initial recognition US $16,949.152 (Rs.10,00,000/59) Rate on Balance Sheet date Exchange Difference Gain US $16,949.152 × Rs. (62-59) **Treatment:** Credit Profit and Loss A/c by Rs.50,847.456 and Debit Trade Receivables	1 US $= Rs.59 1 US $= Rs.62	10,00,000 50,847.456

Q50. RTP November 2019

Trade receivables as on 31.3.2019 in the books of XYZ Ltd. include an amount receivable from Umesh Rs. 5,00,000 recorded at the prevailing exchange rate on the date of sales, i.e. at US $ 1= Rs. 58.50. US $ 1 = Rs. 61.20 on 31.3.2019. Explain briefly the accounting treatment needed in this case as per AS 11 as on 31.3.2019

Ans: As per AS 11 "The Effects of Changes in Foreign Exchange Rates", exchange differences arising on the settlement of monetary items or on reporting an enterprise's monetary items at rates different from those at which they were initially recorded during the period, or reported in previous financial statements, should be recognized as income or as expenses in the period in which they arise.

Accordingly, exchange difference on trade receivables amounting Rs. 23,076{Rs.5,23,076(US $ 8547*x Rs. 61.20) less Rs. 5,00,000} should be charged to profit & Loss account.
***US $ 8,547 = 5,00,000/58.50**

AS-12 ACCOUNTING FOR GOVERNMENT GRANTS

Q51. RTP May 2020, Nov 20

How would you treat the following in the accounts in accordance with AS 12 'Government Grants'?
(i) Rs. 35 Lakhs received from the Local Authority for providing Medical facilities to the employees.
(ii) Rs. 100 Lakhs received as Subsidy from the Central Government for setting up a unit in a notified backward area.
(iii) Rs. 10 Lakhs Grant received from the Central Government on installation of anti- pollution equipment.

Ans. (i) Rs. 35 lakhs received from the local authority for providing medical facilities to the employees is a grant received in the nature of a revenue grant. Such grants are generally presented as a credit in the profit and loss statement, either separately or under a general heading such as 'Other Income'. Alternatively, Rs. 35 lakhs may be deducted in reporting the related expense i.e. employee benefit expenses.
(ii) As per AS 12 'Accounting for Government Grants', where the government grants are in the nature of promoters' contribution, i.e. they are given with reference to the total investment in an undertaking or by way of contribution towards its total capital outlay and no repayment is ordinarily expected in respect thereof, the grants are treated as capital reserve which can be neither distributed as dividend nor considered as deferred income.
In the given case, the subsidy received from the Central Government for setting up a unit in notified backward area is neither in relation to specific fixed asset nor in relation to revenue. Thus, amount of Rs. 100 lakhs should be credited to capital reserve.
(iii) Rs. 10 lakhs grant received for installation anti-pollution equipment is a grant related to specific fixed asset. Two methods of presentation in financial statements of grants related to specific fixed assets are regarded as acceptable alternatives. Under first method, the grant is shown as a deduction from the gross value of the asset concerned in arriving at its book value. The grant is thus recognised in the profit and loss statement over the useful life of a depreciable asset by way of a reduced depreciation charge. Under the second method, grants related to depreciable assets are treated as deferred income which is recognised in the profit and loss statement on a systematic and rational basis over the useful life of the asset.
Thus, Rs. 10 lakhs may either be deducted from the cost of equipment or treated as deferred income to be recognized on a systematic basis in profit & Loss A/c over the useful life of equipment.

Q52. RTP May 2021, May 23

(i) Hygiene Ltd. had received a grant of Rs. 50 lakh in 2012 from a State Government towards installation of pollution control machinery on fulfilment of certain conditions. The company, however, failed to comply with the said conditions and consequently was required to refund the said amount in 2020. The company debited the said amount to its machinery account in 2020 on payment of the same. It also reworked the depreciation for the said machinery from the date of its purchase and passed necessary adjusting entries in the year 2020 to incorporate the retrospective impact of the same. State whether the treatment done by the company is correct or not.
(ii) ABC Ltd. received two acres of land received for set up of plant. It also received Rs.2 lakhs received for purchase of machinery of Rs. 10 lakhs. Useful life of machinery is 5 years. Depreciation on this machinery is to be charged on straight-line basis. How should ABC Ltd. recognize these government grants in its books of accounts?
Ans. (i) As per the facts of the case, Hygiene Ltd. had received a grant of Rs. 50 lakh in 2012 from a State Government towards installation of pollution control machinery on fulfilment of certain conditions. However, the amount of grant has to be refunded since it failed to comply with the prescribed conditions. In such circumstances, AS 12, "Accounting for Government Grants", requires that the amount refundable in respect of a government grant related to a specific fixed asset is recorded byincreasing the book value of the asset or by reducing the capital reserve or the deferred income balance, as appropriate, by the amount refundable. The Standard further makes it clear that in the first alternative, i.e., where the book value of the asset is increased, depreciation on the revised book value should be provided prospectively over the residual useful life of the asset. Accordingly, the accounting treatment given by Hygiene Ltd. of

increasing the value of the plant and machinery is quite proper. However, the accounting treatment in respect of depreciation given by the company of adjustment of depreciation with retrospective effect is improper and constitutes violation of AS 12.

(ii) ABC Ltd. should recognize the grants in the following manner:

● As per AS 12, government grants may take the form of non-monetary assets, such as land or other resources, given at concessional rates. In these circumstances, it is usual to account for such assets at their acquisition cost. Non-monetary assets given free of cost are recorded at a nominal value. Accordingly, land should be recognised at nominal value in the balance sheet.

● The standard provides option to treat the grant either as a deduction from the gross value of the asset or to treat it as deferred income as per provisions of the standard. Under first method, the grant is shown as a deduction from the gross value of the asset concerned in arriving at its book value. The grant is thus recognised in the profit and loss statement over the useful life of a depreciable asset by way of a reduced depreciation

charge. Accordingly, the grant of Rs. 2 lakhs is deducted from the cost of the machinery. Machinery will be recognised in the books at Rs. 10 lakhs – Rs. 2 lakhs = Rs. 8 lakhs and depreciation will be charged on it as follows:

Rs. 8 lakhs/ 5 years = Rs. 1.60 lakhs per year.

Under the second method, grants related to depreciable assets are treated as deferred income which is recognised in the profit and loss statement on a systematic and rational basis over the useful life of the asset. Such allocation to income is usually made over the periods and in the proportions in which depreciation on related assets is charged. Rs. 2 lakhs should be recognised as deferred income and will be transferred to profit and loss over the useful life of the asset. In this case, Rs. 40,000 [Rs. 2 lakhs / 5 years] should be credited to profit and loss each year over the period of 5 years.

Q53. RTP Nov 2021

D Ltd. acquired a machine on 01-04-2017 for Rs. 20,00,000. The useful life is 5 years. The company had applied on 01-04-2017, for a subsidy to the tune of 80% of the cost. The sanction letter for subsidy was received in November 2020. The Company's Fixed Assets Account for the financial year 2020-21 shows a credit balance as under:

Particulars	Rs.
Machine (Original Cost)	20,00,000
Less: Accumulated Depreciation (from 2017-18- to 2019-20 on Straight Line Method)	12,00,000
	8,00,000
Less: Grant received	(16,00,000)
Balance	**(8,00,000)**

You are required to explain how should the company deal with this asset in its accounts for 2020-21?

Ans. From the above account, it is inferred that the Company has deducted grant from the book value of asset for accounting of Government Grants. Accordingly, out of the Rs. 16,00,000 that has been received, Rs. 8,00,000 (being the balance in Machinery A/c) should be credited to the machinery A/c.

The balance Rs. 8,00,000 may be credited to P&L A/c, since already the cost of the asset to the tune of Rs. 12,00,000 had been debited to P&L A/c in the earlier years by way of depreciation charge, and Rs. 8,00,000 transferred to P&L A/c now would be partial recovery of that cost.

There is no need to provide depreciation for 2020-21 or 2021-22 as the depreciable amount is now Nil.

Q54. RTP May 2022

A fixed asset is purchased for Rs. 30 lakhs. Government grant received towards it is Rs. 12 lakhs. Residual Value is Rs. 6 lakhs and useful life is 4 years. The company charges depreciation based on Straight-Line method. Asset is shown in the balance sheet net of grant. After 1 year, grant becomes refundable to the extent of Rs. 7.5 lakhs due to non-compliance with certain conditions. You are required to give necessary journal entries for second year.

Ans.

Journal Entries

Year	Particulars		Rs. in lakhs (Dr.)	Rs. in lakhs (Cr.)
2nd	Fixed Asset Account Dr.	Dr.	7.5	

	To Bank Account (Being government grant on asset partly refunded which increased the cost of fixed asset)			7.5
	Depreciation Account (W.N.) To Fixed Asset Account (Being depreciation charged on SLM on revised value of fixed asset prospectively)	Dr.	5.5	5.5
	Profit & Loss Account To Depreciation Account (Being depreciation transferred to Profit and Loss Account at the end of year 2)	Dr.	5.5	5.5

Working Note:
Depreciation for Year 2

	Rs.
Cost of the Asset	30
Less: Government grant received	(12)
	18
Less: Depreciation for the first year [18-6/4]	3
	15
Add: Government grant refundable	7.5
	22.5
Depreciation for the second year [22.5-6/3]	5.5

AS-16 BORROWING COSTS

Q55.

Assume NDA Limited begins construction on a new building on 1st January, 2004. In addition, NDA Limited obtained a Rs. 1 lakh loan to finance the construction of the building on 1st January, 2004 at an annual interest rate of 10%. The company's other outstanding debt during 2004 consists of two loans of Rs. 6 lakhs and Rs. 8 lakhs with interest rates of 11% and 13% respectively. Expenditures that were made on the building project were as follows:

January 2004	2,00,000
April 2004	3,00,000
July 2004	4,00,000
December 2004	1,20,000

Compute the cost to be capitalized including the borrowing cost.

Ans. Step 1

Computation of average accumulated expenses

Rs. 2,00,000 × 12/12 (January-December)	= Rs. 2,00,000
Rs. 3,00,000 × 9/12 (April – December)	= Rs. 2,25,000
Rs. 4,00,000 × 6/12 (July – December)	= Rs. 2,00,000
Rs. 1,20,000 ×1/12 (December)	= Rs. 10,000
Rs. 10,20,000 Average Accumulated Expenses	= Rs. 6,35,000

Step 2

Compute the average interest rate based on the other outstanding debt of the entity other than specific borrowings:

6,00,000 × 11%	= Rs. 66,000
8,00,000 × 13%	= Rs. 1,04,000
14,00,000	Rs. 1,70,000

Average interest rate: Rs. 1,70,000/14,00,000 = 12.14%

Step 3

Compute the interest on average accumulated expenses

Average Accumulated Expenses (AAE)	Interest to be capitalized (based on AAE)
1,00,000 (Specific borrowings) × 10% 5,35,000 (6,35,000-1,00,000) × 12.14%	10,000 64,950
6,35,000	74,950

Step 4
Compute actual interest costs incurred during the year

1,00,000 × 10%	=	Rs. 10,000
6,00,000 × 11%	=	Rs. 66,000
8,00,000 × 13%	=	Rs. 1,04,000
Total		Rs. 1,80,000

Amount to be capitalized is Rs. 74,950 which is not more than actual interest of Rs. 1,80,000

(Amount in Rs.)

Building A/c	Dr.	10,94,950	
To Cash			10,94,950

Q56. RTP May 2020,MTP Nov 2018 Sr.-I,II,MTP Nov 19

Govind Ltd. issued 12% secured debentures of Rs. 100 Lakhs on 01.04.2018, to be utilized as under:

Particulars	Amount (Rs. in lakhs)
Construction of factory building	40
Purchase of Machinery	35
Working Capital	25

In March 2019, construction of the factory building was completed and machinery was installed and ready for its intended use. Total interest on debentures for the financial year ended 31.03.2019 was Rs. 12,00,000. During the year 2018-19, the company had invested idle fund out of money raised from debentures in banks' fixed deposit and had earned an interest of Rs. 3,00,000.

You are required to show the treatment of interest under Accounting Standard 16 and also explain nature of assets.

Ans. According to AS 16 "Borrowing Costs", borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset should be capitalised as part of the cost of that asset. The amount of borrowing costs eligible for capitalisation should be determined in accordance with this Standard. Other borrowing costs should be recognised as an expense in the period in which they are incurred.

It also states that to the extent that funds are borrowed specifically for the purpose of obtaining a qualifying asset, the amount of borrowing costs eligible for capitalization on that asset should be determined as the actual borrowing costs incurred on that borrowing during the period less any income on the temporary investment of those borrowings.

Thus, eligible borrowing cost
= Rs. 12,00,000 – Rs. 3,00,000
= Rs. 9,00,000

Sr. No.	Particulars	Nature of assets	Interest to be capitalized (Rs.)	Interest to be charged to Profit & Loss Account (Rs.)
(i)	Construction of factory building	Qualifying Asset	9,00,000x40/100 = Rs. 3,60,000	NIL
(ii)	Purchase of Machinery	Not a Qualifying Asset	NIL	9,00,000x35/100 = Rs. 3,15,000
(iii)	Working Capital	Not a Qualifying Asset	NIL	9,00,000x25/100 = Rs. 2,25,000
	TOTAL		**Rs. 3,60,000**	**Rs. 5,40,000**

Q57. RTP Nov 2020

(a) Vital Limited borrowed an amount of Rs.150 crores on 1.4.2019 for construction of boiler plant @ 10% p.a. The plant is expected to be completed in 4 years. Since the weighted average cost of capital is 13% p.a., the accountant of Vital Ltd. capitalized Rs. 19.50 crores for the accounting period ending on 31.3.2020. Due to surplus fund out of Rs.150 crores, an income of Rs. 1.50 crores was earned and credited to profit and loss account. Comment on the above treatment of accountant with reference to relevant accounting standard.

(b) When capitalization of borrowing cost should cease as per Accounting Standard 16? Explain in brief.

Ans. (a) Para 10 of AS 16 'Borrowing Costs' states that to the extent the funds are borrowed specifically for the purpose of obtaining a qualifying asset, the amount of borrowing costs eligible for capitalization on that asset should be determined as the actual borrowing costs incurred on that borrowing during the period less any income on the temporary investment of those borrowings. The capitalization rate should be the weighted average of the borrowing costs applicable to the borrowings of the enterprise that are outstanding during the period, other than borrowings made specifically for the purpose of obtaining a qualifying asset. Hence, in the above case, treatment of accountant of Vital Ltd. is incorrect. The amount of borrowing costs capitalized for the financial year 2019-20 should be calculated as follows:

Actual interest for 2019-20 (10% of Rs. 150 crores)	Rs. 15.00 crores
Less: Income on temporary investment from specific borrowings	(Rs.1.50 crores)
Borrowing costs to be capitalized during year 2019-2020	**Rs. 13.50 crores**

(b) Capitalization of borrowing costs should cease when substantially all the activities necessary to prepare the qualifying asset for its intended use or sale are complete.

An asset is normally ready for its intended use or sale when its physical construction or production is complete even though routine administrative work might still continue.

If minor modifications such as the decoration of a property to the user's specification, are all that are outstanding, this indicates that substantially all the activities are complete. When the construction of a qualifying asset is completed in parts and a completed part is capable of being used while construction continues for the other parts, capitalization of borrowing costs in relation to a part should cease when substantially all the activities necessary to prepare that part for its intended use or sale are complete.

Q58. RTP Nov 2021

In May, 2020, Omega Ltd. took a bank loan from a Bank. This loan was to be used specifically for the construction of a new factory building. The construction was completed mid January, 2021 and the building was put to its use immediately thereafter. Interest on the actual amount used for construction of the building till its completion was Rs. 18 lakhs, whereas the total interest payable to the bank on the loan for the period till 31 st March, 2021 amounted to Rs. 25 lakhs. the company wants to treat Rs. 25 lakhs as part of the cost of factory building and thus capitalize it on the plea that the loan was specifically taken for the construction of factory building? Explain the treatment in line with the provisions of AS 16.

Ans. AS 16 clearly states that capitalization of borrowing costs should cease when substantially all the activities necessary to prepare the qualifying asset for its intended use are completed. Therefore, interest on the amount that has been used for the construction of the building up to the date of completion (January, 2021) i.e. Rs. 18 lakhs alone can be capitalized. It cannot be extended to Rs. 25 lakhs.

Q59. RTP May 2022

(a) An enterprise has constructed a complex piece of equipment (qualifying asset) that is to be installed on the production line of a manufacturing plant. The equipment has been constructed over a period of 15 months. However, on installation, certain calibrations are required to achieve the desired level of production before it is finally commissioned. This process is expected to take approximately 2 months during which test runs will be made. Should the borrowing costs attributable to borrowings pertaining to the 2 months test run period be capitalized?

(b) Should capitalization of borrowing costs be continued when the qualifying asset has been constructed but marketing activities to sell the asset are still in progress?

Ans. (a) As per AS 16 Borrowing Costs "Capitalization of borrowing costs should cease when substantially all the activities necessary to prepare the qualifying asset for its intended use or sale are complete". On installation of the equipment, an evaluation has to be made to conclude whether substantially all the activities necessary to prepare the asset are complete. After an equipment has been installed it is usually tested and adjusted for commercial production before it is finally commissioned. The calibrations and adjustments required during this period are performed in order to bring the equipment up to the stage at which it is ready to commence commercial production. Until the asset reaches the stage when it is ready to support commercial levels of production, it is not appropriate to conclude that substantially all the activities necessary to prepare the asset are complete. Thus, the borrowing cost incurred during the normal period of test runs (after the installation) are required to be capitalized.

(b) As per provisions of AS 16, capitalization of borrowing costs should cease when substantially all the activities necessary to prepare the qualifying asset for its intended use or sale are complete. Further, the standard also explains that "An asset is normally ready for its intended use or sale when its physical construction or production is complete even though routine administrative work might sill continue. If minor modifications, such as the decoration of a property to the user's specification, are all that are outstanding, this indicates that substantially all the activities are complete". The emphasis in the Standard is on "to prepare the qualifying asset for its intended use or sale" and not the actual activity of sale. Therefore, where the physical construction of the asset is complete, substantially all the activities necessary to prepare the qualifying asset for its intended use or sale are complete. Therefore, in the given case, the borrowing costs pertaining to the period during which the marketing activities to sell the asset are still in progress should not be capitalized as part of the cost of the asset.

Q60. RTP Nov 2022

Harish Construction Company is constructing a huge building project consisting of four phases. It is expected that the full building will be constructed over several years but Phase I and Phase II of the building will be started as soon as they are completed.

Following is the detail of the work done on different phases of the building during the current year:

(Rs. in lakhs)

	Phase I Rs.	Phase II Rs.	Phase III Rs.	Phase IV Rs.
Cash expenditure	10	30	25	30
Building purchased	24	34	30	38
Total expenditure	34	64	55	68
Total expenditure of all phases				221
Loan taken @ 15% at the beginning of the year				200

During mid of the current year, Phase I and Phase II have become operational. Find out the total amount to be capitalized and to be expensed during the year.

Ans.

	Particulars	Rs.
1.	Interest expense on loan Rs. 2,00,00,000 at 15%	30,00,000
2.	Total cost of Phases I and II (Rs. 34,00,000 +64,00,000)	98,00,000
3.	Total cost of Phases III and IV (Rs. 55,00,000 + Rs. 68,00,000)	1,23,00,000
4.	Total cost of all 4 phases	2,21,00,000
5.	Total loan	2,00,00,000
6.	Interest on loan used for Phases I & II, based on proportionate Loan amount = 30,00,000/2,21,00,000 x 98,00,000	13,30,317 (approx.)
7.	Interest on loan used for Phases III & IV, based on proportionate Loan amount = 30,00,000/2,21,00,000 x 1,23,00,000	16,69,683 (approx.)

Accounting treatment:

1. For Phase I and Phase II

Since Phase I and Phase II have become operational at the mid of the year, half of the interest amount of Rs. 6,65,158.50 (i.e. Rs. 13,30,317/2) relating to Phase I and Phase II should be capitalized (in the ratio of asset costs 34:64) and added to respective assets in Phase I and Phase II and remaining half of the interest amount of Rs. 6,65,158.50 (i.e. Rs. 13,30,317/2) relating to Phase I and Phase II should be expensed during the year.

2. For Phase III and Phase IV

Interest of Rs. 16,69,683 relating to Phase III and Phase IV should be held in Capital Work-in-Progress till assets construction work is completed, and thereafter capitalized in the ratio of cost of assets. No part of this interest amount should be charged/expensed off during the year since the work on these phases has not been completed yet.

AS-17 SEGMENT REPORTING

Q61. ICAI RTP May 22 **REG. PAGE NO.**

(a) 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.

(b) 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?

Ans. (a) 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."

(b) 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.

Q62. ICAI RTP Nov 22 **REG. PAGE NO.**

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?

Ans. 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.

Q63. ICAI New May 23 **REG. PAGE NO.**

The Accountant of X. Ltd. provides the following data regarding its five segments:

Division	A	B	C	D	E	Total
Segment Assets	50	20	15	10	5	100
Segment Result	(85)	10	10	(15)	5	(75)
Segment Revenue	250	50	40	60	30	430

The 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

Ans. 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.

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 75% of total enterprise revenue is included in reportable segments.

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

On the basis of the result criteria, segments A, B, C and D are reportable segments (since their results in absolute amount are 10% or more of Rs. 100 crore).

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

Hence, the opinion of chief accountant that only segment A alone should be reported, is wrong as all segments are reportable except E.

AS-18 RELATED PARTY DISCLOSURES

Q64. ICAI RTP Nov 21 **REG. PAGE NO.**

(a) 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)?

(b) 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?

Ans. (a) 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.

(b) 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.

Q65. ICAI RTP May 22 REG. PAGE NO.

(a) 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?

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

Ans. (a) 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

(b) 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.

Q66. ICAI New May 23 REG. PAGE NO.

Answer the following with respect to AS-18:

(i) ABC Ltd. sold goods of Rs. 2,00,000 to its associate company for the 1stquarter ending 30.06.2022. After that the related party relationship ceased to exist. However, goods were supplied to any other ordinary customer. Decide whether transactions of the entire year have to be disclosed as related party transaction.

(ii) If the majority of directors of Arjun Ltd. constitute the majority of the Board of another Company Bheem Ltd. in their individual capacity as professionals (and not by virtue of their being Directors in Arjun Ltd.). Are both the companies related?

(iii) Asha Ltd. sells all the manufactured furniture of Rs. 1,00,00,000 to Sasha Ltd, as per agreement. Sasha Ltd. is the only customer to Asha Ltd. In the financial statements, Asha Ltd. wants to present Sasha company as a related party. Comment on the disclosure requirement.

Ans. (i) As per AS 18, parties are considered to be related if any time during the reporting period one party has the ability to control the other party or exercise significant influence over the other party. Transactions of ABC Ltd. with its associate company for the first quarter ending 30.06.2022 only are required to be disclosed as related party transactions as the company has the ability to exercise significant influence only till 30.6.2022.

The transactions for the period in which related party relationship did not exist need not be reported.

(ii) In the given case, Arjun Ltd. cannot be said to control the composition of board of directors of Bheem Ltd. as the directors have been appointed in their indivi dual capacity as professionals and not by virtue of their being directors in Arjun Ltd.

Hence, it cannot be concluded that the companies are related merely because the majority of the directors of one company became the majority of the directors of the second in their individual capacity as professionals.

(iii) In the context of AS 18, a single customer, supplier, franchiser, distributor, or general agent with whom an enterprise transacts a significant volume of business cannot be construed as Related Party Relationship merely by virtue of the resulting economic dependence. There is an economic dependence between the companies but no one controls or exercise significant influence on the other.

In the given case, Asha Ltd. need not report Sasha Company as its related party in its financial statements.

Q67. ICAI MTP Nov 20,May 22 Sr. I, Nov 23 Sr. II **REG. PAGE NO.**

Mr. Arnav a relative of key management personnel received remuneration of Rs. 3,00,000 for his services in the company for the period April 1, 2019 to June 30, 2019. On July 1, 2019 he left the job.

Should Mr. Arnav be identified as Related Party at the closing date i.e. March 31, 2020 for the purposes of AS 18?

(ii) A limited company sold goods to its associate company for the 1st quarter ending June 30, 2020. After that, the related party relationship ceased to exist. However, goods were supplied continuously even after June 30, 2020 as was supplied to another ordinary customer. Does this require disclosure as related party transaction for the entire financial year?

Ans. (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. Arnav a relative of key management personnel should be identified as related party as at the closing date i.e. on 31.3.2020.

(ii) As per AS 18, transactions of company with its associate company for the first quarter ending 30.06.2020 only are required to be disclosed as related party transactions. The transactions for the period in which related party relationship did not exist need not be reported.

AS-19 LEASES

Q68. ICAI MTP May 18, Nov 18 **REG. PAGE NO.**

A Ltd. sold machinery having WDV of Rs. 40 lakhs to B Ltd. for Rs. 50 lakhs and the same machinery was leased back by B Ltd. to A Ltd. The lease back is operating lease. Explain the accounting treatment as per AS 19 in the following cases:

(i) Sale price of Rs. 50 lakhs is equal to fair value.
(ii) Fair value is Rs. 45 lakhs and sale price is Rs. 38 lakhs.
(iii) Fair value is Rs. 40 lakhs and sale price is Rs. 50 lakhs.
(iv) Fair value is Rs. 46 lakhs and sale price is Rs. 50 lakhs
(v) Fair value is Rs. 35 lakhs and sale price is Rs. 39 lakhs.

Ans. Following will be the treatment in the given cases:

(i) When sales price of Rs. 50 lakhs is equal to fair value, A Ltd. should immediately recognise the profit of Rs. 10 lakhs (i.e. 50 – 40) in its books.

(ii) 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 recognised by A Ltd. in its books provided loss is not compensated by future lease payment.

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

(iv) When fair value is Rs. 46 lakhs & sales price is Rs. 50 lakhs, profit of Rs. 6 lakhs (46-40) to be immediately recognised in its books and balance profit of Rs. 4 lakhs (50-46) is to be amortised/deferred over lease period.
(v) When fair value is Rs. 35 lakhs & sales price is Rs. 39 lakhs, then the loss of Rs. 5 lakhs (40-35) to be immediately recognised by A Ltd. in its books and profit of Rs. 4 lakhs (39-35) should be amortised/deferred over lease period.

Q69. ICAI MTP Nov 20, Dec 21 Sr. I **REG. PAGE NO.**

Monu Ltd. sold machinery having WDV of Rs. 400 lakhs to Sonu Ltd. for Rs. 500 lakhs and the same machinery was leased back by Sonu Ltd. to Monu Ltd. The lease back was in nature of operating lease.
Explain the accounting treatment as per AS 19 in the following cases:
(i) Sale price of Rs. 500 lakhs is equal to fair value.
(ii) Fair value is Rs. 450 lakhs and sale price is Rs. 380 lakhs.
(iii) Fair value is Rs. 400 lakhs and sale price is Rs. 500 lakhs.
(iv) Fair value is Rs. 460 lakhs and sale price is Rs. 500 lakhs
Ans. Following will be the treatment in the given cases:
(i) When sales price of Rs. 500 lakhs is equal to fair value, Monu Ltd. should immediately recognise the profit of Rs. 100 lakhs (i.e. 500 – 400) in its books.
(ii) When fair value of leased machinery is Rs. 450 lakhs & sales price is Rs. 380 lakhs, then loss of Rs. 20 lakhs (400 – 380) to be immediately recognised by Monu Ltd. in its books provided loss is not compensated by future lease payment.
(iii) When fair value is Rs. 400 lakhs & sales price is Rs. 500 lakhs then, profit of Rs. 100 lakhs is to be deferred and amortised over the lease period.
(iv) When fair value is Rs. 460 lakhs & sales price is Rs. 500 lakhs, profit of Rs. 60 lakhs (460-400) to be immediately recognised in its books and balance profit of Rs. 40 lakhs (500-460) is to be amortised/deferred over lease period.

Q70. ICAI MTP Dec 21 Sr. II, May 23 Sr. II **REG. PAGE NO.**

S. Square Private Limited has taken machinery on finance lease from S.K. Ltd. The information is as under:
Lease term = 4 years
Fair value at inception of lease = Rs. 20,00,000
Lease rent = Rs. 6,25,000 p.a. at the end of year
Guaranteed residual value = Rs. 1,25,000
Expected residual value = Rs. 3,75,000
Implicit interest rate = 15%
Discounted rates for 1st year, 2nd year, 3rd year and 4th year are 0.8696, 0.7561, 0.6575 and 0.5718 respectively.
You are required to calculate the value of the lease liability as per AS-19 and also disclose impact of this on Balance sheet and Profit & loss account at the end of year 1.
Ans. According to AS 19 "Leases", the lessee should recognise the lease as an asset and a liability at an amount equal to the lower of the fair value of the leased asset at the inception of the finance lease and the present value of the minimum lease payments from the standpoint of the lessee.

Year	Minimum Lease Payment (Rs.)	Internal rate of return (Discount rate @15%)	Present value (Rs.)
1	6,25,000	0.8696	5,43,500
2	6,25,000	0.7561	4,72,563
3	6,25,000	0.6575	4,10,937
4	7,50,000*	0.5718	4,28,850
Total	26,25,000		18,55,850

Present value of minimum lease payments Rs. 18,55,850 is less than fair value at the inception of lease i.e. Rs. 20,00,000, therefore, the asset and corresponding lease liability should be recognised at Rs. 18,55,850 as per AS 19.

AS-20 EARNINGS PER SHARE

Q71. ICAI RTP May 21 **REG. PAGE NO.**

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.

Ans. 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.

Q72. ICAI RTP Nov 21 **REG. PAGE NO.**

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?

Ans. 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.

Q73. ICAI RTP May 22 **REG. PAGE NO.**

(a) 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.

(b) 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?

Ans.(a) 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.

(b) 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)

Q74. ICAI New May 18, MTP Dec 21 Sr. I, MTP May 22 Sr. I, May 23 Sr. I REG. PAGE NO.

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".

Ans. Basic Earnings per share (EPS) = $\frac{\text{Net profit attributable to equity shareholders}}{\text{Weighted average number of equity shares outstanding during the year}}$

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

= 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 (Rs.)	Amount paid per share (Rs.)	Weighted Average no. of Equity Shares
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

Q75. ICAI New May 19 REG. PAGE NO.

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

Ans. (a) Calculation of Basic Earning Per Share

Basic EPS = $\frac{\text{Net Profit for the Current Year}}{\text{No. of Equity Shares}}$

$\frac{2,50,00,000}{50,00,000}$

Basic EPS per share = Rs.5

Calculation of Diluted Earning Per Share

Diluted EPS = Adjusted Net Profit for the Current Year

Weighted Average no. of Equity Shares

Adjusted net profit for the current year .

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.)

Q75. ICAI New Nov 19, RTP May 23 **REG. PAGE NO.**

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 isRs. 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.

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

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

Theoretical ex-rights fair value per share = Rs. 100.86

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.

AS-22 ACCOUNTING FOR TAXES ON INCOME

Q76.ICAI New Nov 22, Similar RTP May 21 **REG. PAGE NO.**

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 in allowed in the 1st year for income tax purpos, 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.

Ans. Statement of profit and Loss for the year ended 31st March, 2022 (An Extract)

	Rs.
Profit before taxes and depreciation	1,28,000
Less: Depreciation (56,000+ 6,000)	62,000
Profit before tax	66,000
Less: Current tax (W.N)	(32,400)
Deferred Tax	Nil
Profit after tax	33,600

Working Note:

Computation of taxable income

	Rs.
Profit before taxes and depreciation	1,28,000
Less: Depreciation (38,000+ 24,000)	62,000
	66,000
Add: Donation*	15,000
	81,000
Current tax (40%)	32,400

Note: The profit of Rs. 1,28,000 given in the question is before depreciation and taxes. It has been considered that this amount is after making adjustment of donation amounting Rs.15,000.

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

Transactions	Nature of Difference	Effect	Amount
(1) Difference in depreciation (old machinery)	Timing Difference	Reversal of DTL	Rs. 18,000 (56,000 – 38,000) x 40% = (+) Rs. 7,200
(2) Depreciation on new machinery	Timing Difference	Creation of DTL	Rs. 18,000 (24,000 – 6,000) x 40% = (-) Rs. 7,200
(3) Donation to private trusts	Permanent difference	Not applicable	-
Net Effect of Deferred Tax			NIL

Q77. ICAI RTP Nov 20 REG. PAGE NO.

(a) Write short note on Timing differences and Permanent differences as per AS 22

(b) 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%.

__Ans.__ (a) 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.

(b) Table showing calculation of deferred tax asset / liability

Particulars	Amount (Rs.)	Timing Difference	Deferred tax	Amount @30% (Rs.)
Excess Depreciation as per tax records (Rs. 10,00,000-Rs. 4,00,000)	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

Q78. ICAI RTP Nov 21 REG. PAGE NO.

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.

Ans. 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.

AS-24 DISCONTINUING OPERATIONS

Q79. ICAI RTP May 21 REG. PAGE NO.

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.

Ans. 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.

Q80. ICAI RTP Nov 21 REG. PAGE NO.

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

Ans. 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.

Q81. ICAI RTP Nov 22 REG. PAGE NO.

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

Ans. 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.

Q82. ICAI SM Q.6 **REG. PAGE NO.**

What are the initial disclosure requirements of AS 24 for discontinuing operations?

Ans. 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.

AS-26 INTANGIBLE ASSETS

Q83. ICAI New Nov 19, RTP May 23 **REG. PAGE NO.**

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.

Ans. 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 corre ct treatment by debiting the sum of 50 lakhs to Profit and Loss Account.

Q84. ICAI New Nov 20 **REG. PAGE NO.**

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 Rs. 75 Lacs. Determine the amortization cost of the patent for each of the above years as per Accounting Standard 26.

Ans. 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.

Q85.ICAI New Dec 21 **REG. PAGE NO.**

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

Further expenditure incurred on the process for the financial year ending 31st March 2021 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 future 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 2020;

(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.

Ans. As per AS 26 Rs.Intangible AssetsRs.

(i) Expenditure 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

Q86. ICAI RTP May 18, RTP Nov 19, RTP Nov 22 REG. PAGE NO.

K Ltd. launched a project for producing X in October 2016. The Company incurred Rs. 40 lakhs towards Research and Development expenses upto 31st March, 2017. Due to prevailing market conditions, the management comes to conclusions 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.

You are required to advise the company as per applicable Accounting Standard.

Ans. As per provisions 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 derecognized 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, 2017.

Q87. ICAI RTP Nov 18 REG. PAGE NO.

Desire Ltd. acquired a patent at a cost of Rs. 1,00,00,000 for a period of 5 years and the product life-cycle is also 5 years. The company capitalized the cost and started amortizing the asset on SLM. After two years it was found that the product life-cycle may continue for another 5 years from then. The net cash flows from the product during these 5 years were expected to be Rs. 45,00,000, Rs. 42,00,000, Rs. 40,00,000, Rs. 38,00,000 and Rs. 35,00,000.

Patent is renewable and company changed amortization method from 3rd year (i.e. from SLM to ratio of expected new cash flows).

You are required to compute the amortization cost of the patent for each of the years 1st year to 7th year)

Ans. Desire Limited amortised Rs. 20,00,000 per annum for the first two years i.e. Rs. 40,00,000. The remaining carrying cost can be amortized during next 5 years on the basis of net cash flows arising from the sale of the product. The amortisation may be found as follows:

Year	Net cash flows (Rs.)	Amortization Ratio	Amortization Amount (Rs.)
I	-	0.200	20,00,000
II	-	0.200	20,00,000
III	45,00,000	0.225	13,50,000
IV	42,00,000	0.21	12,60,000
V	40,00,000	0.20	12,00,000
VI	38,00,000	0.19	11,40,000
VII	35,00,000	0.175	10,50,000
Total	2,00,00,000	1.000	1,00,00,000

It may be seen from above that from third year onwards, the balance of carrying amount i.e., Rs. 60,00,000 has been amortized in the ratio of net cash flows arising from the product of Desire Ltd

Q88. ICAI RTP May 19 REG. PAGE NO.

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 crores 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?

Ans. According to AS 26 Rs.Intangible AssetsRs., "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.

Q89. ICAI RTP May 20 **REG. PAGE NO.**

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

Ans. 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
		1.00	1200

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

AS-29 PROVISIONS, CONTINGENT LIABILITIES AND CONTINGENT ASSETS

Q91. ICAI RTP Nov 19, MTP May 22 Sr. I **REG. PAGE NO.**

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.

Ans. 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.

Q92. ICAI RTP May 20, MTP May 21 **REG. PAGE NO.**

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 31 st Dec. 2019, it goes into liquidation. (Balance Sheet date 31-3-19).

Ans. (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.

Q93. ICAI RTP Nov 20 REG. PAGE NO.

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

(b) 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 31 st March, 2019, in line with provisions of AS 29?

Ans. (a) 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.

(b) 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.

Q94. ICAI RTP May 21 **REG. PAGE NO.**

(a) 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.

(b) Explain whether provision is required in the following situations in li ne 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.

<u>Ans.</u> (a) 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.

(b) (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.

Q95. ICAI RTP Nov 21 **REG. PAGE NO.**

(a) 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.

(b) An oil company has been contaminating land for several years. It does not clean up because there is 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?

Ans. (a) 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.

(b) 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.

Q96. ICAI RTP May 22, RTP Nov 22 REG. PAGE NO.

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.

Ans. 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.

Q97. ICAI MTP Dec 21 Sr. II, May 23 Sr. II **REG. PAGE NO.**

An airline is required by law to overhaul its aircraft once in every five years. The pacific Airlines which operate aircrafts does not provide any provision as required by law in its final accounts. You are required to comment on the validity of the treatment done by the company in line with the provisions of AS 29.

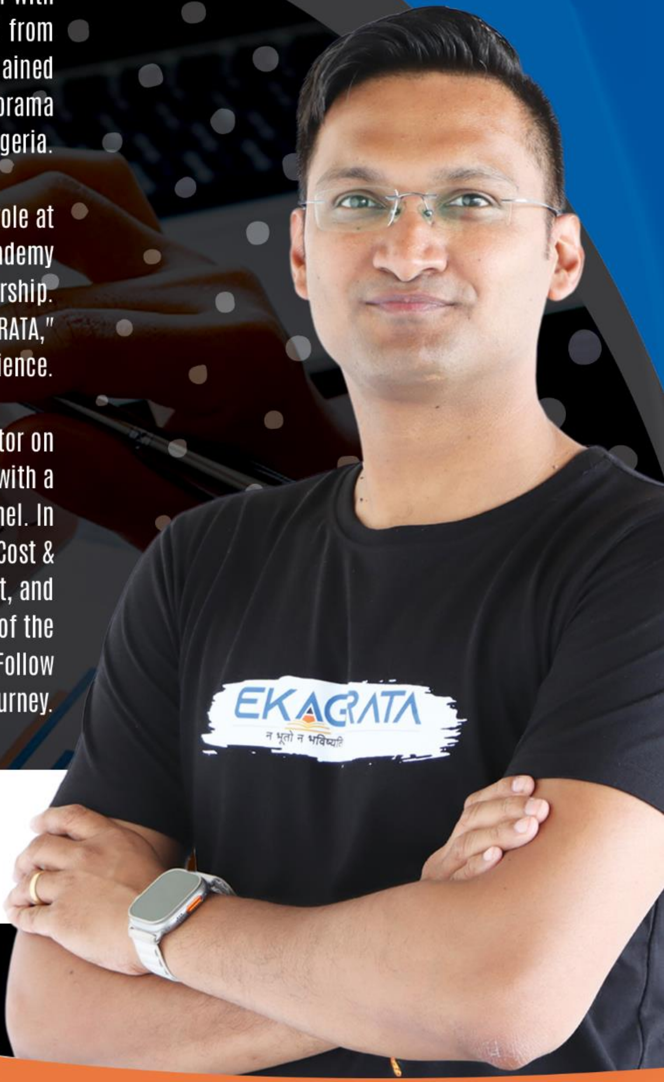
Ans. A provision should be recognized only when an enterprise has a present obligation arising from a past event or obligation. In the given case, there is no present obligation but a future one, therefore no provision is recognized as per AS 29.

The cost of overhauling aircraft is not recognized as a provision because it is a future obligation and the incurring of the expenditure depends on the company's decision to continue operating the aircrafts. Even a legal requirement to overhaul does not require the company to make a provision for the cost of overhaul because there is no present obligation to overhaul the aircrafts. Further, the enterprise can avoid the future expenditure by its future action, for example by selling the aircraft. However, an obligation might arise to pay fines or penalties under the legislation after completion of five years. Assessment of probability of incurring fines and penalties depends upon the provisions of the legislation and the stringency of the enforcement regime. A provision should be recognized for the best estimate of any fines and penalties if airline continues to operate aircrafts for more than five years.

Anshul Agrawal, a Chartered Accountant and Company Secretary, is a passionate teacher with a remarkable academic background. He achieved both his professional degrees in 2011 from Pune, excelling in his first attempt. Hailing from Jodhpur and raised in Amravati, he gained industry experience at Deloitte Haskins and Sells, Pune, and internationally at Indorama Eleme Petrochemicals Ltd., Nigeria.

His teaching journey began in his early student days, evolving into a professional role at Zaware's Professional Academy before becoming the Director. In 2020, he joined Unacademy and swiftly became a leading CA educator, boasting over 200 million minutes of viewership. Despite a setback in August 2023, he rebounded and established his brand, "EKAGRATA," showcasing resilience.

Anshul Agrawal is a prominent figure on YouTube, ranked as the No.1 CA educator on Unacademy. His presence extends beyond teaching; he is a professional Vlogger with a self-titled channel. An influential speaker, he featured on the popular Josh Talk channel. In addition to this book, he authored others on CA-Intermediate Accounting and Cost & Management Accounting. Known for his success mantras of #Patience, #Trust, and #SelfReliance, Agrawal is recognized for his strong leadership as the Vice-Chairman of the Pune Branch of WICASA (Western Indian Chartered Accountant Student's Association). Follow him for more updates on his journey.



CA CS ANSHUL AGRAWAL

FOUNDER & DIRECTOR,
EKAGRATA EDUSERV PVT. LTD.

"न भूतो
न भविष्यति"

Published By
ALLBOOKS

MRP: Rs. 1299/-
(All Volumes)

Distributed By
EKAGRATA
न भूतो न भविष्यति!