मेहनत अगर आदत बन जाए तो, कामयाबी मुकद्दर बन जाती है!

CA INTER
ADVANCED ACCOUNTING

182 TOP MOST IMPORTANT QUESTIONS

FOR

SEPTEMBER 2024

BY

CA P. S. Beniwal

Faculty of CA Inter - Advance Accounting
Faculty of CA Final-Financial Reporting
Member of IND AS Implementation Committee of ICAI

Contact Number: 9990301165, 9318445989

Telegram channel: "t.me/capsbeniwalclasses"

Website: capsbeniwal.com

Youtube: https://bit.ly/332doKz

LINK OF IMPORTANT VIDEOS

ICAI STUDY MATERIAL BATCH

Lecture 1: AS 16 AND AS 12 https://youtu.be/Nbvhs84a4lA?si=y_86D7Rpc2BanVhj

Lecture 2: AS 10 AND AS 2 https://youtu.be/25Wumsd3d5M?si=KgDYCGr1rjxgamDM

Lecture 3: Investment Accounting - AS 13 https://youtu.be/KDWr0sGIZBY?si=XS_exHfCmvwuB-kq

Lecture 4: AS 19 AND AS 20 https://youtu.be/yqoqzkOmWok?si=f3zvmTH2YRP6HKFD

Lecture 5: INTERNAL RECONSTRUCTION https://youtu.be/ZYqCrg-KxcE?si=c_PVIivsqutfa8qN

Lecture 6: AS 11, AS 7 AND AS 9 https://youtu.be/itLouZQ7tBw?si=52KCcva1y0bvOTSl

Lecture 7: BUY-BACK OF SECURITIES https://youtu.be/qSqRIXY_Xf8?si=Ssjc-vjJt_blp1bG

Lecture 8: AS 22, AS 15 AND AS 1 https://youtu.be/jAOnEBZO3AM?si=t2G0MB9PZx2Cu6JA

Lecture 9: AS 28 AND AS 26 https://youtu.be/UriJZeK8Ufg?si=uPx5egiEQLZxULpd

Lecture 10: AS 17, AS 18, AS24 AND AS 25 https://youtu.be/ne59H6FgUKc?si=3b1p13-88oegYyho

Lecture 11: AS 5, AS 4, AS 29, Applicability of AS & IND AS and Framework
https://youtu.be/jAl7Bu9NiME?si=-WoEoz6Lx6VGWXSQ

Lecture 12: AMALGAMATION OF COMPANIES - AS 14
https://youtu.be/9BFKIW02OR8?si=kH5YBGyZQvYH_YhT

Lecture 13: FINANCIAL STATEMENTS OF COMPANIES & SCHEDULE III
https://youtu.be/IIwwfPBn7vs?si=1UK4vAvBQzaZgv8d

Lecture 14: BRANCH https://youtu.be/L56SQXRvQvg?si=IOkOGVrr6VJH_-YA

Lecture 15: CASH FLOW STATEMENT - AS 3 https://youtu.be/-iAGNUGDqm0?si=MRWnThEslz1kkztv

Lecture 16: CONSOLIDATED FINANCIAL STATEMENTS (AS 21, AS 23 & AS 27)
https://youtu.be/Ge7Qmih0Xp4

Play list of all the lectures https://www.youtube.com/watch?v=Nbvhs84a4lA&list=PLqE5aHjZDY868-krklrXH3o4WHRtSwwT9

Play list of all RTP and MTP

https://www.youtube.com/watch?v=NrbplGgcWdE&list=PLqE5aHjZDY87bdP2tM6zKaK1K5wZRriZe

182 TOP MOST IMPORTANT QUESTIONS FOR SEPTEMBER 24

CA INTER – ADVANCED ACCOUNTING

INDEX

Telegram Link: https://t.me/capsbeniwalclasses

Youtube link: https://youtube.com/@PSBeniwalClasses

Instagram ID: https://www.instagram.com/capsbeniwal5/

WWW.CAPSBENIWAL.COM

ALL THE BEST

CA P.S. Beniwal

CONSOLIDATED FINANCIAL STATEMENTS (AS 21, 23 AND 27)

1. On 31st March, 2004 the Balance Sheets of H Ltd. and its subsidiary S Ltd. stood as follows:

	H Ltd.	S Ltd.
Liabilities	Rs. in lakhs	Rs. in lakhs
Share Capital:		
Authorised	15,000	6,000
Issued and Subscribed:		
Equity Shares of Rs. 10 each, fully paid up	12,000	4,800
General Reserve	2,784	1,380
Profit and Loss Account	2,715	1,620
Bills Payable	372	160
Sundry Creditors	1,461	854
Provision for Taxation	855	394
Dividend Payable	1,200	-------
	21,387	**9,208**

	H Ltd.	S Ltd.
Assets	Rs. in lakhs	Rs. in lakhs
Land and Buildings	2,718	-----
Plant and Machinery	4,905	4,900
Furniture and Fittings	1,845	586
Investments in shares in S Ltd.	3,000	-----
Stock	3,949	1,956
Debtors	2,600	1,363
Cash and Bank Balances	1,490	204
Bills Receivable	360	199
Sundry Advances	520	-------
	21,387	**9,208**

The following information is also provided to you:

(a) H Ltd. purchased 180 lakh shares in S Ltd. on 1st April, 2003 when the balances to General Reserve and Profit and Loss Account of S Ltd. stood at Rs. 3,000 lakh and 1,200 lakh respectively.

(b) On 4th July, 2003 S Ltd. declared a dividend @ 20% for the year ended 31st March, 2003. H Ltd. credited the dividend received by it to its Profit and Loss Account.

(c) On 1st January, 2004 S Ltd. issued 3 fully paid-up shares for every 5 shares held as bonus shares out of balances to its general reserve as on 31st March, 2003.

(d) On 31st March, 2004 all the bills payable in S Ltd.'s balance sheet were acceptances in favour of H Ltd. But on that date, H Ltd. held only Rs. 45 lakh of these acceptances in hand, the rest having been endorsed in favour of its creditors.

(e) On 31st March, 2004 S Ltd.'s stock included goods which it had purchased for Rs. 100 lakh from H Ltd. which made a profit @ 25% on cost.

Prepare a Consolidated Balance Sheet of H Ltd. and its subsidiary S Ltd. as at 31st March, 2004 bearing in mind the requirements of AS 21.

Solution: Consolidated Balance Sheet of H Ltd. and its subsidiary S Ltd. as at 31st March, 20X1

Particulars	***Note No.***	***(₹ in Lacs)***
I. Equity and Liabilities		
(1) **Shareholder's Funds**		
(a) Share Capital	1	12,000
(b) Reserves and Surplus	2	7,159
(2) **Minority Interest [W.N.6]**		3,120
(3) **Current Liabilities**		
(a) Trade payables	3	2,802
(b) Short term provisions	4	1,249
(c) Other current liabilities	5	1,200
Total		27,530

II.	**Assets**			
	(1)	**Non-current assets**		
		Property, Plant and Equipment	6	14,954
	(2)	**Current assets**		
	(a)	Inventories	7	5,885
	(b)	Trade receivables	8	4,477
	(c)	Short term loans and advances	9	520
	(d)	Cash and cash equivalents	10	1,694
		Total		27,530

Notes to Accounts

			(₹ in lacs)	*(₹ inlacs)*
1.	**Share Capital**			
	Authorized share capital			15,000
	Equity shares of ₹10 each, fully paid up			
	Issued and Subscribed:			
	Equity shares of ₹ 10 each, fully paid up			12,000
	Total			12,000
2.	**Reserves and surplus**			
	Capital Reserve (Note 5)		1,320	
	General Reserve (2,784 + 108)		2,892	
	Profit and Loss Account:			
	H Ltd.	2,715		
	Less: Dividend wrongly credited 360			
	Unrealized Profit 20	(380)		
		2,335		
	Add: Share in S Ltd.'s Revenue profits	612	2,947	
	Total			7,159
3.	**Trade payables**			
	Creditors			
	H Ltd. 1,461			
	S Ltd. 854		2,315	
	Bills Payable			
	H Ltd. ₹ 372			
	S Ltd. ₹ 160			
	₹ 532			
	Less: Mutual owing ₹ (45)		487	2,802

4.	**Short term provisions**			
	Provision for Taxation			
	H Ltd.		855	
	S Ltd.		394	
	Total			1,249
5.	**Other current liabilities**			
	Dividend payable			
	H Ltd.			1,200
6.	**Property, plant and equipment**			
	Land and Buildings			
	H Ltd.		2,718	
	Plant and Machinery			
	H Ltd.	₹ 4,905		
	S Ltd.	₹ 4,900	9,805	
	Furniture and Fittings			
	H Ltd.	₹ 1,845		
	S Ltd.	₹ 586	2,431	
	Total			14,954
7.	**Inventories**			
	Stock			
	H Ltd.		3,949	
	S Ltd.		1,956	
			5,905	
	Less: Unrealized profit		(20)	5,885
8.	**Trade receivables**			
	Debtors			
	H Ltd.	₹ 2,600		
	S Ltd.	₹ 1,363	3,963	
	Bills Receivable			
	H Ltd.	₹ 360		
	S Ltd.	₹ 199		
		₹ 559		
	Less: Mutual Owing	₹ (45)	514	4,477
9.	**Short term loans and advances**			
	Sundry Advances			520
10.	**Cash and cash equivalents**			
	Cash and Bank Balances			1,694

Share holding pattern of S Ltd.

Shares as on 31st March, 20X1 (Includes bonus shares issued on 1st January, 20X1)	480 lakh shares (4,800 lakhs/ ₹ 10)
H Ltd.'s holding as on 1st April, 20X0	180 lakhs
Add: Bonus received on 1st January, 20X1	108 lakhs (180 / 5 × 3)
Total H Ltd.'s holding as on 31st March, 20X1	288 lakhs i.e. 60 % [288/480×100]
Minority Shareholding	40%

Working Notes:

1. S Ltd.'s General Reserve Account

	₹ in lakhs		₹ in lakhs
To Bonus to equity shareholders (WN-8)	1,800	By Balance b/d	3,000
To Balance c/d	1,380	By Profit and Loss A/c (Balancing figure)	180
	3,180		3,180

2. S Ltd.'s Profit and Loss Account

	₹ in lakhs		₹ in lakhs
To General Reserve [WN 1]	180	By Balance b/d	1,200
To Dividend paid (20% on ₹3,000 lakhs)	600	By Net Profit for the year* (Balancing figure)	1,200
To Balance c/d	1,620		
	2,400		2,400

***Out of ₹ 1,200 lakhs profit for the year, ₹ 180 lakhs has been transferred to reserves.**

3. Distribution of Revenue profits

	₹ in lakhs
Revenue profits (W. N. 2)	1,200
Less: Share of H Ltd. 60%	
(General Reserve ₹ 108 + Profit and Loss Account ₹ 612)	(720)
Share of Minority Shareholders (40%)	480

Note: The question can also be solved by taking ₹ 1,020 lakhs as post acquisition Profit and Loss balance and ₹ 180 lakhs as post acquisition General Reserve balance. The final answer will be same.

4. Calculation of Capital Profits

	₹ in lakhs
General Reserve on the date of acquisition less bonus shares (₹ 3,000 – ₹ 1,800)	1,200
Profit and loss account on the date of acquisition less dividend paid (₹ 1,200 – ₹ 600)	600
	1,800

H Ltd.'s share = 60% of ₹ 1,800 lakhs = ₹ 1,080 lakhs
Minority interest = ₹ 1,800 – ₹ 1,080 = ₹ 720 lakhs

5. Calculation of capital reserve

	₹ in lakhs
Paid up value of shares held (60% of ₹4,800)	2,880
Add: Share in capital profits [WN 4]	1,080
	3,960
Less: Cost of shares less dividend received (₹ 3,000 – ₹ 360)	(2,640)
Capital reserve	1,320

6. Calculation of Minority Interest

	₹ in lakhs
40% of share capital (40% of ₹ 4,800)	1,920
Add: Share in revenue profits [WN 3]	480

Share in capital profits [WN 4]	720
	3,120

7. Unrealized profit in respect of inventory

= ₹ 100 lakhs X 25 / 125

= ₹ 20 lakhs

8. Computation of bonus to equity shareholders

	₹ In lakhs
Shares as on 31 March 20X1 including bonus share issued on 1 January 20X1	4,800
Or we can say these are 1 + 3/5 or 8/5	
i.e. Shares before bonus issue should have been 4,800 ÷ 8/5	
Accordingly, bonus issue would be (4,800-3,000)	1,800

2. H Limited acquired 64000 Equity Shares of Rs. 10 each in S Ltd. as on 1st October, 2019. The Balance Sheets of the two companies as on 31st March, 2020 were as under:

Particulars	H Ltd. (Rs.)	S Ltd. (Rs.)
Equities and Liabilities:		
Equity Share Capital: Shares of Rs. 10 each	20,00,000	8,00,000
General Reserve (1st April, 2019)	9,60,000	4,20,000
Profit & Loss Account	2,28,800	3,28,000
Preliminary Expenses (1st April, 2019)	-	(20,000)
Bank Overdraft	3,00,000	-
Bills Payable	-	52,000
Trade Payables	1,66,400	80,000
Total	36,55,200	16,60,000
Assets:		
Land and Building	7,20,000	7,60,000
Plant & Machinery	9,60,000	5,40,000
Investment in Equity Shares of S Ltd.	12,27,200	-
Inventories	4,56,000	1,68,000
Trade Receivables	1,76,000	1,60,000
Bills Receivable	59,200	-
Cash in Hand	56,800	32,000
Total	36,55,200	16,60,000

Additional Information:

(1) The Profit & Loss Account of S Ltd. showed credit balance of Rs. 1,20,000 on 1st April, 2019. S Ltd. paid a dividend of 10% out of the same on 1st November, 2019 for the year 2018-19. The dividend was correctly accounted for by H Ltd.

(2) The Plant & Machinery of S Ltd. which stood at Rs. 6,00,000 on 1st April, 2019 was considered worth Rs. 5,20,000 on the date of acquisition by H Ltd. S Ltd. charges depreciation @ 10% per annum on Plant & Machinery.

Prepare consolidated Balance Sheet of H Ltd. and its subsidiary S Ltd. as on 31st March, 2020 as per Schedule III of the Companies Act, 2013.

Solution: Consolidated Balance Sheet of H Ltd. and its subsidiary, S Ltd. as at 31st March, 2020

Particulars	Note No.	(Rs.)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	20,00,000

	(b) Reserves and Surplus	2	13,07,200
	(2) Minority Interest (W.N 4)		2,96,400
	(3) Current Liabilities		
	(a) Trade Payables	3	2,98,400
	(b) Short term borrowings		3,00,000
	Total		42,02,000
II.	Assets		
	(1) Non-current assets		
	(i) Property, Plant and Equipment	4	29,34,000
	(ii) Intangible assets (W.N.5)		1,60,000
	(2) Current assets		
	(a) Inventories	5	6,24,000
	(b) Trade receivables	6	3,95,200
	(c) Cash & Cash equivalents (Cash)	7	88,800
	Total		42,02,000

Notes to Accounts

			Rs.	Rs.
1.	Share Capital			
	2,00,000 equity shares of Rs. 10 each			20,00,000
2.	Reserves and Surplus			
	Reserves		9,60,000	
	Profit & loss			
	H Ltd.	2,28,800		
	S Ltd. (As per W.N. 3)	1,18,400	3,47,200	13,07,200
3.	Trade Payables			
	H Ltd.		1,66,400	
	S Ltd. (80,000+52,000)		1,32,000	2,98,400
4.	Property, Plant and Equipment			
	Land and building			
	H Ltd.	7,20,000		
	S Ltd.	7,60,000	14,80,000	
	Plant & Machinery			
	H Ltd.	9,60,000		
	S Ltd. (As per W.N. 7)	4,94,000	14,54,000	29,34,000
5.	Inventories			
	H Ltd.		4,56,000	
	S Ltd.		1,68,000	6,24,000
6.	Trade Receivables			
	H Ltd.	1,76,000		
	S Ltd.	1,60,000	3,36,000	
	Bills receivable: H Ltd.		59,200	3,95,200
7.	Cash & Cash equivalents			
	Cash			
	H Ltd.		56,800	
	S Ltd.		32,000	88,800

Working Notes:

(1) Share holding pattern

Total Shares of S Ltd 80,000 shares
Shares held by H Ltd 64,000 shares i.e. 80 %;
Minority Shareholding 16,000 shares i.e. 20 %

(2) Capital profits of S Ltd.

	Rs.	Rs.
Reserve on 1st October, 2019 (Assumed there is no movement in reserves during the year and hence balance as on 1st October, 2019 is same as of 31st March 2020)		4,20,000
Profit & Loss Account Balance on 1st April, 2019	1,20,000	
Less: Dividend paid	(80,000)	40,000
Profit for year:		
Total Rs. 3,28,000 Less: Rs. 40,000 (opening balance)		
Rs. 2,88,000 Proportionate up to 1st October, 2019 on time basis (Rs. 2,88,000/2)		1,44,000
Reduction in value of Plant & Machinery (WN 6)		(50,000)
		5,54,000
Less: Preliminary expenses written off		(20,000)
Total Capital Profit		5,34,000
Holding company's share (5,34,000 X 80%)		4,27,200
Minority Interest (5,34,000 X 20%)		1,06,800

Note: Preliminary expenses as on 1st April, 2019 amounting Rs. 20,000 have been written off.

(3) **Revenue profits of S Ltd.**

Profit after 1st October, 2019 (3,28,000 - 40,000)/2		1,44,000
Less 10% depreciation on Rs.5,20,000 for 6 months	(26,000)	
Add: Depreciation already charged for 2nd half year on 6,00,000	30,000	4,000
		1,48,000
Holding company's share (1,48,000 X 80%)		1,18,400
Minority Interest (1,48,000 X 20%)		29,600

(4) Minority interest

Par value of 16,000 shares (8,00,000 X 20%)	1,60,000
Add: 1/5 Capital Profits [WN 2]	1,06,800
1/5 Revenue Profits [WN 3]	29,600
	2,96,400

(5) Cost of Control

Amount paid for 64,000 shares		12,27,200
Less:		
Par value of shares (8,00,000 X 80%)	6,40,000	
Capital Profits – share of H Ltd. [WN 2]	4,27,200	(10,67,200)
Cost of Control or Goodwill		1,60,000

(6) Calculation of revaluation loss on Plant and Machinery of S Ltd. on 1st October, 2019

	Rs.
Value of plant and machinery as on 1st April,2019	6,00,000
Less: Depreciation for the six months	(30,000)
Value of plant and machinery as on 1st October, 2019	5,70,000
Less: Plant and machinery valued by H Ltd. on 1st October,2019	(5,20,000)
Revaluation Loss	50,000

(7) Value of plant & Machinery of S Ltd. On 31st March,2020

Value of machinery on 1st October, 2019	5,20,000
Less: depreciation for next six month	(26,000)
	4,94,000

3. King Ltd. acquires 70% of equity shares of Queen Ltd. as on 31st March, 20X1 at a cost of ₹ 140 lakhs. The following information is available from the balance sheet of Queen Ltd. as on 31st March, 20X1:

	₹ in lakhs
Property, plant and equipment	240
Investments	110
Current Assets	140
Loans & Advances	30
15% Debentures	180
Current Liabilities	100

The following revaluations have been agreed upon (not included in the above figures):
Property, plant and equipment- up by 20% and Investments- down by 10%.
King Ltd. purchased the shares of Queen Ltd. @ ₹20 per share (Face value - ₹10).
Calculate the amount of goodwill/capital reserve on acquisition of shares of Queen Ltd.
Solution: Revalued net assets of Queen Ltd. as on 31st March, 20X1

	₹ in lakhs	₹ in lakhs
PPE [240 X 120%]		288
Investments [110 X 90%]		99
Current Assets		140
Loans and Advances		30
Total Assets after revaluation		557
Less: 15% Debentures	180.0	
Current Liabilities	100.0	(280)
Equity / Net Worth		277
King Ltd.'s share of net assets (70% of 277)		193.9
King Ltd.'s cost of acquisition of shares of Queen Ltd. (₹140 lakhs)		(140)
Capital reserve		53.9

4. The Profit and Loss Accounts of A Ltd. and its subsidiary B Ltd. for the year ended 31st March, 2018 are given below : (Rs ,000)

Incomes	A Ltd.	B Ltd.
Sales and other income	7,500	1,500
Increase in Inventory	1,500	300
Total	9,000	1,800
Expenses		
Raw material consumed	1,200	300
Wages and Salaries	1,200	225
Production expenses	300	150
Administrative expenses	300	150
Selling and distribution expenses	300	75
Interest	150	75

Depreciation	150	75
Total	3,600	1,050
Profit before tax	5,400	750
Provision for tax	1,800	300
Profit after tax	3,600	450
Dividend paid	1,800	225
Balance of Profit	1,800	225

The following information is also given:

(i) A Ltd sold goods of ₹ 180 Lakhs to B Ltd at cost plus 25%. (1/6 of such goods were still in inventory of B Ltd at the end of the year)
(ii) Administrative expenses of B Ltd include ₹ 8 Lakhs paid to A Ltd as consultancy fees.
(iii) Selling and distribution expenses of A Ltd include ₹15 Lakhs paid to B Ltd as commission.
(iv) A Ltd holds 72% of the Equity Capital of B Ltd. The Equity Capital of B Ltd prior to 2016-17 is ₹1,500 Lakhs

Prepare a consolidated Profit and Loss Account for the year ended 31st March, 2018.

Solution: Consolidated Statement of Profit & Loss of A Ltd. and its subsidiary B Ltd. for the year ended on 31st March, 2022

Particulars	Note No.	₹ in Lacs
I. Revenue from operations	1	8,797
II. Total revenue		8,797
III. Expenses		
Cost of Material purchased/consumed	3	1,770
Changes of Inventories of finished goods	2	(1,794)
Employee benefit expense	4	1,425
Finance cost	6	225
Depreciation and amortization expense	7	225
Other expenses	5	802
Total expenses		2,653
IV. Profit before Tax(II-III)		6,144
V. Provision for Taxation (1,800 + 300)		(2,100)
VI. Profit after Tax		4,044

Notes to Accounts

		₹ in Lacs	₹ in Lacs
1.	Revenue from Operations		
	Sales and other income		
	A Ltd.	7,500	
	B Ltd.	1,500	
		9,000	
	Less: Inter-company Sales	(180)	
	Consultancy fees received by A Ltd. from B Ltd.	(8)	
	Commission received by B Ltd. from A Ltd.	(15)	8,797
2.	Increase in Inventory		
	A Ltd.	1,500	
	B Ltd.	300	
		1,800	
	Less: Unrealized profits ₹ 180×1/6 x 25/125	(6)	1,794

3.	Cost of Material purchased/consumed		
	A Ltd.	1,200	
	B Ltd.	300	
		1,500	
	Less: Purchases by B Ltd. from A Ltd.	(180)	1,320
	Direct Expenses		
	A Ltd.	300	
	B Ltd.	150	450
			1,770
4.	Employee benefits and expenses		
	Wages and Salaries:		
	A Ltd.	1,200	
	B Ltd.	225	1,425
5.	Other Expenses		
	Administrative Expenses		
	A Ltd.	300	
	B Ltd.	150	
		450	
	Less: Consultancy fees received by A Ltd. from B Ltd.	(8)	442
	Selling and Distribution Expenses:		
	A Ltd.	300	
	B Ltd.	75	
		375	
	Less: Commission received from B Ltd. from A Ltd.	(15)	360
			802
6.	Finance Cost		
	Interest:		
	A Ltd.	150	
	B Ltd.	75	225
7.	Depreciation and Amortization		
	Depreciation:		
	A Ltd.	150	
	B Ltd.	75	225

5. H Ltd. acquire 70% of equity share of S Ltd. as on 1st January, 2011 at a cost of Rs. 5,00,000 when S Ltd. had an equity share capital of Rs. 5,00,000 and reserve and surplus of Rs. 40,000.
Both the companies follow calendar year as the accounting year.
In the four consecutive years, S Ltd. fared badly and suffered losses of Rs. 1,25,000, Rs. 2,00,000, Rs. 2,50,000 and Rs. 60,000 respectively. Thereafter in 2015, S Ltd. experienced turnaround and registered an annual profit of Rs. 25,000. In the next two years i.e. 2016 and 2017, S Ltd. recorded annual profits of Rs. 50,000 and Rs. 75,000 respectively. Show the Minority Interests and Cost of Control at the end of each year for the purpose of consolidation.
Solution: AS per AS21 consolidated Financial Statements; the losses applicable to the minority in a consolidated subsidiary may exceed the minority interest in the equity of the subsidiary. The excess, and any further losses applicable to the minority, are adjusted against the majority interest except to that the minority has a binding obligation to, and is able to, make good the the losses. If the subsidiary subsequently repots profits, all such profits are allocated to the majority until the minority,s share of losses previously absorbed by the majority has been recovered.

Accordingly,

Year	Details	Minority Interest (MI) (20%)	Minority's Share of losses borne by H Ltd.	Cost of Control (W.N. 2)
Minority Interest at the time of acquisition i.e. on 01.01.2011		1,62,000 (W.N 1)		1,22,000
For 2011	(1,25,000 x 30%)	(37,500)		
On 31.12.2011		1,24,500		1,22,000
For 2012	(2,00,000 x 30%)	(60,000)		
On 31.12.2012		64,500		1,22,000
For 2013	(2,50,000 x 30%)	(75,000)		
		(10,500)		
	Loss amounting Rs. 10,500 of minority borne by majority shareholders on application of AS 21	10,500	10,500	
On 31.12.2013		Nil	10,500	1,22,000
For 2014	(60,000 x 30%)	(18,000)		
	Loss amounting Rs. 18,000 of minority borne by majority shareholders on application of AS 21	18,000	18,000	
On 31.12.2014		Nil	28,500	1,22,000
For 2015	(25,000 X 30%)	7,500		
	On application of AS 21, profit transferred to majority shareholders	(7,500)	(7,500)	
On 31.12.2015		Nil	21,000	1,22,000
For 2016	(50,000 X 30%)	15,000		
	On application of AS 21, profit transferred to majority shareholders	(15,000)	(15,000)	
On 31.12.2016		Nil	6,000	1,22,000
For 2017	(75,000 X 30%)	22,500		
	On application of AS 21, profit transferred to majority shareholders to the extent earlier loss was borne by majority share holders	(6,000)	(6,000)	
On 31.12.2017		16,500	Nil	1,22,000

Working Notes:

(1) Calculation of Minority Interest as on 01.01.2011

	Total Amount (100%) (Rs)	Minority Interest (20%) (Rs)
Share Capital (30%)	5,00,000	1,50,000
Add: Share in Reserves (30%)	40,000	12,000
		1,62,000

(2) Calculation of Cost of Control

		Rs.
Cost of Investment		5,00.000
Less: Net Asset of S Ltd.		
Share Capital (5,00,000 X 70%)	3,50,000	
Share in Reserves (40,000 X 70%)	28,000	(3,78,000)
Goodwill		1,22,000

6. Long Limited acquired 60% stake in Short Limited for a consideration of Rs. 112 lakhs. On the date of acquisition Short Limited's Equity Share Capital was Rs. 100 lakhs, Revenue Reserve was Rs. 40 lakhs and balance in Profit & Loss Account was Rs. 30 lakhs. From the above information you are required to calculate Goodwill / Capital Reserve in the following situations:
(i) On consolidation of Balance Sheet.
(ii) If Long Limited showed the investment in subsidiary at a carrying amount of Rs. 104 lakhs.
(iii) If the consideration paid for acquiring the 60% stake was Rs. 92 lakhs.

Solution: **(Rs. in lakhs)**

60% of the Equity Share Capital Rs. 100 Lakhs	60
60% of Accumulated Reserve Rs. 70 Lakhs (40+30) Lakhs	42
Book value of shares of Short Ltd.	102

(i) Goodwill / Capital Reserve computation on consolidation of balance sheet:
Long Ltd. paid a positive differential of Rs. 10 Lakhs (112 - 102). This differential Rs. 10 Lakhs is called goodwill and is shown in the balance sheet under the head intangibles.
(ii) If Long Ltd. showed the investment in Short Ltd. at carrying amount of Rs. 104 Lakhs, then the goodwill will be Rs. 2 Lakhs.
(iii) If the consideration paid is Rs. 92 lakhs, then there would have been capital reserve amounting Rs. 10 Lakhs (102- 92).

7. Consider the following balance sheets of subsidiary B Ltd.:

	2008 (₹)	2009(₹)		2008 (₹)	2009(₹)
Share-Capital			Fixed Assets		
Issued & subscribed			Cost	3,20,000	3,20,000
5,000 equity shares			Less: Accumulated		
of Rs. 100 each	5,00,000	5,00,000	depreciation	48,000	96,000
Reserves & Surplus				2,72,000	2,24,000
Revenue reserves	2,86,000	7,14,000	Investments		
Current Liabilities &			at cost	—	4,00,000
Provisions:			Current Assets:		
Sundry Creditors	4,90,000	4,94,000	Stock	5,97,000	7,42,000
Bank overdraft	—	1,70,000	Sundry Debtors	5,94,000	8,91,000
Provision for taxation	3,10,000	4,30,000	Prepaid Expenses	72,000	48,000
			Cash at Bank	51,000	3,000
	15,86,000	**23,08,000**		**15,86,000**	**23,08,000**

Consider also the following information:
(a) B Ltd. is a subsidiary of A Ltd. Both the companies follow calendar year as the accounting year.
(b) A Ltd. values stocks on LIFO basis while B Ltd. used FIFO basis. To bring B Ltd.'s values in line with those of A Ltd. its value of stock is required to be reduced by Rs. 12,000 at the end of 2008 and Rs. 34,000 at the end of 2009.
(c) B Ltd. deducts 1% from sundry debtors as a general provision against doubtful debts.
(d) Prepaid expenses in B Ltd. include advertising expenditure carried forward of Rs. 60,000 in 2008 and Rs. 30,000 in 2009, being part of initial advertising expenditure of Rs. 90,000 in 2008 which is being written off over three years. Similar amount of advertising expenditure of A Ltd. has been fully written off in 2008.

Restate the balance sheet of B Ltd. as on 31st December, 2009 after considering the above information for the purpose of consolidation. Such restatement is necessary to make the accounting policies adopted by A Ltd. and B Ltd. uniform.

Solution: As per para 20 and 21 of AS 21, Consolidated financial statements: Consolidated financial statements should be prepared using uniform accounting policies for like transactions and other events in similar circumstances. If it is not practicable to use uniform accounting policies in preparing the consolidated financial statements, that fact should be disclosed together with the proportions of the items in the consolidated financial statements to which the different accounting policies have been applied.

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

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

Adjusted reserves of B Ltd.:

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

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

Restated Balance Sheet of B Ltd. as at 31st December, 2009

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

Notes to Accounts

			20X1 (₹)
1.	**Share capital**		
	5,000 equity shares of Rs 10 each, fully paid up		5,00,000
2.	**Reserves and Surplus**		
	General Reserves (refer to WN)		6,59,000
3.	**Short term borrowings**		
	Bank overdraft		1,70,000
4.	**Short term provisions**		
	Provision for taxation		4,30,000

5.	**Property, plant and equipment**		
	Cost		3,20,000
	Less: Depreciation		(96,000)
	Total		2,24,000
6.	**Inventory**		
	Actual inventory		7,42,000
	Less: Change in method of valuation		(34,000)
	Total		7,08,000
7.	**Trade receivables**		
	Actual trade receivables		8,91,000
	Add: Adjustment for provision		9,000
	Total		9,00,000
8.	**Other current Assets**		
	Prepaid expenses		48,000

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

	₹
Property, plant and equipment	10,50,000
Current Assets	6,45,000
1,50,000 equity shares of ₹ 10 each fully paid	15,00,000
Pre-incorporation profits	30,000
Profit and Loss Account	60,000
Trade payables	1,05,000

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

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

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

Calculate as on 31st March, 2021 (i) Cost of Control/Capital Reserve; (ii) Minority Interest; (iii) Consolidated Profit and Loss Account in each of the following cases:

(a) Before issue of bonus shares.

(b) Immediately after issue of bonus shares.

Solution:

Shareholding pattern

Particulars	**Number of Shares**	**% of holding**
a. P Ltd.		
(i) Purchased on 31.03.20X1	1,05,000	
(ii) Bonus Issue (1,05,000/2)	52,500	

	Total	1,57,500	70%
b.	Minority Interest	67,500	30%

Calculations of (i) Cost of Control/Capital Reserve; (ii) Minority Interest; (iii) Consolidated Profit and Loss Account as on 31st March, 20X3:

(a) Before issue of bonus shares

(i)	**Cost of control/capital reserve**	**₹**	**₹**
	Investment in Q Ltd.		12,00,000
	Less: Face value of investments (Share Capital)	10,50,000	
	Capital profits (W.N.)	63,000	(11,13,000)
	Cost of control (i.e., Goodwill)		87,000
(ii)	**Minority Interest**		**₹**
	Share Capital		4,50,000
	Capital profits (W.N.)		27,000
	Revenue profits (W.N.)		6,79,500
			11,56,500
(iii)	**Consolidated profit and loss account – P Ltd.**		**₹**
	Balance		15,75,000
	Add: Share in revenue profits of Q Ltd. (W.N.)		15,85,500
			31,60,500

(b) Immediately after issue of bonus shares

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

	Add: Share in revenue profits of Q Ltd. (W.N.)		10,60,500
			26,35,500

Working Note:
Analysis of Profits of Q Ltd.

	Capital Profits (Pre-acquisition)	Revenue Profits (Post-acquisition)	
	(Before and after issue of bonus shares) ₹	Before Bonus Issue ₹	After Bonus Issue ₹
Pre-incorporation profits	30,000		
Profit and loss account on 31.3.20X1	60,000		
	90,000		
General reserve*		19,05,000	19,05,000
Less: Bonus shares			(7,50,000)
			11,55,000
Profit for period of 1st April, 20X1 to 31st March, 20X3 (₹ 4,20,000 – ₹ 60,000)		3,60,000	3,60,000
		22,65,000	15,15,000
P Ltd.'s share (70%)	63,000	15,85,500	10,60,500
Minority's share (30%)	27,000	6,79,500	4,54,500

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

9. Variety Ltd. holds 46% of the paid-up share capital of VR Ltd. The shares were acquired at a market price of ₹ 17 per share. The balance of shares of VR Ltd. are held by a foreign collaborating company. A memorandum of understanding has been entered into with the foreign company providing for the following:
(a) The shares held by the foreign company will be sold to Variety Ltd. The price per share will be calculated by capitalising the yield at 15%. Yield, for this purpose, would mean 40% of the average of pre-tax profits for the last 3 years, which were ₹ 30 lakhs, ₹ 40 lakhs and ₹ 65 lakhs.
(b) The actual cost of the shares to the foreign company was ₹ 5,40,000 only. The profit that would accrue to them would be taxable at an average rate of 30%. The tax payable will be deducted from the proceeds and Variety Ltd. will pay it to the Government.
(c) Out of the net consideration, 50% would be remitted to the foreign company immediately and the balance will be an unsecured loan repayable after two years.
The above agreement was approved by all concerned for being given effect to on 1.4.20X1. The total assets of VR Ltd. as on 31st March, 20X1 was ₹ 1,00,00,000. It was decided to write down Property, Plant and Equipment by ₹ 1,75,000. Current liabilities of VR Ltd. as on the same date were ₹ 20,00,000. The paid-up share capital of VR Ltd. was ₹ 20,00,000 divided into 2,00,000 equity shares of ₹ 10 each.
Find out goodwill/capital reserve to Variety Ltd. on acquiring wholly the shares of VR Ltd.

Solution:

1. Computation of Purchase Consideration

(a) Yield of VR Ltd. [(40 / 100) × (30 + 40 + 65) / 3]:	₹ 18 lakhs
(b) Price per share of VR Ltd.:	
Capitalized Yield: (18 lakhs / 0.15)	₹ 120 lakhs
No. of shares	2 lakhs
Therefore, price per share	₹ 60
(c) Purchase Consideration for 54% shares in VR Ltd.	
2 lakh shares x 54% x ₹ 60 per shares	₹ 64.80 lakhs
(d) Discharge of Purchase Consideration:	
Tax at source (₹ 64.80 lakhs – ₹ 5.40 lakhs) × 30 / 100	₹ 17.82 lakhs
50% of purchase consideration (net of tax) in cash [₹ (64.80 – 17.82) x 50%]	₹ 23.49 lakhs
Balance – Unsecured Loan	₹ 23.49 lakhs

2. Goodwill / Capital Reserve to Variety Ltd.

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

10. A Ltd. acquired 40% share in B Ltd. on April 01, 20X1 for ₹ 10 lacs. On that date B Ltd. had 1,00,000 equity shares of ₹ 10 each fully paid and accumulated profits of ₹ 2,00,000. During the year 20X1-20X2, B Ltd. suffered a loss of ₹ 10,00,000; during 20X2-20X3 loss of ₹ 12,50,000 and during 20X3-20X4 again a loss of ₹ 5,00,000. Show the extract of consolidated balance sheet of A Ltd. on all the four dates recording the above events.

Solution: Calculation of Goodwill/Capital Reserve under Equity Method

Particulars	**₹**
Equity Shares	10,00,000
Reserves & Surplus	2,00,000
Net Assets	12,00,000
40% share of Net Assets	4,80,000
Less: Cost of Investment	(10,00,000)
Goodwill	5,20,000

Consolidated Balance Sheet (Extract) as on April 01, 20X1:

ASSETS

Investment in Associate as per AS 23	₹	₹
Share of Net Assets on April 1	4,80,000	
Add: Goodwill	5,20,000	10,00,000

Calculation of Carrying Amount of Investment as at 31 March 20X2:

Investment in Associate as per AS 23	₹
Share of Net Assets on 1 April, 20X1	4,80,000
Add: Goodwill	5,20,000
Cost of Investment	10,00,000
Less: Loss for the year (10,00,000 x 40%)	(4,00,000)
Carrying Amount of Investment	6,00,000

Consolidated Balance Sheet (Extract) as on March 31, 20X2:
ASSETS

Investment in Associate as per AS 23	₹	₹
Share of Net Assets on 1 April, 20X1		4,80,000
Less: Share of Loss as above		(4,00,000)
		80,000
Add: Goodwill		5,20,000
		6,00,000

Calculation of Carrying Amount of Investment as at 31 March 20X3:

Investment in Associate as per AS 23	₹
Carrying Amount of Investment as on 31 March 20X2	6,00,000
Less: Loss for the year (12,50,000 x 40%)	(5,00,000)
Carrying Amount of Investment	1,00,000

Consolidated Balance Sheet (Extract) as on March 31, 20X3:
ASSETS

Investment in Associate as per AS 23	₹	₹
Share of Net Assets on 1 April, 20X1	4,80,000	
Less: Share of Loss as above (₹ 4,00,000 + ₹ 5,00,000)	(9,00,000)	
	(4,20,000)	
Add: Goodwill	5,20,000	1,00,000

Calculation of Carrying Amount of Investment as at 31 March 20X4:

Investment in Associate as per AS 23	**₹**
Carrying Amount of Investment	1,00,000
Less: Loss for the year (5,00,000 x 40% = 2,00,000, restricted to Carrying amount of Investment in B Ltd.) - refer note below	(1,00,000)
Carrying Amount of Investment	-

Consolidated Balance Sheet (Extract) as on March 31, 20X4:
ASSETS

Investment in Associate as per AS 23		**₹**
Investment in Associate as per AS 23	₹	₹
Share of Net Assets on 1 April, 20X1	4,80,000	
Less: Share of Loss as above (₹ 4,00,000 + ₹ 5,00,000 + ₹ 1,00,000)	(10,00,000)	
	(5,20,000)	
Add: Goodwill	5,20,000	Nil

11. Bright Ltd. acquired 30% of East India Ltd. shares for ₹ 2,00,000 on 01-06-20X1. By such an acquisition Bright can exercise significant influence over East India Ltd. During the financial year ending on 31-03-20X1 East India earned profits ₹ 80,000 and declared a dividend of ₹ 50,000 on 12-08-20X1. East India reported earnings of ₹ 3,00,000 for the financial year ending on 31-03-20X2 (assume profits to accrue evenly) and declared dividends of ₹ 60,000 on 12-06-20X2.
Calculate the carrying amount of investment in:
(i) Separate financial statements of Bright Ltd. as on 31-03-20X2;
(ii) Consolidated financial statements of Bright Ltd.; as on 31-03-20X2;
(iii) What will be the carrying amount as on 30-06-20X2 in consolidated financial statements?
Solution:

(i) Carrying amount of investment in Separate Financial Statement of Bright Ltd. as on 31.03.20X2

	₹
Amount paid for investment in Associate (on 1.06.20X1)	2,00,000
Less: Pre-acquisition dividend (₹ 50,000 x 30%)	(15,000)
Carrying amount as on 31.3.20X2 as per AS 13	1,85,000

(ii) Carrying amount of investment in Consolidated Financial Statements* of Bright Ltd. as on 31.3.20X2 as per AS 23

	₹
Carrying amount as per separate financial statements	1,85,000
Add: Proportionate share of 10-month profit of investee as per equity method (30% of ₹ 3,00,000 x 10/12)	75,000
Carrying amount as on 31.3.20X2	2,60,000

(iii) Carrying amount of investment in Consolidated Financial Statement of Bright Ltd. as on 30.6.20X2 as per AS 23

	₹
Carrying amount as on 31.3.20X2	2,60,000
Less: Dividend received (₹ 60,000 x 30%)	(18,000)
Carrying amount as on 30.6.20X2	2,42,000

* It is assumed that Bright Ltd. has a subsidiary company and it is preparing Consolidated Financial Statements.

12. P Ltd. owns 80% of S and 40% of J and 40% of A. J is jointly controlled entity and A is an associate. Balance Sheet of four companies as on 31.03.09 are:

	P Ltd.	S	J	A
Investment in S	800	-	-	-
Investment in J	600	-	-	-
Investment in A	600	-	-	-
Fixed assets	1,000	800	1,400	1,000
Current assets	2,200	3,300	3,250	3,650
Total	5,200	4,100	4,650	4,650
Liabilities:				
Share capital Rs. 1				
Equity share	1,000	400	800	800
Retained earnings	4,000	3,400	3,600	3,600
Creditors	200	300	250	250
Total	5,200	4,100	4,650	4,650

P Ltd. acquired shares in 'S' many years ago when 'S' retained earnings were Rs. 520 lakhs. P Ltd. acquired its shares in 'J' at the beginning of the year when 'J' retained earnings were Rs. 400 lakhs. P Ltd. acquired its shares in 'A' on 01.04.08 when 'A' retained earnings were Rs. 400 lakhs.
The balance of goodwill relating to S had been written off three years ago. The value of goodwill in 'J' remains unchanged.
Prepare the Consolidated Balance Sheet of P Ltd. as on 31.03.09 as per AS 21, 23, and 27.

Solution: Consolidated Balance Sheet of P Ltd. as at 31st March, 2009

Particulars	***Note No.***	***(₹ in Lacs)***
I. Equity and Liabilities		
(1) **Shareholder's Funds**		
(a) Share Capital	1	1,000
(b) Reserves and Surplus	2	8,800
(2) **Minority Interest [W.N.3]**		760
(3) **Current Liabilities**		
Creditors	3	600
Total		11,160
II. Assets		
(1) **Non-current assets**		
Property, Plant and Equipment	4	2,360

	Goodwill (W.N. 1) (0 + 120)		120
	Investment in Associates (W.N. 4)		1,880
	(Including Goodwill Rs. 120 lakhs)		
(2)	**Current assets**	5	6,800
	Total		11,160

Notes to Accounts

(₹ (₹ in lacs)

1. Share Capital

Authorized Issued and Subscribed share capital

Equity shares of ₹1 each, fully paid up		1,000

2. Reserves and surplus

Retained Earnings (W.N. 2)		8,800

3. Trade payables

P Ltd.	200	
S Ltd.	300	
J Ltd. (250 X 40%)	100	600

4. Property, plant and equipment

P Ltd.	1,000	
S Ltd.	800	
J Ltd. (250 X 40%)	560	2,360

5. Current Assets

P Ltd.	2,200	
S Ltd.	3,300	
J Ltd. (3,250 X 40%)	1,300	6,800

Working Notes:

1. **Computation of Goodwill**

S (subsidiary)

		Rs. in lakhs
Cost of investment		800
Less: Paid up value of shares acquired	320	
Share in pre- acquisition profits of S Ltd. (520 × 80%)	416	736
Goodwill		64
Less: Goodwill written off		64
Balance		Nil

J (Jointly Controlled Entity)

		Rs. in lakhs
Cost of Investment		600
Less: Paid up value of shares acquired (40% of 800)	320	
Share in pre-acquisition profits (40% of 400)	160	480
Goodwill		120

Note: Jointly controlled entity ‘J’ to be consolidated on proportionate basis i.e. 40% as per AS 27

Associate A (AS 23)

		Rs. in lakhs
Cost of investment		600
Less: Paid up value of shares acquired (800 x 40%)	320	
Share in pre-acquisition profits (400 x 40%)	160	480
Goodwill		120

2. Consolidated Retained Earnings	**Rs. in lakhs**
P Ltd.	4,000
Share in post acquisition profits of S - 80% X (3,400 – 520)	2,304
Share in post acquisition profits of J - 40% X (3,600 – 400)	1,280
Share in post acquisition profits of A - 40% X (3,600 – 400)	1,280
Less: Goodwill written off of ‘S’	(64)
	8,800

3. Minority Interest ‘S’	**Rs. in lakhs**
Share Capital (20% of 400)	80
Share in Retained Earnings (20% of 3,400)	680
	760

4. Investment in Associates	**Rs. in lakhs**
Cost of Investments (including goodwill Rs. 120 lakhs)	600
Share of post acquisition profits	1,280
Carrying amount of Investment (including goodwill Rs. 120 lakhs)	1,880

CASH FLOW STATEMENT

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

Balance Sheets

	Particulars	Note	31.03.2019 (Rs.)	31.03.2018 (Rs.)
I	EQUITY AND LIABILITES			
	(1) Shareholder's Funds			
	(a) Share Capital	1	3,50,000	3,00,000
	(b) Reserves and Surplus	2	82,000	38,000
	(2) Non-Current Liabilities			
	(3) Current Liabilities			
	(a) Trade Payables		65,000	44,000
	(b) Other Current Liabilities	3	37,000	27,000
	(c) Short term Provisions (provision for tax)		32,000	28,000
	Total		5,66,000	4,37,000
II	ASSETS			
	(1) Non-current Assets			
	(a) Tangible Assets	4	2,66,000	1,90,000
	(b) Intangible Assets (Goodwill)		47,000	60,000
	Non-Current Investments		35,000	10,000
	(2) Current Assets			
	(a) Inventories		78,000	85,000
	(b) Trade Receivables		1,08,000	75,000
	(c) 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	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	-
Total	82,000	38,000

Note 3: Current Liabilities

Particulars	31.03.2019 (Rs.)	31.03.2018 (Rs.)
Dividend declared	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
Total	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 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	₹	₹
1		**Cash Flow from Operating Activities**		
	A.	Closing balance as per Profit and Loss Account		27,000
		Less: Opening balance as per Profit & Loss Account *Add:* Dividend declared during the year		(18,000) 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. F.	Operating profit before working capital changes [B + C - D] *Add:* Decrease in Current Assets and Increase in Current Liabilities		1,30,500
		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		50,000
		Interim Dividend paid		(10,000)
		Final dividend 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

1. Land and Building Account

Particulars	₹	*Particulars*	₹
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	₹	*Particulars*	₹
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	₹	*Particulars*	₹
To Balance b/d	10,000	By Bank A/c (Div. received)	600
To bank A/c (Purchase	25,600	By Balance c/d	35,000
	35,600		35,600

2. The Balance Sheet of Max Ltd. for the year ending 31st March, 2022 and 31st March, 2021 were summarised as:

Particulars	Note No	2022 (₹)	2021 (₹)
Equity and Liabilities			
Shareholders' funds			
Equity share capital		1,20,000	1,00,000
Reserves	1	9,000	8,000
Current Liabilities			
(i) Trade Payables		8,000	5,000
(ii) Short term provision	2	7,000	4,000
		1,44,000	1,17,000
Non-current assets			
(i) PPE (at W.D.V)	3	78,000	58,000
(ii) Long Term Investments		32,000	28,000

Current Assets		
(i) Inventory	14,000	8,000
(ii) Trade Receivables	8,000	6,000
(iii) Cash & Bank	12,000	17,000
	1,44,000	1,17,000

Notes to accounts

		2022	2021
1	**Reserves and Surplus**		
	Profit & Loss A/c	9,000	8,000
2	**Short term provision**		
	Provision for Income tax	7,000	4,000
3	**PPE**		
	Building	19,000	20,000
	Furniture & Fixture	34,000	22,000
	Cars	25,000	16,000
		78,000	58,000

The Profit and Loss statement for the year ended 31st March, 2022 disclosed:

	₹
Profit before tax	8,000
Income Tax	(7,000)
Profit after tax	1,000

Further Information is available:

(1) Depreciation on Building for the year ₹ 1,000

(2) Depreciation on Furniture & Fixtures for the year ₹ 2,000

(3) Depreciation on Cars for the year ₹ 5,000. One car was disposed during the year for ₹ 3,400 whose written down value was ₹ 2,000.

(4) Purchase investments for ₹ 6,000.

(5) Sold investments for ₹ 10,000, these investments cost ₹ 2,000.

Prepare Cash Flow Statements for the year ended 31st March, 2022 as per AS-3 (revised) using indirect method.

Solution: **Max Ltd.**

Cash Flow Statement for the year ended 31st March, 2022	**(₹)**	**(₹)**
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	(4,000)	
Net cash generated from operating activities (A)		**(2,400)**
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	
Net cash from financing activities(C)		**20,000**
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**

Working Notes:

1. Calculation of Income taxes paid

	₹
Income tax expense for the year	7,000
Add: Income tax liability at the beginning of the year	4,000
	11,000
Less: Income tax liability at the end of the year	(7,000)
	4,000

2. Calculation of Fixed assets acquisitions

	Furniture & Fixtures (₹)	Car (₹)
W.D.V. at 31.3.2022	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 31.3.2021	(22,000)	(16,000)
Acquisitions during 2021-2022	14,000	16,000

3. J Ltd. presents you the following information for the year ended 31st March, 2007:

		(Rs. in Lacs)
(i)	Net Profit before tax provision	36,000
(ii)	Dividend paid	10,202
(iii)	Income-tax paid	5,100
(iv)	Book value of Assets sold	222
	Loss on sale of Asset	48
(v)	Depreciation debited in P & L account	24,000
(vi)	Capital grant received – amortised in P & L A/c	10
(vii)	Book value of investment sold	33,318
	Profit on sale of investment	120
(viii)	Interest income from investment credited in P & L A/c	3,000
(ix)	Interest expenditure debited in P & L A/c	12,000
(x)	Interest actually paid (Financing activity)	13,042
(xi)	Increase in working Capital [Excluding cash and Bank Balance]	67,290
(xii)	Purchase of fixed assets	22,092
(xiii)	Expenditure on construction work	41,688
(xiv)	Grant received for Capital projects	18
(xv)	Long-term borrowings from Banks	55,866
(xvi)	Provision for Income-tax debited in P & L A/c	6,000
	Cash and Bank Balance on 1.4.2006	6,000
	Cash and Bank Balance on 31.3.2007	8,000

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:		36,000
Net profit before tax provision		
Add: Non cash expenditures:		
Depreciation	24,000	
Loss on sale of assets	48	
Interest expenditure (non operating activity)	12,000	36,048
Less: Non cash income		72,048
Amortisation of capital grant received	(10)	
Profit on sale of investments (non operating income)	(120)	
Interest income from investments (non operating income)	(3,000)	3,130
Operating profit		68,918
Less: Increase in working capital		(67,290)
Cash from operations		1,628
Less: Income tax paid		(5,100)
Net cash generated from operating activities		(3,472)
Cash flows from investing activities:		
Grants for capital projects	18	
Sale of assets (222 – 48)	174	
Sale of investments (33,318+120)	33,438	
Interest income from investments	3,000	
Purchase of fixed assets	(22,092)	
Expenditure on construction work	(41,688)	
Net cash used in investing activities		(27,150)
Cash flows from financing activities:		
Long term borrowings	55,866	
Interest paid	(13,042)	
Dividend paid	(10,202)	
Net cash from financing activities		32,622
Net increase in cash		2,000
Add: Cash and bank balance as on 1.4.2018		6,000
Cash and bank balance as on 31.3.2019		8,000

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

(1) Gross Profit Ratio was 25% for the year, it 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.
(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 & 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 31/03/2019 Rs. 2,00,000, 7%Debentures 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: (A) Cash Flow Statement of M/s PQR Ltd. for the year ended 31st March 2019 (Direct Method)

Particulars	Rs.	Rs.
A. CASH FLOW FROM OPERATING ACTIVITIES:		
Cash Receipt from Sale of Goods (Rs. 3,75,000/25%)	15,00,000	
Cash Payments to Trade Payable	(6,10,000)	
Cash Payments of Wages	(5,55,000)	
Cash Payments for Expense/ services (Administration and selling Expenses) (35,000 + 15,000)	(50,000)	
Cash Generated from Operations before Taxes & Extra Ordinary Items	2,85,000	
Less: Taxes Paid	(55,000)	
Net Cash Flow from / (used in) Operating Activities [A]		2,30,000
B. CASH FLOW FROM INVESTING ACTIVITIES:		
Sale Proceeds of Investments (Book Value 8,20,000 + Profit 20,000)	8,40,000	
Purchase of New Plant & Machinery	(3,50,000)	
Net Cash Flow from / (used in) Investing Activities [B]		4,90,000
C. CASH FLOW FROM FINANCING ACTIVITIES:		
Repayment of Bank Loan Principal (2,05,000 – 5,000)	(2,00,000)	
Interest on Bank Loan	(5,000)	
Dividends paid (inclusive of Dividend Distribution Tax)	(40,000)	
Net Cash Flow from/ (used in) Financing Activities [C]		(2,45,000)
D. Net Increase or Decrease in Cash or Cash Equivalents [A+B+C]		4,75,000
E. Opening Balance of Cash & Cash Equivalents (given)		2,25,000
F. Closing Balance of Cash & Cash Equivalents (B/F)		7,00,000

(B) Cash Flow from Operating Activity of M/s PQR Ltd. for the year ended 31st March 2019 (Indirect Method)

Particulars	Amount(Rs.)
Net Profit after Tax(B/F)	2,50,000
(+) Provision for Tax	30,000
Net Profit before Tax	2,80,000
Add: Interest Expenses	5,000
Depreciation(40,000 + 20,000)	60,000
Less: Profit on sale of Inventory	(20,000)
Increase in Inventory	(25,000)
Decrease in Trade Payable	(15,000)
Tax Paid	(55,000)
Net Cash Flow from Operating Activities [A]	2,30,000

Working Note 1: Trade Payable Account

Particulars	Amount	Particulars	Amount
To bank A/c	6,10,000	By balance b/d	50,000
To balance c/d	35,000	By Purchases (B/F)	5,95,000
	6,45,000		6,45,000

5. Prepare cash flow from investing activities as per AS 3 of M/s Subham Creative Ltd. for year ended 31.3.2019.

Particulars	Amount (Rs.)
Machinery acquired by issue of shares at face value	2,00,000
Claim received for loss of machinery in earthquake	55,000
Unsecured loans given to associates	5,00,000
Interest on loan received from associate company	70,000
Pre-acquisition dividend received on investment made	52,600
Debenture interest paid	1,45,200
Term loan repaid	4,50,000
Interest received on investment (TDS of Rs. 8,200 was deducted on the above interest)	73,800
Purchased debentures of X Ltd., on. 1st December, 2018 which are redeemable within 3 months	3,00,000
Book value of plant & machinery sold (loss incurred Rs. 9,600)	90,000

Solution: Cash Flow Statement from Investing Activities of Subham Creative Ltd. for the year ended 31/03/19

Cash generated from investing activities	*Rs.*	*Rs.*
Interest on loan received	70,000	
Pre-acquisition dividend received on investment made Unsecured	52,600	
loans given to subsidiaries	(5,00,000)	
Interest received on investments (gross value) Less TDS	73,800	
deducted on interest (82,000 – 8,200)		
Sale of Plant & Machinery Rs.(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)

Notes:

(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.

6. Explain the meaning of the terms 'cash' and 'cash equivalent' for the purpose of Cash Flow Statement as per AS-3 Ruby Exports had a bank balance of USD 25,000, stated in books at Rs 16,76,250 using the rate of exchange Rs 67.05 per USD prevailing on the date of receipt of dollars. However, on the balance sheet date, the closing rate of exchange was Rs 67.80 and the bank balance had to be restated at Rs 16,95,000. Comment on the effect of change in bank balance due to exchange rate fluctuation and also discuss how it will be disclosed in Cash Flow Statement of Ruby Exports with reference to AS-3.

Solution:

Meaning of Cash:- Cash in hand and deposits repayable on demand with any bank or other financial institutions.

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

Effect of change in bank balance due to exchange rate fluctuation: Cash flows arising from transactions in foreign currency should be recorded in an enterprise's reporting currency by applying to the foreign currency amount the exchange rate between the reporting currency and the foreign currency at the date of the cash flow. A rate that approximates the actual rate may be used if the result is substantially the same as would arise if the rates at the dates of the cash flows were used. The effect of charges in exchange rates on cash and cash equivalents held in a foreign currency should be reported as a separate part of the reconciliation of the changes in cash and cash equivalents during the period.

In the given question Foreign Exchange differences shall be treated as follows:

(i) **Under direct Method:** Rs. 67.80 X $ 25,000=Rs. 16,95,000 – Rs. 16,76,250 = Rs. 18,750 is to deducted from closing bank balance of the purpose of reconciliation.

(ii) **Under indirect Method:** Once Rs. 67.80 X $ 25,000=Rs. 16,95,000 – Rs. 16,76,250 = Rs. 18,750 is to deducted from closing bank balance of the purpose of reconciliation and also deducted from operating Activity as foreign exchange gain.

7. Classify the following activities as (a) Operating activities, (b) Investing activities (c) Financing activities (d) Cash equivalents with reference to AS 3 (Revised).

(a) Brokerage paid on purchase of investments
(b) Underwriting commission paid
(c) Trading commission received
(d) Proceeds from sale of investment
(e) Purchase of goodwill
(f) Redemption of preference shares
(g) Rent received from property held as investment
(h) Interest paid on long-term borrowings
(i) Marketable securities (having risk of change in value)
(j) Refund of income tax received

Solution: Classification of activities with reference to AS 3

a.	Brokerage paid on purchased of investments	Investing Activities
b.	Underwriting Commission paid	Financing Activities
c.	Trading Commission received	Operating Activities
d.	Proceeds from sale of investment	Investing Activities
e.	Purchase of goodwill	Investing Activities
f.	Redemption of Preference shares	Financing Activities
g.	Rent received from property held as investment	Investing Activities
h.	Interest paid on long term borrowings	Financing Activities
i.	Marketable securities	Not a Cash equivalent
j.	Refund of Income tax received	Operating activities

8. From the following Balance Sheets of Mr. Zen, prepare a Cash flow statement as per AS-3 for the year ended 31.3,2010:

Liabilities	**As on 1.4.2009**	**As on 1.4.2010**
Zen's Capital A/c	10,00,000	12,24,000
Sundry creditors	3,20,000	3,52,000
Mrs. Zen's loan	2,00,000	--
Loan from Bank	3,20,000	4,00,000
	18,40,000	19,76,000
Assets	**As on 1.4.2009**	**As on 1.4.2010**
Land	6,00,000	8,80,000
Plant and Machinery	6,40,000	4,40,000

Stock	2,80,000	2,00,000
Debtors	2,40,000	4,00,000
Cash	80,000	56,000
	18,40,000	19,76,000

Additional information: A machine costing Rs. 80,000 (accumulated depreciation there on Rs. 24,000) was old for Rs. 40,000. The provision for depreciation on 1.4.2009 was Rs. 2,00,000 and 31.3.2010 was Rs. 3,20,000. The net profit for the year ended on 31.3.2010 was Rs. 3,60,000.

Solution: Cash Flow Statement of Mr. Zen as per AS 3 for the year ended 31.3.2010

		Rs.
(i) Cash flow from operating activities		
Net Profit (given)		3,60,000
Adjustments for		
Depreciation on Plant & Machinery	1,44,000	
Loss on Sale of Machinery	16,000	1,60,000
Operating Profit before working capital changes		5,20,000
Decrease in Stock	80,000	
Increase in Debtors	(1,60,000)	
Increase in Creditors	32,000	(48,000)
Net cash generated from operating activities		4,72,000
(ii) Cash *flow from* investing activities		
Sale of Machinery	40,000	
Purchase of Land	(2,80,000)	
Net cash used in investing activities		(2,40,000)
(iii) Cash *flow from* financing activities		
Repayment of Mrs. Zen's Loan	2,00,000	
Drawings	(1,36,000)	
Loan from Bank	80,000	
Net cash used in financing activities		(2,56,000)
Net decrease in cash		(24,000)
Opening balance as on 1.4.2009		80,000
Cash balance as on 31.3.2010		56,000

Working Notes:

1. Plant & Machinery A/c

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

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

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

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

	Rs.
Opening Capital	10,00,000
Add: Net Profit	3,60,000
	13,60,000
Less: Closing Capital	(12,24,400)
Drawing	1,36,000

9.

Liabilities	31.3.2011	31.3.2012	Assets	31.3.2011	31.3.2012
Share Capital	5,00,000	5,00,000	Discount on		
15% Debentures	5,00,000	7,50,000	issue of shares	1,15,000	90,000
Unpaid Interest	--	5,000	Discount on issue		
Profit & Loss A/c	50,000	90,000	of Debentures	90,000	1,15,000

You are required to show the related items in Cash Flow Statement, if Discount on issue of Debentures amounting to Rs. 10,000 has been written off during the year. Goodwill was written off during the year by Rs. 25,000.

Solution: An Extract of Cash Flow Statement for the year ending 31.3.20X2

Particulars	**Rs.**
Closing balance as per Profit & Loss A/c	90,000
Less: Opening balance as per Profit & Loss Alc.	(50,000)
Profit for the year	40,000
Add: Goodwill amortisation	25,000
Add: Discount on issue of Debentures	10,000
Interest on Debentures	75,000
Net Cash from Operating Activities	1,50,000

Cash flows from financing activities:

Proceeds from debentures	2,15,000
Interest paid on Debentures [less unpaid]	(70,000)
Net Cash from Financing Activities	1,45,000

Working Note:

(a) Discount on issue of Debentures Account

Particulars	**Rs.**	**Particular**	**Rs.**
To Balance b/d	90,000	By Profit & Loss A/c (w/o)	10,000
To 15% Debentures A/c (Bal. fig.)	35,000	By Balance c/d	1,15,000
	1,25,000		1,25,000

(b) 15% Debentures Account

Particulars	**Rs.**	**Particular**	**Rs.**
To Balance c/d	7,50,000	By Balance b/d	5,00,000
		By Bank A/c (Bal. fig.)	2,15,000
		By Discount on issue of Debentures A/c	35,000
	7,50,000		7,50,000

10. ABC Ltd. gives you the Balance sheets as at 31st March 20X0 and 31st March 20X1. You are required to prepare Cash Flow Statement by using indirect method as per AS 3 for the year ended 31st March 20X1:

Particulars			Notes	31st March 20X0 (₹)	31st March 20X1 (₹)
		Equity and Liabilities			
1		Shareholders' funds			
	A	Share capital Reserves and		50,00,000	50,00,000
	B	Surplus		26,50,000	36,90,000
2		Non-current liabilities			
		Long term borrowings	1	-	9,00,000
3		Current liabilities Short-term			
	A	borrowings (Bank loan)		1,50,000	3,00,000
		Trade payables		8,80,000	8,20,000
	B	Other current liabilities	2	4,80,000	2,70,000
	C	Total		91,60,000	1,09,80,000
		Assets			
1		Non-current assets			
	A	Property, plant and Equipment	3	21,20,000	32,80,000
2		Current assets			
	A	Current Investments		11,80,000	15,00,000
	B	Inventory		20,10,000	19,20,000
	C	Trade receivables	4	22,40,000	26,40,000
	D	Cash and Cash equivalents		15,20,000	15,20,000
	E	Other Current assets (Prepaid expenses)		90,000	1,20,000
		Total		91,60,000	1,09,80,000

Notes to accounts

No.	Particulars		₹20X0	20X1
1	Long term borrowings			
	9% Debentures (issued at the end of year)		-	9,00,000
	Total		-	9,00,000
2.	Other current liabilities			
	Dividend payable		1,50,000	-
	Liabilities for expenses		3,30,000	2,70,000
	Total		4,80,000	2,70,000
3	Property, plant and equipment			
	Plant and machinery		27,30,000	40,70,000
	Less: Depreciation		(6,10,000)	(7,90,000)
	Net carrying value		21,20,000	32,80,000
4	Trade receivables			
	Gross amount		23,90,000	28,30,000
	Less: Provision for doubtful debts		(1,50,000)	(1,90,000)
	Total		22,40,000	26,40,000

Additional Information:

(i) Net profit for the year ended 31st March, 20X1, after charging depreciation ₹ 1,80,000 is ₹ 10,40,000.

(ii) Trade receivables of ₹ 2,30,000 were determined to be worthless and were written off against the provisions for doubtful debts account during the year.

Solution: Cash Flow Statement of ABC Ltd. for the year ended 31.3.20X1

Cash flows from Operating Activities		₹	₹
Net Profit		10,40,000	
Add: Adjustment For Depreciation (₹7,90,000 – ₹6,10,000)		1,80,000	
Add: Adjustment for Provision for Doubtful Debts (₹ 4,20,000 – ₹1,50,000)		2,70,000	
Operating Profit Before Working Capital Changes		14,90,000	
Add: Decrease in Inventories (₹ 20,10,000 – ₹ 19,20,000)		90,000	
		15,80,000	
Less: Increase in Current Assets			
Trade Receivables (₹ 30,60,000 – ₹23,90,000)	6,70,000		
Prepaid Expenses (₹ 1,20,000 – ₹90,000)	30,000		
Decrease in Current Liabilities:			
Trade Payables (₹ 8,80,000 – ₹ 8,20,000)	60,000		
Expenses Outstanding (₹ 3,30,000 – ₹ 2,70,000)	60,000	(8,20,000)	
Net Cash generated from Operating Activities			**7,60,000**
Cash Flows from Investing Activities			
Investment in Current Investments		(3,20,000)	
Purchase of Plant & Machinery (₹ 40,70,000 – ₹ 27,30,000)		(13,40,000)	
Net Cash Used in Investing Activities			**(16,60,000)**
Cash Flows from Financing Activities			
Bank Loan Raised (₹ 3,00,000 – ₹ 1,50,000)		1,50,000	
Issue of Debentures		9,00,000	
Payment of Dividend		(1,50,000)	
Net Cash Used in Financing Activities			9,00,000
Net Increase in Cash During the Year			-
Add: Cash and Cash Equivalents as on 1.4.20X0			15,20,000
Cash and Cash Equivalents as on 31.3.20X1			15,20,000

Note:

(1) Bad debts amounting ₹ 2,30,000 were written off against provision for doubtful debts account during the year. In the above solution, Bad debts have been added back in the balances of provision for doubtful debts and trade receivables as on 31.3.20X1. Alternatively, the adjustment of writing off bad debts may be ignored and the solution can be given on the basis of figures of trade receivables and provision for doubtful debts as appearing in the balance sheet on 31.3.20X1.

(2) Current investments (i.e. Marketable securities) may not be readily convertible to a known amount of cash and be subject to an insignificant risk of changes in value as per the requirements of AS 3 and hence those have been considered as investing activities.

11. From the following information, prepare a CFS as per AS-3 for Banjara Ltd., using direct method:

Balance Sheet as on 31st March 2010 (Rs. '000)

		2010		2009
Assets:-				
Cash on hand and balances with bank		200		25
Marketable Securities (Having one month maturity)		670		135
Sundry Debtors		1,700		1,200
Interest Receivable		100		-
Inventories		900		1,950
Investments		2,500		2,500
Fixed Assets at Cost	2,180		1,910	
Accumulated Depreciation	(1,450)		(1,060)	
Fixed Assets(Net)		730		850
Total Assets		6,800		6,660

Liabilities:-			
Sundry Creditors	150		1,890
Interest Payable	230		100
Income tax Payable	400		1000
Long Term Debt	1,110		1,040
Total Liability	1,890		4,030
Shareholder's Fund:			
Share Capital	1,500		1,250
Reserves	3,410		1,380
	4,910		2,630
Total Liabilities & Shareholders' Fund	**6,800**		**6,660**

Statement of Profit or Loss for the year ended 31st March 2010

Particulars	Amount in Rs. '000
Sales	**30,650**
Cost of Sales	**(26,000)**
Gross Profit	4,650
Depreciation	(450)
Administrative and selling expenses	(910)
Interest Expenses	(400)
Interest Income	300
Dividend Income	200
Net Profit before taxation and Extraordinary items	3,390
Extraordinary items:	
Insurance Proceeds from earthquake disaster settlement	140
Net Profit after extraordinary items	3,530
Income Tax	(300)
	3,230

Additional Information:-

(i) An amount of Rs. 250 was raised from the issue of share capital and a further Rs. 250 was raised from long-term borrowings.

(ii) Interest expenses was Rs. 400 of which Rs. 170 was paid during the period Rs. 100 relating to interest expenses of the prior period was also paid during the year.

(iii) Dividend paid were Rs. 1,200.

(iv) Tax Deducted at Source on Dividends received (Including in the tax expenses of Rs. 300 for the year) amounted to Rs. 40.

(v) During the period the enterprise acquired fixed assets for Rs. 350. The payment was made in cash.

(vi) Plant with original cost Rs. 80 and Accumulated depreciation of Rs. 60 was sold for Rs. 20.

(vii) Sundry debtors and sundry creditors include amounts relating to credit sales and credit purchase only.

Solution: Cash Flow Statement (direct method)

Cash flows from Operating Activities		
Cash receipts from customers (W.N.2)	30,150	
Cash paid to suppliers, employees and for expenses (W.N.3)	(27,600)	
Cash generated from operations	2,550	
Income tax paid (W.N.4)	(860)	
	1,690	
Cash flow before extraordinary item:		
proceeds from earthquake disaster settlement	140	
Net cash from operating activities		1,830

Cash flows from Investing Activities		
Purchase of fixed assets	(350)	
Proceeds from sale of equipment	20	
Interest received (300 – 100)	200	
Dividends received (200 – 40)	160	
Net cash from investing activities		30
Cash flows from Financing Activities		
Proceeds from issuance of share capital	250	
Proceeds from long term borrowings	250	
Repayment of long term borrowings (W.N.5)	(180)	
Interest paid (W.N.6)	(270)	
Dividends paid	(1,200)	
Net cash used in financial activities		(1,150)
Net increase in cash and cash equivalents		710
Cash and cash equivalents at beginning of the period (W.N.1)		160
Cash and cash equivalents at end of the period (W.N.1)		870

Working Notes:

(1) Cash and cash equivalents

Cash and cash equivalents consist of cash in hand and balances with banks and investments in money market instruments for short period.

		₹'000
	2010	2009
Cash in hand and balance with bank	200	25
Short-term investments	670	135
Cash and cash equivalents	870	160

(2) Cash receipts from customers

	₹'000
Total sales	30,650
Add: Sundry debtors at the beginning of the year	1,200
	31,850
Less: Sundry debtors at the end of the year	(1,700)
Cash sales	30,150

(3) Cash paid to suppliers, employees and for expenses

		₹'000
Cost of sales		26,000
Administrative and selling expenses		910
		26,910
Add: Sundry creditors at the beginning of the year	1,890	
Inventories at the end of year	900	2,790
		29,700
Less: Sundry creditors at the end of year	(150)	
Inventories at the beginning of the year	(1,950)	(2,100)
		27,600

(4) Income tax paid (including TDS from dividends received)

	₹'000
Income tax expense for the year (including tax deducted at source from dividends received)	300
Add: Income tax liability at the beginning of the year	1,000
	1,300
Less: Income tax liability at the end of the year	(400)
	900

Out of ₹ 900 thousands, tax deducted at source on dividends received (amounting to ₹40 thousands) is included in cash flows from investing activities and the balance of ₹860 thousands is included in cash flows from operating activities.

(5) Repayment of long term borrowings during the year

	₹'000
Long term debts at the beginning of the year	1,040
Add: Long term borrowings made during the year	250
	1,290
Less: Long term borrowings at the end of the year	(1,110)
	180

(6) Interest paid during the year

	₹'000
Interest expense for the year	400
Add: Interest payable at the beginning of the year	100
	500
Less: Interest payable at the end of the year	(230)
	270

INVESTMENT ACCOUNTS

1. On 1st April, 2009 XY Ltd. has 15,000 equity shares of ABC Ltd. at a book value of Rs. 15 per share (face value Rs. 10 per share). On 1st June, 2009, XY Ltd. acquired 5,000 equity shares of ABC Ltd. Rs. 1,00,000 on cum right basis. ABC Ltd. announced a bonus and right issue.

(1) Bonus was declared, at the rate of one equity share for every five shares held, on 1st July 2009.

(2) Right shares are to be issued to the existing shareholders on 01st September 2009. The company will issue one right share for every 6 shares at 20% premium. No dividend was payable on these shares.

(3) Dividend for the year ended 31.03.09 were declared by ABC Ltd. @ 20%, which was received by XY Ltd. on 31st October 2009. XY Ltd.

(i) Took up half the right issue.

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

(iii) Sold half of its share holdings on 01st January 2010 at Rs. 16.50 per share. Brokerage being 1%.

You are required to prepare Investment Account of XY Ltd. for the year ended 31st March 2010 assuming the shares are being valued at average cost.

Solution:

In the books of XY Ltd.
Investment in Equity Shares of ABC Ltd.
For the year ended 31st March 20X2

Date	Particulars	No.	Income Rs.	Amount Rs.	Date	Particulars	No.	Income Rs.	Amt Rs.
20X1 April 1	To Balance b/d	15,000	-	2,25,000	20X1 Oct. 31	By Bank A/c (W.N. 5)	-	30,000	10,000
June 1	To Bank A/c	5,000	--	1,00,000	20X2 Jan. 1	By Bank A/c (W.N.4)	13,000	-	2,12,355
July 1	To Bonus Issue (W.N. 1)	4,000	-	-	March 31	By Balance c/d (W.N. 6)	13,000	-	1,69,500
Sept.1	To Bank A/c (W.N. 2)	2,000	-	24,000					
20X2 Jan 1	To P & L A/c (W.N. 4)	-	-	42,855					
"20X2 March 31	To P & L A/c	-	30,000	-					
		26,000	30,000	3,91,855			26,000	30,000	3,91,855

Working Notes:

1. Calculation of no. of bonus shares issued

Bonus Shares = (15,000 shares + 5,000 shares) x 1/5 = 4,000 shares

2. Calculation of right shares subscribed

Right Shares

$$\frac{15{,}000 \text{ shares} + 5{,}000 \text{ shares} + 4{,}000 \text{ shares}}{6}$$

= 4,000 shares

Shares subscribed by XY Ltd. = 4,000/2 = 2,000 shares

Value of right shares subscribed = 2,000 shares @ Rs. 12 per share = Rs. 24,000

3. **Calculation of sale o f right entitlement**
2,000 shares x Rs. 8 per share = Rs. 16,000
Amount received from sale of rights will be credited to statement of profit and loss.

4. **Calculation of Profit on sale of shares.**
Total holding = 15,000 shares original
5,000 shares purchased
4,000 shares bonus
2,000 shares right shares
26,000 shares

50% of the holdings were sold i.e. 13,000 shares (26,000 x1/2) were sold.

Cost of total holdings of 26,000 shares (on average basis)
= Rs. 2,25,000 + Rs. 1,00,000 + Rs. 24,000– Rs. 10,000 = Rs. 3,39,000

Average cost of 13,000 shares would be
= (3,39,000 / 26,000) X 13,000
= Rs. 1,69,500

	Rs.
Sale proceeds of 13,000 shares (13,000 x Rs.16.50)	2,14,500
Less: 1% Brokerage	(2,145)
	2,12,355
Less: Cost of 13,000 shares	(1,69,500)
Profit on sale	42,855

5. **Dividend received on investment held as on 1st April, 20X1**
= 15,000 shares X Rs. 10 X 20%
= Rs. 30,000 will be transferred to Profit and Loss A/c
Dividend received on shares purchased on 1st June, 20X1

= 5,000 shares X Rs. 10 X 20% = Rs.10,000 will be adjusted to Investment A/c

Note: It is presumed that no dividend is received on bonus share as bonus share are declared on 1st July, X1 and dividend pertains to the year ended 31.03.X1.

6. **Calculation of closing balance of shares (On average basis) as on 31st March X2.**
= 13,000 (3,39,000/26,000)

2. On 1st December 2015, M/s. Blue & Black purchased, 20,000 12% fully paid debentures of Rs.100 each at Rs.105 cum Interest price, also paying brokerage @ 1% of cum interest amount of the purchase. On 1st March, 2016, the firm sold all these debentures at Rs.110 cum-interest price, again paying brokerage @ 1% cum interest amount. Prepare Investment Account in the books of M/s. Blue & Black for the period 1st December, 2015 to 1st March 2016. Interest being payable half yearly on 30th September and 31st March of every accounting year.

Solution:

Books of M/s. Blue & Black for the period 1st Dec., 2015 to 1st March 2016

Investment in 12% Debentures Account

Date	Particulars	Face Value	Interest	Amount	Date	Particulars	Face Value	Interest	Amount
1.12.2015 31.3.2016	To bank To profit & loss (B/F)	20,00,000	40,000 60,000	20,81,000	1.3.2016	By Bank A/c BY P & L A/c (B/F)	20,00,000 -	1,00,000	20,78,000 3,000
		20,00,000	1,00,000	20,81,000			20,00,000	1,00,000	20,81,000

Working Notes:-

1. CALCULATION OF COST OF INVESTMENTS MADE ON 1.12.2015

Purchase price (20,000 X 105)	21, 00,000
Brokerage @ 1% on cum interest price	21,000
	21, 21,000
Less: Interest for 2 months (20000x100x12%x2/12)	(40,000)
Cost of investments	20,81,000

2. CALCULATION OF SALE Value OF INVESTMENTS as on 1.3.2016

Selling price (20,000x110)	22,00,000
Brokerage @1% on cum interest price	(22,000)
	21,78,000
Less: Interest for 5 months(20,000X100X12%X5/12)	(1,00,000)
Net selling price	20,78,000

3. Alpha Ltd. purchased 5,000, 13.5% Debentures of Face Value of ₹ 100 each of Pergot Ltd. on 1st May 2021 @ ₹ 105 on cum interest basis. The interest on these debentures is payable on 31st & 30th of March & September respectively. On August 1st 2021 the company again purchased 2,500 of such debentures @ ₹ 102.50 each on cum interest basis. On October 1st, 2021 the company sold 2,000 Debentures @ ₹ 103 each on ex- interest basis. The market value of the debentures as at the close of the year was ₹ 106. You are required to prepare the Investment in Debentures Account in the books of Alpha Ltd. for the year ended 31st Dec. 2021 on Average Cost Basis.

Solution: **Books of Alpha Ltd.**

Investment in 13.5% Debentures in Pergot Ltd. Account

(Interest payable on 31st March & 30th September)

Date	Particulars	Nominal	Interest	Amount	Date	Particulars	Nominal	Interest	Amount
2021		₹	₹	₹	2021		₹	₹	₹
May 1	To Bank	5,00,000	5,625	5,19,375	Sept.30	By Bank (6 months Int)		50,625	
Aug.1	To Bank	2,50,000	11,250	2,45,000	Oct.1	By Bank	2,00,000		2,06,000
Oct.1	To P&L A/c			2,167					
Dec.31	To P&L A/c		52,313						
					Dec.31	By Balance c/d	5,50,000	18,563	5,60,542
		7,50,000	69,188	7,66,542			7,50,000	69,188	7,66,542

Note: Cost being lower than Market Value the debentures are carried forward at Cost.

Working Notes:

1. Interest paid on ₹ 5,00,000 purchased on May 1st, 2021 for the month of April 2021, as part of purchase price: 5,00,000 x 13.5% x 1/12 = ₹ 5,625

2. Interest received on 30th Sept. 2021
   On ₹ 5,00,000 = 5,00,000 x 13.5% x ½ = 33,750
   On ₹ 2,50,000 = 2,50,000 x 13.5% x ½ = 16,875
   Total ₹ 50,625

3. Interest paid on ₹ 2,50,000 purchased on Aug. 1st 2021 for April 2021 to July 2021 as part of purchase price: 2,50,000 x 13.5% x 4/12 = ₹ 11,250

4. Loss on Sale of Debentures
   Cost of acquisition
   (₹ 5,19,375 + ₹ 2,45,000) x ₹ 2,00,000/₹ 7,50,000 = 2,03,833
   Less: Sale Price (2,000 x 103) = 2,06,000
   Profit on sale = ₹ 2,167

5. Cost of Balance Debentures = (₹ 5,19,375 + ₹ 2,45,000) x ₹ 5,50,000/₹ 7,50,000 = ₹ 5,60,542

6. Interest on Closing Debentures for period Oct.-Dec. 2021 carried forward (accrued interest)
₹ 5,50,000 x 13.5% x 3/12 = ₹ 18,563

4. On 15th June 2018, Y Ltd. wants to re-classify its investment in accordance with AS 13(Revised). Decide and state the amount of transfer, based on the following information:

(1) A portion of long term investments purchased on 1st March, 2017 are to be reclassified as current investments. The original cost of these investments was Rs. 14 but had been written down by Rs. 2 lakhs(to recognize 'other than temporary' decline in value). The market value of these investments on 15th June, 2018 was Rs. 11laks.

(2) Another portion of long term investments purchased on 15th January, 2017 are to be reclassified as current investments. The original cost of these investments was Rs. 7lakhs but had been written down to Rs. 5 lakhs (to recognize 'other than temporary' decline in value). The market value of these investments on 15th June, 2018 was Rs. 4.50laks.

(3) A portion of Current Investments purchased on 15th March, 2018 for Rs. 7 lakhs are to be re-classified as long term investments, as the company has decided to retain them. The market value of these investments on 31st March 2018 was Rs. 6lakhs and Fair Value as on 15th June 2018 was Rs. 8.50lakhs.

(4) Another portion of Current investments purchased on 7th December 2017 for Rs. 4 lakhs has to be re-classified as long term investments. The market value of these investments was:

On 31st March 2018	Rs. 3.5 lakhs
On 15th June 2018	Rs. 3.8 lakhs.

Solution:

(i) Provision of Accounting Standard(AS)-13

(a) As per para 23 of AS 13 'Accounting for Investments', where long term investments are reclassified as current investments, transfers are made at the lower of cost and carrying amount at date of transfer.

(b) As per Para 24 of AS13 'Accounting for Investments', where investments are reclassified from current to long term, transfers are made at the lower of cost and fair value a date to transfer.

(ii) In the given question treatment will be as follows:-

(1) The book value for the investment is Rs. 12lakhs, which is lower than its cost i.e., Rs.14 lakhs. Here, the transfer should be at carrying amount and hence these reclassified current investments should be carried at Rs. 12lakhs.

(2) The book value for the investment is Rs. 5lakhs, which is lower than its cost i.e., Rs.7 lakhs. Here, the transfer should be at carrying amount and hence these reclassified current investments should be carried at Rs. 5lakhs.

(3) The market value of investment is Rs, 8.50 lakhs, and Cost is Rs. 7 lakhs. Therefore, the transfer to long term investments should be carried in the books at the Cost Price i.e., Rs. 7 lakhs.

(4) The market value of investment is Rs. 3.8lakhs, which is lower than its cost i.e. Rs 4 lakhs. Therefore, the transfer to long term investments should be carried in the books at the market value i.e., Rs. 3.8 lakhs.

5. The Investment portfolio of XYZ Ltd. as on 31.03.2020 consisted of the following:

			(Rs. in lacs)
	Current Investments	Cost	Fair Value as on 31.03.2020
(1)	1000 Equity Shares of A Ltd.	5	7
(2)	500 Equity Shares of B Ltd.	10	15
(3)	1000 Equity Shares of C Ltd.	15	12
	Total	30	34

Give your comments on the following:

(i) The company wants to value the above portfolio at Rs. 30 lakhs being lower of cost or fair market value.

(ii) Company wants to transfer 1000 Equity Shares of C Ltd. from current investments to long term investments on 31.03.2020 at cost of Rs. 15 lakhs.

Solution: As per AS 13 "Accounting for Investments", Valuation of current investments on overall (or global) basis is not considered appropriate. Sometimes, the concern of an enterprise may be with the value of a category of related current investments and not with each individual investment, and accordingly the investments may be carried at the lower of cost and fair value computed category-wise (i.e. equity shares, preference shares, convertible debentures, etc.). However, the more prudent and appropriate method is to carry investments individually at the lower of cost and fair value.

(i) Hence the company has to value the current investment at Rs. 27 Lacs (A Ltd. shares at Rs. 5 lacs; B Ltd. shares at Rs. 10 lacs and C Ltd. shares at Rs. 12 lacs). The company's decision to value the portfolio at Rs. 30 lacs is not appropriate.

(ii) Moreover, where investments are reclassified from current to long-term, transfers are made at the lower of cost and fair value at the date of transfer.

Hence, the company has to make transfer of 1,000 equity shares of C Ltd. at Rs. 12 lacs (fair value) and not Rs. 15 lacs (cost) as the fair value is less than cost.

6. Z Bank has classified its total investment on 31-3-2021 into three categories (a) held to maturity (b) available for sale (c) held for trading as per the RBI Guidelines. 'Held to maturity' investments are carried at acquisition cost less amortized amount. 'Available for sale' investments are carried at marked to market. 'Held for trading' investments are valued at weekly intervals at market rates. Net depreciation, if any, is charged to revenue and net appreciation, if any, is ignored. You are required to comment whether the policy of the bank is in accordance with AS 13?

Solution: As per AS 13 'Accounting for Investments', the accounting standard is not applicable to Bank, Insurance Company, Mutual Funds. In this case Z Bank is a bank, therefore, AS 13 does not apply to it. For banks, the RBI has issued separate guidelines for classification and valuation of its investment and Z Bank should comply with those RBI Guidelines/Norms. Therefore, though Z Bank has not followed the provisions of AS 13, yet it would not be said as non-compliance since, it is complying with the norms stipulated by the RBI.

7. A manufacturing company purchased shares of another company from stock exchange on 1st May, 2007 at a cost of Rs.5,00,000. It also purchased Gold of Rs.2,00,000 and Silver of Rs.1,50,000 on 1st April, 2005. How will you treat these investments as per the applicable AS in the books of the company for the year ended on 31st March, 2008, if the values of these investments are as follows:

	Rs.
Shares	2,00,000
Gold	4,00,000
Silver	2,50,000

Solution: As per para 32 of AS 13 on 'Accounting for Investments', any investment of long term period is shown at cost.

Hence, the investment in Gold and Silver (purchased on 1st April 2005) shall continue to be shown at cost i.e., Rs. 2,00,000 and Rs.1,50,000 respectively as their value have increased.

Also as per AS 13, for investment in shares - if the investment is for short-term period then the loss of Rs. 3,00,000 is to be charged to profit & loss account for the year ended 31st March, 2008. If investment is of long term period then it will continue to be shown at cost in the Balance Sheet of the company. However, provision for diminution shall be made to recognize a decline, other than temporary, in the value of the investments, such reduction being determined and made for each investment individually.

8. Mr. X acquires 200 shares of a company on cum-right basis for Rs. 70,000. He subsequently receives an offer of right to acquire fresh shares in the company in the proportion of 1:1 at Rs. 107 each. He does not subscribe but sells all the rights for Rs. 12,000. The market value of the shares after their becoming ex-rights has also gone down to Rs. 60,000. What should be the accounting treatment in this case?

Solution: As per AS 13, where the investments are acquired on cum-right basis and the market value of investments immediately after their becoming ex-right is lower than the cost for which they were acquired, it may be appropriate to apply the sale proceeds of rights to reduce the carrying amount of such investments to the market value. In this case, the amount of the ex-right market value of 200 shares bought by X immediately after the declaration of rights falls to Rs.60,000. In this case, out of sale proceeds of Rs. 12,000, Rs. 10,000 may be applied to reduce the carrying amount to bring it to the market value and Rs. 2,000 would be credited to the profit and loss account.

9. Meera carried out the following transactions in the shares of Kumar Ltd.:

(1) On 1st April, 2019 she purchased 40,000 equity shares of Rs. 1 each fully paid up for Rs. 60,000.

(2) On 15th May 2019, Meera sold 8,000 shares for Rs. 15,200.

(3) At a meeting on 15th June 2019, the company decided:

(i) To make a bonus issue of one fully paid up share for every four shares held on 1st June 2019, and

(ii) To give its members the right to apply for one share for every five shares held on 1st June 2019 at a price of Rs. 1.50 per share of which 75 paise is payable on or before 15th July 2019 and the balance, 75 paise per share, on or before 15th September, 2019.

The shares issued under (i) and (ii) were not to rank for dividend for the year ending 31st December 2019.

(a) Meera received her bonus shares and took up 4,000 shares under the right issue, paying the sum thereon when due and selling the rights of the remaining shares at 40 paise per share; the proceeds were received on 30 th September 2019.

(b) On 15th March 2020, she received a dividend from Kumar Ltd. of 15 per cent in respect of the year ended 31st Dec 2019.

(c) On 30th March 2020, she received Rs. 28,000 from the sale of 20,000 shares.

You are required to record these transactions in the Investment Account in Meera's books for the year ended 31st March 2020 transferring any profits or losses on these transactions to Profit and Loss account. Apply average cost basis. Expenses and tax to be ignored.

Solution: **Investment Account (Shares in Kumar Limited) in the books of Meera**

Date	Particulars	No. of Shares	Dividend	Amount	Date	Particulars	No. of Shares	Dividend	Amount
2019			Rs.	Rs.	2019			Rs.	Rs.
April 1	To Bank (Purchases)	40,000	-	60,000	May 15	By Bank (Sale)	8,000	-	15,200
May 15	To Profit & Loss A/c (W.N.1)	-	-	3,200					
June15	To Bonus Issue	8,000	-	Nil	2020				
July 15	To Bank (@ 75 p. paid on 4,000 shares)	4,000	-	3,000	Mar. 15	By Bank (Dividend @ 15% on Rs. 32,000)		4,800	-
Sept.	To Bank (@ 75 p. paid on 4,000 shares)	-	-	3,000	Mar. 30	By Bank (Sale)	20,000	-	28,000
2020 Mar. 31	To Profit & Loss A/c (W.N.2)			3,455	Mar. 31	By Balance c/d (24,000/44,000) X 54,000	24,000	-	29,455
	To Profit & Loss A/c	-	4,800						
		52,000	4,800	72,655			52,000	4,800	72,655

Working Notes:

(1)	**Profit on Sale on 15-5-2019:**	**Rs.**
	Sales price	15,200
	Less: Cost of 8,000 shares @ Rs.1.50	12,000
	Profit	3,200
(2)	**Cost of 20,000 shares sold:**	**Rs.**
	Cost of 44,000 shares (48,000 + 6,000)	54,000
	Therefore, Cost of 20,000 shares (54,000/44,000 shares) X 20,000 Shares	24,545
	Profit on sale of 20,000 shares (Rs. 28,000 – Rs. 24,545)	**Rs. 3,455**

Note: Sale of right shall be considered at income and transfer into P & L Account

10. A Ltd. Purchased on 1st April, 2015 8% convertible debenture in C Ltd. of face value of Rs. 2,00,000 @ Rs.108. On 1st July, 2015 A Ltd. purchased another Rs. 1,00,000 debenture @ Rs. 112 cum interest.
On 1st October, 2015 Rs.80,000 debenture was sold @ Rs.105. On 1st December, 2015, C Ltd. give option for conversion of 8% convertible debentures into equity share of Rs. 10 each. A Ltd. Receive 5000 equity share in C Ltd. in conversion of 25% debenture held on that date. The Market price of debenture and equity share in C Ltd. at the end of year 2015 is Rs.110 and Rs.15 respectively.
Interest on debenture is payable each year on 31st March, and 30th September.
The accounting year of A Ltd. is calendar year.
Prepare investment account in the books of A Ltd. on average cost basis.

Solution: **Investment in 8% Convertible Debentures Account**

Date	Particulars	Face Value	Interest	Amount	Date	Particulars	No.	Interest	Amount
1.4.2015	To bank	2,00,000	Nil	2,16,000	30.9.2015	By Bank A/c		12,000	-
1.7.2015	To bank	1,00,000	2,000	1,10,000	1.10.2015	By Bank A/c	80,000	-	84,000
31.03.2016	(W.N#1)				1.12.2015	By investment in			
	To P&L A/c					Equity Shares A/c	55,000	-	59,767
	(B/F)					By Bank A/c		733	
					31.3.2016	By Bank A/c		6,600	
					31.3.2016	By Balance c/d	1,65,000	-	1,79,300
						By P& L A/c(B/F)			2,933
		3,00,000		3,26,000			3,00,000		3,26,000

INVESTMENT IN SHARES OF C LIMITED ACCOUNT

Date	Particulars	No. Of shares	Amount	Date	Particulars	No. of shares	Amount
1.12.2015	To investment in Debentures a/c	5,000	59,767	31.3.2016	By balance c/d (refer note)	5,000	59,767
		5,000	59,767			5,000	59,767

Working Notes:-

1. Calculation of purchase value of investments, sale value of investments and Interest Amount:-

a) Calculation of cost of investment purchased on 1.7.2015

Purchase Price (1,000 X 112)	1,12,000
Less:- Interest Amount (100000 X 8% X 3/12)	(2,000)
Purchase Price (Net)	1,10,000

b) Interest Amount as on 30/09/2015 = 3,00,000 X 8% X 6/12 = Rs. 12,000

2. Calculation of cost of share received in conversion as on 01/12/15:-
Number of debentures to be converted=(2,00,000+1,00,000-80,000)x25%=55,000
Cost of debentures to be converted = {(2,16,000+1,10,000)x2,20,000/3,00,000}/25%= 59,767
Interest Amount as on 01/12/15 = 55,000 X 8% X 2/12 = Rs. 733

3. Calculation of interest to be received on 31.3.2016 = 1,65,000 X 8% X 6/12 = Rs. 6,600

4. Valuation of investments in debenture : Lower of two
a) Cost of investment in debenture (2,16,000+1,10,000)x(1,65,000/3,00,000) = 1,79,300
or
b) Market value on balance sheet date (1,65,000x110) = 1,81,500
Therefore, Valuation of investments 1,79,300

5. Valuation of investments in Equity Shares: Lower of two
a) Cost of investment in Equity Shares = 59,767
or
b) Market value on balance sheet date (5,000 X 15) = 75,000
Therefore, Valuation of investments 59,767

11. Mr. Z has made following transactions during the financial year 2020-21:
Investment 1: 8% Corporate Bonds having face value ₹ 100.

Date	Particulars
01-06-2020	Purchased 36,000 Bonds at ₹ 86 cum-interest. Interest is payable on 30th September and 31st March every year
15-02-2021	Sold 24,000 Bonds at ₹ 92 ex-interest

Interest on the bonds is received on 30th September and 31st March.

Investment 2: Equity Shares of G Ltd having face value ₹ 10

Date	Particulars
01-04-2020	Opening balance 8,000 equity shares at a book value of ₹ 190 per share.
01-05-2020	Purchased 7,000 equity shares@ ₹ 230 on cum right basis; Brokerage of 1% was paid in addition.
15-06-2020	The company announced a bonus issue of 2 shares for every 5 shares held
01-08-2020	The company made a rights issue of 1 share for every 7 shares held at ₹ 230 per share. The entire money was payable by 31.08.2020
25-08-2020	Rights to the extent of 30% of his entitlements was sold @ ₹ 75 per share. The remaining rights were subscribed.
16-09-2020	Dividend @ ₹ 6 per share for the year ended 31.03.2020 was received on 16.09.2020. No dividend payable on Right issue and Bonus issue.
01-12-2020	Sold 7,000 shares @ 260 per share. Brokerage of 1% was incurred extra.
25-01-2021	Received interim dividend @ ₹ 3 per share for the year 2020-21.
31-03-2021	The shares were quoted in the stock exchange @ ₹ 260.

Both investments have been classified as Current investment in the books of Mr. Z. On 15th May 2021, Mr. Z decides to reclassify investment in equity shares of G Ltd. as Long term Investment. On 15th May 2021, the shares were quoted in the stock exchange @ ₹ 180.
You are required to:

(i) Prepare Investment Accounts in the books of Mr. Z for the year 2020-21, assuming that the average cost method is followed.
(ii) Profit and loss Account for the year 2020-21, based on the above information.
(iii)Suggest values at which investment in equity shares should be reclassified in accordance with AS 13.

Solution:

(i) **In the books of Mr. Z**
Investment in 8% Corporate Bonds Account
For the period 01 April 2020 to 31 March 2021

Date	Particulars	Nos	Interest (₹)	Amount (₹)	Date	Particulars	Nos	Interest (₹)	Amount (₹)
1/6/20	To Bank A/c (WN1)	36,000	48,000	30,48,000	30/9/20	By Bank A/c (Interest 36,000 x 100 x 8% x 6/12)		1,44,000	
15/2/21	To Profit & Loss A/c (WN 3)			1,76,000	15/2/21	By Bank A/c (WN2)	24,000	72,000	22,08,000
31/3/21	To Profit & Loss A/c		2,16,000		31/3/21	By Bank A/c (Interest 12,000 x 100 x 8% x 6/12)		48,000	
						By Balance c/d (WN 4)	12,000		10,16,000
	Total	36,000	2,64,000	32,24,000		**Total**	36,000	2,64,000	32,24,000

Note: For computing the interest on the bonds sold on 15 Feb 2021, if number of days (138 days) is taken instead of months, the interest received on 15.02.2021 should be ₹72,592 and the total interest transferred to Profit & Loss Account should be ₹ 2,16,592.

Investment in Equity Shares of G Ltd
For the period 1st April 2020 to 31 March 2021

Date	Particulars	Nos	Dividend (₹)	Amount (₹)	Date	Particulars	Nos	Dividend (₹)	Amount (₹)
01/4/20	To Balance b/d	8,000		15,20,000	16/9/20	By Bank A/c (WN 7)		48,000	42,000
01/5/20	To Bank A/c (WN 5)	7,000		16,26,100	1/12/20	By Bank A/c (WN 8)	7000		18,01,800
15/6/20	To Bonus Shares	6,000			25/1/21	By Bank A/c (WN 10)		48,300	
25/8/20	To Bank A/c (Right Shares) (WN 6)	2,100		4,83,000	31/3/21	By Balance c/d (WN 11)	16,100		25,00,100
01/12/20	To Profit & Loss A/c (Sale of shares) (WN 9)			7,14,800					
31/3/21	To Profit & Loss A/c		96,300						
	Total	23,100	96,300	43,43,900		Total	23,100	96,300	43,43,900

Working Notes:

(1) Computation of the Interest element in the bonds purchased on 01 June 2020

No of Bonds purchased		36,000
Face value per bond		₹ 100
Face value of the bonds purchased		₹ 36,00,000
Interest Rate		8%
Interest Amount	(36,00,000 x 8% x 2/12)	₹ 48,000
Cum-interest per bond		₹ 86
Value of bond excluding interest	[(36,000 x ₹ 86) – ₹48,000]	₹ 30,48,000

(2) Computation of the Interest element in the bonds sold on 15 Feb 2021

No of Bonds sold		24,000
Face value per bond		₹ 100
Face value of the bonds sold		₹ 24,00,000
Interest Rate		8%
Interest Amount	(₹ 24,00,000 x 8% x 4.5/12)	= ₹ 72,000

(3) Computation of Profit on Sale of Bonds on 15 Feb 2021

No of Bonds sold		24,000
Face value per bond		₹ 100
Ex- interest Rate per bond		₹ 92
Sales proceeds		₹ 22,08,000
Average Cost of Bonds	(30,48,000/36,000) x 24,000	₹ 20,32,000
Profit on sale of bonds		
Sale Proceeds – Average Cost = (₹ 22,08,000 – ₹ 20,32,000)		₹ 1,76,000

(4) Valuation of Bonds as on 31 March 2021

No of Bonds held as on 31 Mar 2021		12,000
Average Cost of Bonds	(₹ 30,48,000/36,000) x 12,000	₹ 10,16,000

(5) Computation of the cost of the equity shares purchased on 01 May 2020

No of shares purchased	7,000
Cum right price per share	₹ 230
Cost of purchase	₹ 16,10,000
Brokerage @1%	₹ 16,100
Cost including brokerage	₹ 16,26,100

(6) Right Shares

No of Right Shares Issued	(8,000+7,000+6,000)/7	=	3,000 shares
No of right shares sold	3,000 shares x 30%	=	900 shares
Proceeds from sale of right shares to be credited to statement of profit & loss	900 shares x ₹ 75	=	₹ 67,500
No of right shares subscribed	3,000 - 900	=	2,100 shares
Amount of right shares subscribed	2,100 x 230	=	₹ 4,83,000

(7) Computation of Dividend Received on 16 Sept 2020

No of shares held during the period of dividend			8,000 shares
Dividend per share			₹ 6
Dividend Amount	8,000 x 6	=	₹ 48,000
No of shares received after the period of dividend (excluding bonus & right shares)			7,000 shares
Dividend per share			₹ 6
Dividend Amount	7,000 x ₹ 6	=	₹ 42,000

The amount of dividend for the period for which the shares were not held by the investor has been treated as capital receipt. Thus ₹ 42,000 shall be treated as capital receipt

(8) Sale Proceeds for the shares sold on 1st Dec. 2020

No of shares sold			7,000 Shares
Sale price per share			₹ 260
Proceeds from sale of share	7,000 x 260	=	₹ 18,20,000
Less: Brokerage @ 1%			₹ 18,200
Net Sale Proceeds			₹ 18,01,800

(9) Profit on sale of shares on 1st Dec. 2020

Sales Proceeds		₹ 18,01,800
Average Cost (15,20,000+16,26,100+4,83,000-42,000)/23,100x7,000	=	₹ 10,87,000
Profit on sale of shares Sales Proceeds – Average Cost = ₹ 18,01,800 - ₹ 10,87,000	=	₹ 7,14,800

(10) Computation of Amount of Interim Dividend

No of shares held	(8,000+7,000+6,000+2,100-7,000)	=	16,100
Dividend per share			₹ 3 per share
Dividend Received	16,100 shares x ₹ 3 per share	=	₹ 48,300

(11) Valuation of Shares as on 31 March 2021

Cost of Shares	(15,20,000 + 16,26,100 + 4,83,000 – 42,000) / 23,100 X 16,100	=	₹ 25,00,100
Market Value of Shares	₹ 260 x 16,100	=	₹ 41,86,000

Closing stock of equity shares has been value at ₹ 25,00,100 i.e. cost being lower than its market value.

(ii) **Profit & Loss Account (Extract)**
For the period 01 April 2020 to 31 March 2021

Particulars	Amount (₹)	Particulars	Amount (₹)
To Balance c/d	12,70,600	By Investment in 8% Corporate Bonds Account (Profit on sale of bonds)	1,76,000
		By Investment in 8% CorporateBonds Account (Interest on bonds)	2,16,000
		By Sale of Right Shares	67,500
		By Investment in Equity Shares of GLtd (Profit on sale of shares)	7,14,800
		By Investment in Equity Shares of GLtd (Dividend Income)	96,300

(iii) As per AS 13, when investments are classified from Current Investments to Long term Investments, transfer is made at Cost and Fair value, whichever is less (as on the date of transfer). So, in the given case valuation shall be done as follows:

Date of reclassification/transfer = 15 May 2021
Per Unit Cost of 16,100 shares held = ₹ 25,00,100/16,100 shares = ₹ 155.29
Market Price/Fair Value per share = ₹ 180

As the cost per unit is lower than its fair value, the shares are to be transferred at its cost i.e., at ₹ 155.29 per share on 15 May 2021

Note: The entire amount of sale proceeds from rights has been credited to Profit and Loss account in the above solution. However, the sale proceeds of rights in respect of 7,000 shares (purchased cum right on 1.5.20) can be applied to reduce the carrying amount of such investments (without crediting it to profit and loss account) considering that the value of these shares has reduced after becoming their ex-right. In that case, ₹ 22,500 (67,500X 7/21) will be applied to reduce the carrying amount of investment and ₹ 45,000 will be credited to profit and loss account.

12. The following information is presented by Mr. Z, relating to his holding in 9% Debentures of X Ltd.
Opening balance (face value) Rs.1,20,000, Cost Rs.1,18,000 (Face value of each unit is Rs.100).

01.03.2008 Purchased 200 units, ex-interest at Rs.98.
01.07.2008 Sold 500 units, ex-interest out of original holding at Rs.100.
01.10.2008 Purchased 150 units at Rs.98, cum interest.
01.11.2008 Sold 300 units, ex-interest at Rs.99 out of original holdings.

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

Solution: **9% Debentures of X Ltd. (Investment) Account**

Particulars		Face Value	Interest	Principal	Particulars		Face Value	Interest	Principal
2008		**Rs.**	**Rs.**	**Rs.**	**2008**		**Rs.**	**Rs.**	**Rs.**
Jan.1	To Balance b/d	1,20,000	2,700	1,18,000	March 31	By Bank A/c	-	6,300	-
March 1	To Bank A/c	20,000	750	19,600	July 1	By Bank A/c	50,000	1,125	50,000
July 1	To P&L A/c (transfer)	-	-	833	Sept. 30	By Bank A/c	-	4,050	-
					Nov. 1	By Bank A/c	30,000	225	29,700
Oct. 1	To Bank A/c	15,000	-	14,700	Dec. 31	By Balance c/d	75,000	1,688	73,633
Nov. 1	To P&L A/c	-	-	200					
Dec. 31	To P&L A/c (Transfer)		9,938	-					
		1,55,000	13,388	1,53,333			1,55,000	13,388	1,53,333

Working Note:

1. Interest element in opening balance of bonds = 1,20,000 x 9% x 3/12 = ₹ 2,700

2. Purchase of bonds on 1. 3.2008
Interest element in purchase of bonds = 200 x 100 x 9% x 5/12 = ₹ 750
Investment element in purchase of bonds = 200 x 98 = ₹ 19,600

3. Interest for half-year ended 31 March = 1,400 x 100 x 9% x 6/12 = ₹ 6,300

4. Sale of bonds on 1.7.2008
Interest element = 500 x 100 x 9% x 3/12 = ₹ 1,125
Investment element = 500 x 100 = ₹ 50,000

5. Profit on sale of bonds on 1.7.2008
Cost of bonds = (1,18,000/ 1,200) x 500 = ₹ 49,167
Sale proceeds = ₹ 50,000
Profit element = ₹ 833

6. Interest for half-year ended 30 September = 900 x 100 x 9% x 6/12 = ₹ 4,050

7. Sale of bonds on 1.11.2008
Interest element = 300 x 100 x 9% x 1/12 = ₹ 225
Investment element = 300 x 99 = ₹ 29,700

8. Profit on sale of bonds on 1.11.2008
Cost of bonds = (1,18,000/ 1,200) x 300 = ₹ 29,500
Sale proceeds = ₹ 29,700
Profit element = ₹ 200

9. Closing value of investment

Calculation of closing balance:	*Units*	**Cost**	Rs.
Bonds in hand remained in hand at 31st December 2008			
From original holding (1,20,000 – 50,000 – 30,000)=	40,000	(1,18,000/1,20,000) x 40,000	39,333
Purchased on 1st March	20,000		19,600
Purchased on 1st October	15,000		14,700
	75,000		73,633

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

1.4.20X1 Opening balance – Nominal value ₹ 1,20,000, Cost ₹ 1,18,000
1.7.20X1 100 Debentures purchased ex-interest at ₹ 98
1.10.20X1 Sold 200 Debentures ex-interest at ₹ 100
1.1.20X2 Purchased 50 Debentures at ₹ 98 ex-interest
1.2.20X2 Sold 200 Debentures ex-interest at ₹99

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

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

Solution: **Investment A/c of Mr. Purohit for the year ending on 31-3-20X2**
(Scrip: 8% Debentures of P Limited)
(Interest Payable on 30th September and 31st March)

Date	Particulars	Nominal Value	Interest	Cost	Date	Particulars	Nominal Value	Interest	Cost
			₹	₹				₹	₹
1.4.20X1	To Balance b/d	1,20,000	-	1,18,000	30.9.20X1	By Bank (1,300 x 100 x 8% x 6/12)	-	5,200	-
1.7.20X1	To Bank (ex-	10,000	200	9,898	1.10.20X1	By Bank (W.N.4)	20,000	-	19,800

	Interest) (W.N.1)								
1.10.20X1	To Profit & Loss A/c (W.N.4)			133	1.2.20X2	By Bank (ex-Interest) (W.N.5)	20,000	533	19,602
1.1.20X2	To Bank (ex-Interest) (W.N.2)	5,000	100	4,949	1.2.20X2	By Profit & Loss A/c (W.N.5)			64
31.3.20X2	To Profit & Loss A/c (Bal. fig.)	-	9,233		31.3.20X2	By Bank (950 x 100 x 8% x 6/12)	-	3,800	-
					31.3.20X2	By Balance c/d (W.N.3)	95,000	-	93,514
		1,35,000	9,533	1,32,980			1,35,000	9,533	1,32,980

Working Notes:

1. Purchase of debentures on 1.7.20X1

Interest element = 100 x 100 x 8% x 3/12 = ₹ 200

Investment element = (100 x 98) + [1% (100 x 98)] = ₹ 9,898

2. Purchase of debentures on 1.1.20X2

Interest element = 50 x 100 x 8% x 3/12 = ₹ 100

Investment element = {(50 x 98) + [1%(50 x 98)]} = ₹ 4,949

3. Valuation of closing balance as on 31.3.20X2:

Market value of 950 Debentures at ₹ 99		=	₹ 94,050
Cost of			
800 Debentures cost	= (1,18,000 / 1,20,000) X 80,000	=	78,667
100 Debentures cost		=	9,898
50 Debentures cost		=	4,949
			93,514

Value at the end = ₹ 93,514, i.e., whichever is less

4. Profit on sale of debentures as on 1.10.20X1

		₹
Sales price of debentures (200 x ₹ 100)		20,000
Less: Brokerage @ 1%		(200)
		19,800
Less: Cost of Debentures	(1,18,000 / 1,20,000) X 20,000	(19,667)
Profit on sale		133

5. Loss on sale of debentures as on 1.2.20X2

		₹
Sales price of debentures (200 x ₹ 99)		19,800
Less: Brokerage @ 1%		(198)
		19,602
Less: Cost of Debentures	(1,18,000 / 1,20,000) X 20,000	(19,666)
Loss on sale		64
Interest element in sale of investment = 200 x 100 x 8% x 4/12		**₹ 533**

AMALGAMATION OF COMPANIES

1. The summarized Balance Sheet of A Ltd. and B Ltd. as at 31st March, 2022 are as under:

	A Ltd. (in ₹)	B Ltd. (in ₹)
Equity shares of ₹10 each, fully paid up	30,00,000	24,00,000
Securities Premium Account	4,00,000	
General Reserve	6,20,000	5,00,000
Profit and Loss Account	3,60,000	3,20,000
Retirement Gratuity Fund Account	1,00,000	
10% Debentures	20,00,000	
Unsecured Loan (including loan from A Ltd.)	6,00,000	8,20,000
Trade Payables	1,00,000	3,40,000
	71,80,000	43,80,000
Land and Buildings	28,00,000	21,00,000
Plant and Machinery	20,00,000	7,60,000
Long term advance to B Ltd.	2,20,000	
Inventories	10,40,000	7,00,000
Trade Receivables	8,20,000	5,20,000
Cash and Bank	3,00,000	3,00,000
	71,80,000	43,80,000

B Ltd. is to declare and pay ₹ 1 per equity share as dividend, before the following amalgamation takes place with Z Ltd.

Z Ltd. was incorporated to take over the business of both A Ltd. and B Ltd.

(a) The authorized share capital of Z Ltd. is ₹ 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 ₹ 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 ₹ 2,00,000 is to be treated as actual liability.

(e) Liquidation expenses including Registered Valuer fees of A Ltd.₹ 50,000 and B Ltd. ₹ 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.**

		₹	₹
Business Purchase A/c	Dr.	54,00,000	
To Liquidator of A Ltd. A/c			54,00,000
Land & Building A/c	Dr.	28,00,000	
Plant & Machinery A/c	Dr.	20,00,000	
Long term advance to B Ltd. A/c	Dr.	2,20,000	
Inventories A/c	Dr.	10,40,000	
Trade Receivables A/c	Dr.	8,20,000	
Cash and Bank A/c	Dr.	3,00,000	
Goodwill A/c	Dr.	12,20,000	

To Retirement Gratuity Fund A/c			1,00,000
To 10% Debentures A/c			20,00,000
To Unsecured Loan A/c			6,00,000
To Trade Payables A/c			1,00,000
To Other liabilities A/c			2,00,000
To Business Purchase A/c			54,00,000
10% Debentures A/c	Dr.	20,00,000	
To 12% Debentures A/c			20,00,000
Liquidator of A Ltd. A/c	Dr.	54,00,000	
To Equity Share Capital A/c			27,00,000
To Securities Premium A/c			27,00,000
Business Purchase A/c	Dr.	28,80,000	
To Liquidator of B Ltd. A/c			28,80,000
Land and Building A/c	Dr.	21,00,000	
Plant & Machinery A/c	Dr.	7,60,000	
Inventories A/c	Dr.	7,00,000	
Trade Receivables A/c	Dr.	5,20,000	
Cash and Bank (less dividend) A/c	Dr.	60,000	
To Unsecured Loan A/c			8,20,000
To Trade Payables A/c			3,40,000
To Business Purchase A/c			28,80,000
To Capital Reserve A/c			1,00,000
Liquidators of B Ltd. A/c	Dr.	28,80,000	
To Equity Share Capital A/c			14,40,000
To Securities Premium A/c			14,40,000
Unsecured Loans A/c	Dr.	2,20,000	
To Long term Advance to B Ltd. A/c			2,20,000
*Capital Reserve A/c	Dr.	1,00,000	
To Cash and Bank A/c (Liquidation expenses)			80,000
To Goodwill A/c			20,000

Note:

1. The journal entries for A Ltd. and B Ltd. have been given separately in the above solution. Alternatively, the entries may be given as combined for both companies.
2. *Alternatively, following set of entries may be given in place of the last entry given in the above solution.

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

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

Particulars	**Note No.**	**(₹)**
I. **Equity and Liabilities**		
(1) **Shareholder's Funds**		
(a) Share Capital	1	41,40,000
(b) Reserves and Surplus	2	41,40,000
(2) **Non-Current Liabilities**		
(a) Long-term borrowings	3	20,00,000
(b) Long term provisions	4	1,00,000
(3) **Current Liabilities**		
(a) Short-term borrowings[1]	5	12,00,000
(b) Trade payables	6	4,40,000
(a) Other liability		2,00,000
Total		1,22,20,000
II. **Assets**		
(1) **Non-current assets**		
(a) i. Property, plant and equipment	7	76,60,000
ii. Intangible assets (Goodwill 12,20,000-20,000)		12,00,000
(2) **Current assets**		
(a) Inventories	8	17,40,000
(b) Trade receivables	9	13,40,000
(c) Cash and cash equivalents	10	2,80,000
Total		1,22,20,000

Notes to Accounts

		(₹)	(₹)
1.	Share Capital		
	Authorized Share Capital		
	6,00,000 Equity shares of ₹ 10 each		60,00,000
	Issued: 4,14,000 Equity shares of ₹ 10 each (all these shares were Issued for considerationother than cash)		41,40,000
2.	Reserves and surplus		
	Securities Premium Account(4,14,000 shares × ₹ 10)		41,40,000
3.	Long-term borrowings		
	12% Debentures		20,00,000
4	Long term Provisions		
	Retirement gratuity fund		1,00,000

5.	Short-term borrowings			
	Unsecured loans			
	A Ltd.	6,00,000		
	B Ltd.	8,20,000	14,20,000	
	Less: Mutual		(2,20,000)	12,00,000
6.	Trade payables			
	A Ltd.		1,00,000	
	B Ltd.		3,40,000	4,40,000
7.	Property, plant & equipment			
	Land and Building			
	A Ltd.		28,00,000	
	B Ltd.		21,00,000	49,00,000
	Plant and Machinery			
	A Ltd.		20,00,000	
	B Ltd.		7,60,000	27,60,000
				76,60,000
8.	Inventories			
	A Ltd.		10,40,000	
	B Ltd.		7,00,000	17,40,000
9	Trade receivables			
	A Ltd.		8,20,000	
	B Ltd.		5,20,000	13,40,000
10	Cash & cash equivalents			
	A Ltd.		3,00,000	
	B Ltd. [3,00,000-2,40,000(dividend)]		60,000	
			3,60,000	
	Less: Liquidation Expenses		(80,000)	2,80,000

Working Note:

Calculation of amount of Purchase Consideration

	A Ltd.	B Ltd.
Existing shares	3,00,000	2,40,000
Agreed value per share	₹18	₹12
Purchase consideration	54,00,000	28,80,000
No. of shares to be issued of ₹20 each (including ₹10 premium)	2,70,000	1,44,000
Face value of shares at ₹10	27,00,000	14,40,000
Premium of shares at ₹10	27,00,000	14,40,000

2. A Limited and B Limited are carrying on business of same nature. On 31st March, 2021 their summarized Balance Sheet was as follows:

	A Ltd.(₹)	B Ltd. (₹)
Share Capital		
- Equity Shares 10 each (Fully Paid)	12,00,000	7,20,000
- 10% Preference Shares of ₹ 100 each	6,00,000	-
- 8% Preference Shares of ₹ 100 each	-	5,00,000
General Reserve	3,00,000	2,50,000
Investment Allowance Reserve	-	60,000
Security Premium	2,40,000	-
Export Profit Reserve	1,80,000	1,20,000
Profit & Loss Account	2,16,000	1,92,000
9% Debentures (₹ 10 each)	3,00,000	2,00,000
Secured Loan	-	3,60,000
Sundry Creditors	3,12,000	2,04,000
Bills Payable	75,000	1,00,000
Other Current Liabilities	50,000	75,000
	34,73,000	27,81,000
Land and Building	10,80,000	8,40,000
Plant and Machinery	6,00,000	5,60,000
Office Equipment	3,45,000	2,10,000
Investments	96,000	3,00,000
Stock in Trade	6,30,000	4,20,000
Sundry Debtors	4,90,000	3,20,000
Bills Receivables	60,000	70,000
Cash at Bank	1,72,000	61,000
	34,73,000	27,81,000

A Limited take over B Limited on the above date, both companies agreeing on a scheme of Amalgamation on the following terms:

(a) A Limited will issue 80,000 Equity Shares of ₹ 10 each at par to the Equity Shareholders of B Limited.

(b) A Limited will issue 10% Preference Shares of ₹ 100 each to discharge the Preference Shareholders of B Limited at 15% premium in such a way that the existing dividend quantum of the preference shareholders of B Limited will not get affected. Accordingly, ₹ 5,00,000 pref. shares are discharged at ₹ 5,75,000 (5,00,000X 115%) by issue of 4,000 preference shares of ₹ 100 each at premium of ₹ 43.75 each.

(c) The Debentures of B Limited will be converted into equivalent number of Debentures of A Limited.

(d) All the Bills Receivable of A Limited were accepted by B Limited.

(e) A contingent liability of B Limited amounting to ₹ 72,000 to be treated as actual liability in trade payables.

(f) Expenses of Amalgamation amounted to ₹ 12,000 were borne by A Limited.

You are required to pass opening Journal Entries in A Limited and prepare the opening Balance Sheet of A Limited as on 1st April, 2021 after amalgamation, assuming that the amalgamation is in the nature of Merger.

Solution:

Journal Entries in the books of A Ltd.

Particulars		*Debit* ₹	*Credit* ₹
Business purchase A/c (W.N.1)	Dr.	13,75,000	
To Liquidator of B Ltd.			13,75,000
(Being business of B Ltd. taken over)			

Land & Building A/c	Dr.	8,40,000	
Plant and machinery A/c	Dr.	5,60,000	
Office equipment A/c	Dr.	2,10,000	
Investments A/c	Dr.	3,00,000	
Inventory A/c	Dr.	4,20,000	
Debtors A/c	Dr.	3,20,000	
Bills receivables A/c	Dr.	70,000	
Bank A/c	Dr.	61,000	
To General reserve A/c (W.N.2) (2,50,000-1,55,000)			95,000
To Export profit reserve A/c			1,20,000
To Investment allowance reserve A/c			60,000
To Profit and loss A/c			1,20,000
To Liability for 9% Debentures A/c (₹ 100 each)			2,00,000
To Secured Loan			3,60,000
To Trade creditors A/c			2,76,000
To Bills payables A/c			1,00,000
To Other current liabilities A/c			75,000
To Business purchase A/c			13,75,000
(Being assets and liabilities taken over)			
Liquidator of B Ltd.	Dr.	13,75,000	
To Equity share capital A/c			8,00,000
To 10% Preference share capital A/c			4,00,000
To Securities premium A/c			1,75,000
(Being purchase consideration discharged)			
General Reserve* A/c	Dr.	12,000	
To Cash at bank			12,000
(Being expenses of amalgamation paid)			
Liability for 9% Debentures in B Ltd. A/c	Dr.	2,00,000	
To 9% Debentures A/c			2,00,000
(Being debentures in B ltd. discharged by issuing own 9% debentures)			
Bills payables A/c	Dr.	60,000	
To Bill receivables A/c			60,000
(Cancellation of mutual owing on account of bills of exchange)			

*Alternatively, profit & loss A/c may be debited in place of general reserve A/c.

Opening Balance Sheet of A Ltd. (after absorption) as at 1st April, 2021

	Particulars	Notes	₹
	Equity and Liabilities		
1	Shareholders' funds		
a	Share capital	1	30,00,000
b	Reserves and Surplus	2	14,94,000

2		Non-current liabilities		
	a	Long-term borrowings	3	8,60,000
3		Current liabilities		
	a	Trade Payables	4	7,03,000
	b	Other current liabilities	5	1,25,000
		Total		61,82,000
		Assets		
1		Non-current assets		
	a	PPE	6	36,35,000
	b	Investments	7	3,96,000
2		Current assets		
	a	Inventories	8	10,50,000
	b	Trade receivables	9	8,80,000
	c	Cash and cash equivalents	10	2,21,000
		Total		61,82,000

Notes to accounts

			₹
1	Share Capital		
	Equity share capital		
	2,00,000 Equity shares of ₹ 10 each (Out of above, 80,000 shares were issued for consideration other than cash)		20,00,000
	Preference share capital		
	10,000 10% Preference shares of ₹ 100 each (Out of above, 4,000 shares were issued for consideration other than cash)		10,00,000
	Total		30,00,000
2	Reserves and Surplus		
	General Reserve		
	Opening balance	3,00,000	
	Add: Adjustment under scheme of amalgamation	95,000	
	Less: Amalgamation expense paid	(12,000)	3,83,000
	Securities premium (2,40,000+1,75,000)		4,15,000
	Export profit reserve		
	Opening balance	1,80,000	
	Add: Adjustment under scheme of amalgamation	1,20,000	3,00,000
	Investment allowance reserve		60,000
	Profit and loss account		
	Opening balance	2,16,000	
	Add: Adjustment under scheme of amalgamation	1,20,000	3,36,000
	Total		14,94,000

3	Long-term borrowings		
	Secured		
	9% Debentures	3,00,000	
	Add: Adjustment under scheme of amalgamation	2,00,000	
	Secured loan	3,60,000	8,60,000
4	Trade payables		
	Creditors: Opening balance	3,12,000	
	Add: Adjustment under scheme of amalgamation	2,76,000	5,88,000
	Bills Payables: Opening balance	75,000	
	Add: Adjustment under scheme of amalgamation	1,00,000	
	Less: Cancellation of mutual owning upon amalgamation	(60,000)	1,15,000
			7,03,000
5	Other current liabilities		
	Opening balance	50,000	
	Add: Adjustment under scheme of amalgamation	75,000	1,25,000
6	PPE		
	Land & Building- Opening balance	10,80,000	
	Add: Adjustment under scheme of amalgamation	8,40,000	19,20,000
	Plant and machinery- Opening balance	6,00,000	
	Add: Adjustment under scheme of amalgamation	5,60,000	11,60,000
	Office equipment- Opening balance	3,45,000	
	Add: Adjustment under scheme of amalgamation	2,10,000	5,55,000
	Total		36,35,000
7	Investments		
	Opening balance	96,000	
	Add: Adjustment under scheme of amalgamation	3,00,000	3,96,000
8	Inventories		
	Opening balance	6,30,000	
	Add: Adjustment under scheme of amalgamation	4,20,000	10,50,000
9	Trade receivables		
	Debtors: Opening balance	4,90,000	
	Add: Adjustment under scheme of amalgamation	3,20,000	8,10,000
	Bills Payables: Opening balance	60,000	
	Add: Adjustment under scheme of amalgamation	70,000	
	Less: Cancellation of mutual owning upon amalgamation	(60,000)	70,000
	Total		8,80,000
10	Cash and cash equivalents		
	Opening balance	1,72,000	
	Add: Adjustment under scheme of amalgamation	61,000	

Less: Amalgamation expense paid	(12,000)	2,21,000

Working Notes:

1. Calculation of purchase consideration

	₹
Equity shareholders of B Ltd. (80,000 x ₹ 10)	8,00,000
Preference shareholders of B Ltd. (5,00,000 x 115%)	5,75,000
Purchase consideration would be	13,75,000

2. Amount to be adjusted from general reserve

The difference between the amount recorded as share capital issued and the amount of share capital of transferor company should be adjusted in General Reserve.
Thus, General reserve will be adjusted as follows:

	₹
Purchase consideration	13,75,000
Less: Share capital issued (₹ 7,20,000 + ₹ 5,00,000)	(12,20,000)
Amount to be adjusted from general reserve	1,55,000

3. Calculation of balances of Profit & Loss and Sundry Creditors of B Limited to be taken over by A Limited

	P&L (₹)	Creditors (₹)
Balance as per Balance Sheet of B Limited	1,92,000	2,04,000
Less / Add: Contingent Trade Payable treated as Actual Liability	(72,000)	72,000
Taken by A Limited	1,20,000	2,76,000

3. P Ltd. and Q Ltd. agreed to amalgamate and form a new company called PQ Ltd. The summarized balance sheets of both the companies on the date of amalgamation stood as below:

Liabilities	P Ltd. Rs	Q Ltd. Rs	Assets	P Ltd. Rs	Q Ltd Rs
Equity Shares	8,20,000	3,20,000	Land & Building	4,50,000	3,40,000
(Rs 100 each)			Furniture & Fittings	1,00,000	50,000
9% Pref. Shares	3,80,000	2,80,000	Plant & Machinery	6,20,000	4,50,000
(Rs 100 each)			Trade receivables	3,25,000	1,50,000
8% Debentures	2,00,000	1,00,000	Inventory	2,33,000	1,05,000
General Reserve	1,50,000	50,000	Cash at bank	2,08,000	1,75,000
Profit & Loss A/c	3,52,000	2,05,000	Cash in hand	54,000	20,000
Unsecured Loan	-	1,75,000			
Trade payables	88,000	1,60,000			
	19,90,000	12,90,000		19,90,000	12,90,000

PQ Ltd. took over the assets and liabilities of both the companies at book value after creating provision @ 5% on inventory and trade receivables respectively and depreciating Furniture & Fittings by @ 10%, Plant and Machinery by @ 10%. The trade receivables of P Ltd. include Rs 25,000 due from Q Ltd.

PQ Ltd. will issue:

(i) 5 Preference shares of Rs 20 each @ Rs 18 paid up at a premium of Rs 4 per share for each pref. share held in both the companies.

(i) 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.

(ii) 6% Debentures to discharge the 8% debentures of both the companies.

(iii) 20,000 new equity shares of Rs 20 each for cash @ Rs18 paid up at a premium of Rs 4 per share.

PQ Ltd. will pay cash to equity shareholders of both the companies in order to adjust their rights as per the intrinsic value of the shares of both the companies.

You are required to prepare ledger accounts in the books of P Ltd. and Q Ltd. to close their books.

Solution: **In the Books of P Ltd.**

Realization Account

		Rs			Rs
To	Land & Building	4,50,000	By	8% Debentures	2,00,000
To	Plant & Machinery	6,20,000	By	Trade Payables	88,000
To	Furniture & Fitting	1,00,000	By	PQ Ltd.	16,02,100
To	Trade receivables	3,25,000		(Purchase consideration)	
To	Inventory/Stock	2,33,000	By	Equity Shareholders A/c	1,37,900
To	Cash at Bank	2,08,000		(loss)	
To	Cash in Hand	54,000			
To	Preference shareholders	38,000			
	(excess payment)				
		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

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

To	Realization A/c	16,02,100	By Shares in PQ Ltd.		
			For Equity	10,82,400	
			For Pref.	4,18,000	15,00,400
			By Cash		1,01,700
		16,02,100			16,02,100

8% Debentures holders Account

To 6% Debentures	2,00,000	By 8% Debentures	2,00,000

Books of Q Ltd.

Realization Account

		Rs			Rs
To	Land & Building	3,40,000	By	8% Debentures	1,00,000
To	Plant & Machinery	4,50,000	By	Trade payables	1,60,000
To	Furniture & Fittings	50,000	By	Unsecured loan	1,75,000
To	Trade receivables	1,50,000	By	PQ Ltd. (Purchase	
To	Inventory	1,05,000		consideration)	7,92,250
To	Cash at bank	1,75,000	By	Equity Shareholders A/c	90,750
To	Cash in hand	20,000		Loss	
To	Pref. shareholders	28,000			
		13,18,000			**13,18,000**

Equity Shareholders Account

	Rs		Rs
To Equity shares in PQ Ltd	4,22,400	By Share Capital	3,20,000
To Realization	90,750	By Profit & Loss A/c	2,05,000
To Cash	61,850	By General Reserve	50,000
	5,75,000		5,75,000

9% Preference Shareholders Account

	Rs		Rs
To Preference Shares in PQ Ltd.	3,08,000	By Share capital By Realization A/c	2,80,000 28,000
	3,08,000		**3,08,000**

PQ Ltd. Account

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

8% Debentures holders Account

	Rs		Rs
To 6% Debentures	1,00,000	By 8% Debentures	1,00,000

Working Notes:

(i)Purchase consideration

	P Ltd.	Q Ltd.
Payable to preference shareholders:	4,18,000	3,08,000
Preference shares at Rs 22 per share	10,82,400	4,22,400
Equity Shares at Rs 22 per share	1,01,700	61,850
Cash [See W.N. (ii)]	16,02,100	7,92,250

(ii)Value of Net Assets

		P Ltd.		Q Ltd.
Land & Building		4,50,000		3,40,000
Plant & Machinery less 10% Depreciation		5,58,000		4,05,000
Furniture & Fittings less 10% Depreciation		90,000		45,000
Trade receivables less 5%		3,08,750		1,42,500
Inventory less 5%		2,21,350		99,750
Cash at Bank		2,08,000		1,75,000
Cash in Hand		54,000		20,000
		18,90,100		12,27,250
Less: Debentures	2,00,000	-	1,00,000	
Trade payables	88,000		1,60,000	
Secured Loans	-	(2,88,000)	1,75,000	(4,35,000)
		16,02,100		7,92,250
Payable in Shares		15,00,400		7,30,400
Payable in cash		1,01,700		(61,850)

(iii)

	P	Q
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.

4. Galaxy Ltd. and Glory Ltd., are two companies engaged in the same business of chemicals. To mitigate competition, a new company Glorious Ltd, is to be formed to which the assets and liabilities of the existing companies, with certain exception, are to be transferred. The summarized Balance Sheet of Galaxy Ltd. and Glory Ltd. as at 31st March, 2020 are as follows:

				Galaxy Ltd.	Glory Ltd.
				Rs.	**Rs.**
(I)	***Equity & Liabilities***				
	(1)	***Shareholders' fund***			
		Share Capital			
		Equity shares of Rs. 10 each		8,40,000	4,55,000
		Reserves & Surplus	.		
		General Reserve		4,48,000	40,000
		Profit & Loss A/c		1,12,000	72,000
	(2)	***Non-current Liabilities***			
		Secured Loan			
		6% Debentures		-	3,30,000
	(3)	***Current Liabilities***			
		Trade Payables		4,20,000	1,83,000
			Total	18,20,000	10,80,000
(II)	***Assets***				
	(1)	***Non-current assets***			
		Property, Plant & Equipment			
		Freehold property, at cost		5,88,000	3,36,000
		Plant & Machinery, at cost less depreciation		1,40,000	84,000
		Motor vehicles, at cost less depreciation		56,000	-
	(2)	***Current Assets***			
		Inventories		3,36,000	4,38,000
		Trade Receivables		4,62,000	1,18,000
		Cash at Bank		2,38,000	1,04,000
			Total	18,20,000	10,80,000

Assets and Liabilities are to be taken at book value, with the following exceptions:

(i) The Debentures of Glory Ltd. are to be discharged, by the issue of 8% Debentures of Glorious Ltd. at a premium of 10%.

(ii) Plant and Machinery of Galaxy Ltd. are to be valued at Rs. 2,52,000.

(iii) Goodwill is to be valued at : Galaxy Ltd. Rs. 4,48,000 Glory Ltd. Rs. 1,68,000

(iv) Liquidator of Glory Ltd. is appointed for collection from trade debtors and payment to trade creditors. He retained the cash balance and collected Rs. 1,10,000 from debtors and paid Rs. 1,80,000 to trade creditors. Liquidator is entitled to receive 5% commission for collection and 2.5% for payments. The balance cash will be taken over by new company.

You are required to :

(1) Compute the number of shares to be issued to the shareholders of Galaxy Ltd. and Glory Ltd, assuming the nominal value of each share in Glorious Ltd. is Rs. 10.
(2) Prepare Balance Sheet of Glorious Ltd., as on 1st April, 2020 and also prepare notes to the accounts as per Schedule III of the Companies Act, 2013.

Solution:

(i) Calculation of Purchase consideration (or basis for issue of shares of Glorious Ltd.

	Galaxy Ltd.	**Glory Ltd.**
Purchase Consideration:	**Rs.**	**Rs.**
Goodwill	4,48,000	1,68,000
Freehold property	5,88,000	3,36,000
Plant and Machinery	2,52,000	84,000
Motor vehicles	56,000	-
Inventory	3,36,000	4,38,000
Trade receivables	4,62,000	-
Cash at Bank	2,38,000	24,000
	23,80,000	10,50,000
Less: Liabilities:		
6% Debentures (3,00,000 x 110%)	-	(3,30,000)
Trade payables	(4,20,000)	
Net Assets taken over	19,60,000	7,20,000
To be satisfied by issue of shares of Glorious. Ltd. @ Rs. 10 each	1,96,000	72,000

(ii) Balance Sheet of Glorious Ltd. as at 1st April, 2020

		Particulars	**Note No**	**Amount**
				Rs.
		EQUITY AND LIABILITIES		
1		Shareholders' funds		
	(a)	Share capital	1	26,80,000
	(b)	Reserves and surplus	2	30,000
2		Non-current liabilities		
	(a)	Long-term borrowings	3	3,00,000
3		Current liabilities		
	(a)	Trade payables		4,20,000
		Total		34,30,000

		ASSETS		
1		Non-current assets		
	(a)			
	i	Property, plant and equipment	4	13,16,000
	ii	Intangible assets	5	6,16,000
2		Current assets		
	(a)	Inventories	6	7,74,000
	(b)	Trade receivables		4,62,000
	(c)	Cash and cash equivalents	7	2,62,000
		Total		34,30,000

Notes to accounts:

		Rs.	Rs.
1.	Share Capital		
	Equity share capital		
	2,68,000 shares of Rs. 10 each		26,80,000
	(All the above shares are issued for consideration other than cash)		
2.	Reserves and surplus		
	Securities Premium		
	(10% premium on debentures of Rs. 3,00,000)		30,000
3.	Long-term borrowings		
	Secured		
	8% 3,000 Debentures of Rs. 100 each		3,00,000
4.	Property Plant and Equipment		
	Freehold property		
	Galaxy Ltd.	5,88,000	
	Glory Ltd.	3,36,000	9,24,000
	Plant and Machinery		
	Galaxy Ltd.	2,52,000	
	Glory Ltd.	84,000	3,36,000
	Motor vehicles - Galaxy Ltd.		56,000
			13,16,000
5	Intangible assets		
	Goodwill		
	Galaxy Ltd.	4,48,000	
	Glory Ltd.	1,68,000	6,16,000
6	Inventories		
	Galaxy Ltd.	3,36,000	
	Glory Ltd.	4,38,000	7,74,000

7	Cash and cash equivalents		
	Galaxy Ltd.	2,38,000	
	Glory Ltd.(As per working note)	24,000	2,62,000

Working note:
Calculation of cash balance of Glory Limited to be taken over by Glorious Limited

		Rs.
Cash balance as at 31st March, 2020		1,04,000
Add: Received from debtors		1,10,000
		2,14,000
Less: paid to creditors		(1,80,000)
		34,000
Less: Commission to liquidators		
On Debtors @ 5%	5,500	
On Creditors @ 2.5%	4,500	(10,000)
		24,000

Note:

a. It is assumed that the nominal value of debentures of Glory Ltd. is Rs. 100 each.

b. As per the information given in the question, debentures of Glory Ltd. are to be discharged by the issue of debentures of Glorious Ltd. at premium of 10%. It is assumed in the above solution that the debentures are issued at premium of Rs. 10 for discharge of debentures of Rs. 3,30,000. Alternative answer considering other reasonable assumption is also possible.

5. The following are the Balance Sheets of Andrew Ltd. and Barry Ltd., as at 31.12.2007:

Andrew Ltd.

(in Rs.'000s)

Liabilities		**Assets**	
Share capital		Fixed assets	3,400
3,00,000 Equity shares of Rs.10 Each	3,000	Stock (pledged with secured loan creditors)	18,400
10,000 Preference shares of Rs.100 each	1,000	Other Current assets	3,600
General reserve	400	Profit and Loss account	16,600
Secured loans (secured against pledge of stocks)	16,000		
Unsecured loans	8,600		
Current liabilities	13,000		
	42,000		42,000

Barry Ltd.

(in Rs.'000s)

Liabilities		**Assets**	
Share capital		Fixed assets	6,800
1,00,000 Equity shares of Rs.10 Each	1,000	Current assets	9,600
General reserve	2,800		
Secured loans	8,000		
Current liabilities	4,600		
	16,400		16,400

Both the companies go into liquidation and Charlie Ltd., is formed to take over their businesses. The following information is given:

(a) All Current assets of two companies, except pledged stock are taken over by Charlie Ltd. The realisable value of all Current assets are 80% of book values in case of Andrew Ltd. and 70% for Barry Ltd. Fixed assets are taken over at book value.

(b) The break up of Current liabilities is as follows:

	Andrew Ltd. Rs.	Barry Ltd. Rs.
Statutory liabilities (including Rs.22 lakh in case of Andrew Ltd. in case of a claim not having been admitted shown as contingent liability)	72,00,000	10,00,000
Liability to employees	30,00,000	18,00,000

The balance of Current liability is miscellaneous creditors.

(c) Secured loans include Rs.16,00,000 accrued interest in case of Barry Ltd.

(d) 2,00,000 equity shares of Rs.10 each are allotted by Charlie Ltd. at par against cash payment of entire face value to the shareholders of Andrew Ltd. and Barry Ltd. in the ratio of shares held by them in Andrew Ltd. and Barry Ltd.

(e) Preference shareholders are issued Equity shares worth Rs.2,00,000 in lieu of present holdings.

(f) Secured loan creditors agree to continue the balance amount of their loans to Charlie Ltd. after adjusting value of pledged security in case of Andrew Ltd. and after waiving 50% of interest due in the case of Barry Ltd.

(g) Unsecured loans are taken over by Charlie Ltd. at 25% of Loan amounts.

(h) Employees are issued fully paid Equity shares in Charlie Ltd. in full settlement of their dues.

(i) Statutory liabilities are taken over by Charlie Ltd. at full values and miscellaneous creditors are taken over at 80% of the book value.

Show the opening Balance Sheet of Charlie Ltd. Workings should be part of the answer.

Solution: **Balance sheet of Charlie Ltd. as at 31st December, 2011**

Particulars	**Note No.**	**(Rs.'000)**
I. **Equity and Liabilities**		
(1) **Shareholder's Funds**		
Share Capital	1	7,000
(2) **Non-Current Liabilities**		
Long-term borrowings	2	10,630
(3) **Current Liabilities**	3	13,640
Total		31,270
II. **Assets**		
(1) **Non-current assets**		
i. Property, Plant and Equipment		
ii. Intangible assets	4	10,200
(2) **Current assets**	5	9,470
Total	6	11.600
		31,270

Notes to Accounts

			(Rs.000)
1.	Share Capital *Issued, subscribed & Paid up:* 7,00,000 equity shares of Rs. 10 each, fully paid up (W.N.5) (of the above 5,00,000 shares have been issued for consideration other than cash)		7,000
2.	Long Term Borrowings		
	Secured loans (Rs. 1,280 +Rs. 7,200) – WN 2	8,480	
	Unsecured Loans (25% of Rs. 8,600)	2,150	10,630
3.	Current Liabilities (Rs. 7,200 +Rs. 1,000 +Rs. 4,000 +Rs.1,440)		13,640
4.	Property, Plant and Equipment Fixed Assets (Rs. 3,400 +Rs. 6,800)		10,200

5.	Intangible assets		
	Goodwill (W.N.4)		9,470
6.	Current Assets		
	Cash & Cash Equivalent	2,000	
	Other Current Assets (Rs. 2,880+Rs. 6,720)	9,600	11,600

Working Notes:

1. Value of miscellaneous creditors taken over by Charlie Ltd. (Rs.'000)

	Andrew Ltd.	**Barry Ltd**
Given in balance sheet	13,000	4,600
Less: Statutory liabilities [72 lakhs – 22 lakhs]	(5,000)	(1,000)
Liability to employees	(3,000)	(1,800)
Miscellaneous creditors	5,000	1,800
80% thereof	4,000	1,440

2. Value of total liabilities taken over by Charlie Ltd. (Rs. '000)

	Andrew Ltd.		**Barry Ltd.**	
Current liabilities				
Statutory liabilities	7,200		1,000	
Liability to employees	3,000		1,800	
Miscellaneous creditors (W.N.1)	4,000	14,200	1,440	4,240
Secured loans				
Given in Balance Sheet	16,000		8,000	
Interest waived -	-		800	7,200
Value of Stock				
(80% of Rs. 184 lakhs)	14,720	1,280		
Unsecured Loans				
(25% of Rs. 86 lakhs)		2,150		-
		17,630		11,440

3. Assets taken over by Charlie Ltd. (Rs. '000)

	Andrew Ltd.	**Barry Ltd**
Fixed Assets (Assumed on book value basis)	3,400	6,800
Current Assets 80% and 70% respectively of book value	2,880	6,720
	6,280	13,520

4. Goodwill / Capital Reserve on amalgamation (Rs. '000)

Liabilities taken over (W.N. 2)		17,630	11,440
Equity shares to be issued to Preference Shareholders		200	-
	A	17,830	11,440
Less: total assets taken over (W.N. 3)	B	(6,280)	(13,520)
	A-B	11,550	(2,080)
		Goodwill	Capital Reserve
Net Goodwill		9,470	

5. Equity shares issued by Charlie Ltd.

			Number
(i)	For Cash		2,00,000
	For consideration other than cash		
(ii)	In Discharge of Liabilities to Employees	4,80,000	
(iii)	To Preference shareholder	20,000	5,00,000
			7,00,000
	Value of shares (Rs. 10 x 7,00,000) Rs. 70 lakhs		Rs.70 lakhs

6. The summarized Balance Sheet of Srishti Ltd as on 31st March 2014 was as follows:

Liabilities	Amount (Rs)	Assets	Amount (Rs)
Equity Shares of Rs 10 fully paid	30,00,000	Good will	5,00,000
Export profit Reserves	8,50,000	Tangible Fixed Assets	30,00,000
General Reserves	50,000	Stock	10,40,000
Profit and loss Account	5,00,000	Debtors	1,80,000
9%Dedentures	5,00,000	Cash &Bank	2,80,000
Trade Creditors	1,00,000		
	50,00,000		50,00,000

ANU Ltd. agreed to absorb the business of SRISHTI Ltd. with effect from 1st April, 2014.

a. The purchase consideration settled by ANU Ltd. as agreed:
   (i) 4,50,000 equity Shares of Rs 10each issued by ANU Ltd. by valuing its share @Rs15per share.
   (ii) Cash payment equivalent to Rs 2.50 for every share in SRISHTI Ltd.
b. The issue of such an amount of paid 8% Debentures in ANU Ltd. at 96% as is sufficient to discharge 9% Debentures in SRISHTI Ltd. at a premium of 20%.
c. ANU Ltd. will take over the tangible Fixed Assets at 100%more than the book value, Stock at Rs 7,10,000 and Debtors at their face value subject to a provision of 5%for doubtful Debts.
d. The actual cost of liquidation of SRISHTI Ltd. was Rs 75,000 Liquidation cost of SRISHTI Ltd. is to be reimbursed by ANU Ltd. to the extent of Rs 50.000.
e. Statutory Reserves are to be maintained for 1 more year.

You are required to:

(i) Close the books of SRISHIT Ltd. by preparing Realisation Account, ANU Ltd. Account, Shareholders Account and Debenture Account and

(ii) Pass Journal Entries in the books of ANU Ltd. regarding acquisition of business.

Solution:

(i) **In the books of Srishti Ltd.**

Realisation Account

	₹		₹
To Goodwill	5,00,000	By 9% Debentures	5,00,000
To Tangible Fixed Assets	30,00,000	By Creditors	1,00,000
To Stock	10,40,000	By By Anu Ltd. (Purchase consideration)	75,00,000
To Debtors	1,80,000		
To Cash & Bank A/c (2,80,000- 25,000)	2,55,000		
To Cash & Bank A/c (Realization expenses)	25,000		
To Profit on realization transfer to shareholders	31,00,000		
	81,00,000		81,00,000

Equity Shareholders A/c

		₹			₹
			By	Equity Share Capital	30,00,000
To	Equity Shares in Anu Ltd.	67,50,000	By	Export Profit Reserves	8,50,000
To	Cash & Bank A/c	7,50,000	By	General Reserves	50,000
			By	P & L A/c	5,00,000
			By	Realization A/c	31,00,000
		75,00,000			75,00,000

9% Debentures Account

	₹		₹
To Realization A/c	5,00,000	By Balance b/d	5,00,000

Anu Ltd.

	₹		₹
To Realization A/c	75,00,000	By Share Capital	67,50,000
		By Bank A/c	7,50,000
	75,00,000		75,00,000

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

			₹	₹
1	Business Purchase A/c	Dr.	75,00,000	
	To Liquidator of Srishti Ltd			75,00,000
	(Being business of Srishti Ltd. taken over)			
2	Tangible Fixed Assets	Dr	60,00,000	
	Stock	Dr	7,10,000	
	Debtors	Dr	1,80,000	
	Cash & Bank A/c	Dr	2,55,000	
	Goodwill A/c (Bal. fig.)	Dr	10,64,000	
	To Provision for doubtful debts			9,000
	To Liability for 9 % Debentures			6,00,000
	To Creditors			1,00,000
	To Business Purchase account			75,00,000
	(Being assets and liabilities taken over)			
3	Amalgamation Adjustment Reserve A/c	Dr.	8,50,000	
	To Export Profit Reserves			8,50,000
	(Being statutory Reserves taken over)			
4	Goodwill	Dr.	50,000	
	To Bank A/c			50,000
	(Liquidation expenses reimbursed))			
5	Liquidator of Shristi Ltd.	Dr.	75,00,000	
	To Equity Share Capital			45,00,000
	To Securities Premium			22,50,000
	To Bank A/c			7,50,000
	(Being purchase consideration discharged)			

6	Liability for 9% Debentures (5,00,000 x 120/100) Discount on issue of debentures To 8% Debentures (6,00,000 x 100/96) (Being liability of debenture holders' discharged)	Dr.	6,00,000 25,000	 6,25,000

Working Note 1:
Purchase consideration computation

Cash payment for (3,00,000 x ₹ 2.5)	7,50,000
Equity Shares (4,50,000 x ₹ 15)	67,50,000
	75,00,000

7. The following is the Balance Sheet of A Ltd. as at 31st March, 2006:

Liabilities	Rs.	Assets	Rs.
8,000 equity shares of Rs.100 each	8,00,000	Building	3,40,000
10% debentures	4,00,000	Machinery	6,40,000
Loan from A	1,60,000	Stock	2,20,000
Creditors	3,20,000	Debtors	2,60,000
General Reserve	80,000	Bank	1,36,000
		Goodwill	1,30,000
		Misc. Expenses	34,000
Total	17,60,000	Total	17,60,000

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

(i) B Ltd. would take over all Assets, except bank balance at their book values less 10%. Goodwill is to be valued at 4 year's purchase of superprofits, assuming that the normal rate of return be 8% on the combined amount of share capital and general reserve.

(ii) B Ltd. is to take over creditors at book value.

(iii) 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, 2006 goods costing Rs.1,20,000 to A Ltd. for Rs.1,60,000. Rs.1,00,000 worth of goods are still in stock of A Ltd. on 31st March, 2006. Creditors 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, 2006 after the takeover.

Solution: **Books of A Limited**

Realisation Account

		Rs.		Rs.
To	Building	3,40,000	By Creditors	3,20,000
To	Machinery	6,40,000	By B Ltd.	12,10,000
To	Stock	2,20,000	By Equity Shareholders (Loss)	76,000
To	Debtors	2,60,000		
To	Goodwill	1,30,000		
To	Bank (Exp.)	16,000		
		16,06,000		16,06,000

Bank Account

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

10% Debentures Account

To	Bank	4,00,000	By	Balance b/d	4,00,000
		4,00,000			4,00,000

Loan from A Account

To	Bank	1,60,000	By	Balance b/d	1,60,000
		1,60,000			1,60,000

Misc. Expenses Account

To	Balance b/d	34,000	By	Equity shareholders	34,000
		34,000			34,000

General Reserve Account

To	Equity shareholders	80,000	By	Balance b/d	80,000
		80,000			80,000

B Ltd. Account

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

To	B Ltd.	6,10,000	By	Equity shareholders	6,10,000
		6,10,000			6,10,000

Equity Share Holders Account

To	Realisation	76,000	By	Equity share capital	8,00,000
To	Misc. 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 at 1st April, 2006

Particulars	Rs.	Rs.
I. Equity and Liabilities		
Shareholder fund:-		
a) Share Capital:		
4880 Equity shares of Rs.100 Each (Shares have been issued for consideration other than cash)		4,88,000
b) Reserve and Surplus		
Security Premium		1,22,000
Current Liability		
Creditors (3,20,000 - 40,000)		2,80,000
Bank Overdraft		6,00,000
Total		**14,90,000**
II. Assets		
Non-current Assets		
Property, Plant and Equipment		
Tangible		
Building		3,06,000
Machine		5,76,000
Intangible(2,16,000+15,000)		2,31,000
Current Assets		
Stock (1,98,000 -15,000)		1,83,000
Debtors (2,60,000 – 40,000-26,000)		1,94,000
Total		**14,90,000**

Working Notes:

1. Valuation of Goodwill

		Rs.
Average profit		1,24,400
Less: 8% of Rs.8,80,000		70,400
Super profit		54,000
Value of Goodwill = 54000 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
Stock		1,98,000
Debtors		2,60,000
Total Assets		15,56,000
Less: Creditors	3,20,000	
Provision for bad debts	26,000	3,46,000
Net Assets		12,10,000

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

3. Unrealised Profit on Stock

	Rs.
The stock of A Ltd. includes goods worth Rs.1,00,000 which was sold by B Ltd. on profit. Unrealized profit on this stock will be 40,000/160,000 x 1,00,000	25,000
As B Ltd purchased assets of A Ltd. at a price 10% less than the book value, 10% need to be adjusted from the stock i.e., 10% of Rs.1,00,000.	(-10,000)
Amount of unrealized profit	15,000

8. On 1st April, 2018, Tina Ltd. take over the business of Rina Ltd. and discharged purchase consideration as follows:

(a) Issued 50,000 fully paid Equity shares of ₹ 10 each at a premium of ₹ 5 per share to the equity shareholders of Rina Ltd.

(b) Cash payment of ₹ 50,000 was made to equity shareholders of Rina Ltd.

(c) Issued 2,000 fully paid 12% Preference shares of ₹ 100 each at par to discharge the preference shareholders of Rina Ltd.

(d) Debentures of Rina Ltd. (₹ 1,20,000) will be converted into equal number and amount of 10% debentures of Tina Ltd.

Calculate the amount of Purchase consideration as per AS-14 and pass Journal Entry relating to discharge of purchase consideration in the books of Tina Ltd.

Solution: I Calculation of amount of purchase consideration

Particulars	**₹**
Equity Shares (50,000 x 15)	7,50,000
Cash payment	50,000
12% Preference Share Capital	2,00,000
Purchase Consideration	10,00,000

As per AS 14, consideration for the amalgamation means the aggregate of the shares and other securities issued and the payment made in the form of cash or other assets by the transferee company to the shareholders of the transferor company. Thus, payment to debenture holders are not covered by the term 'consideration'.

II. Journal entry relating to discharge of consideration in the books of Tina Ltd.

Liquidation of Rina Ltd.A/c	10,00,000	
To Equity share capital A/c		5,00,000
To 12% Preference share capital A/c		2,00,000
To Securities premium A/c		2,50,000
To Bank/Cash A/c		50,000
(Discharge of purchase consideration)		

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

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

Notes to Accounts

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

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

	Truth Limited (₹)	**Myth Limited (₹)**
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 Ltd on the basis of intrinsic value per share. Prepare Balance Sheet of Truth Ltd after the amalgamation.

Solution: Balance Sheet of Truth Ltd. (after amalgamated with Myth Ltd.) as at 1.4.2021

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

Notes to Accounts

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

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

Working Notes:

(1) Valuation of Goodwill

(i) Capital Employed

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

(ii) Average Profit before Tax

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

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

(2) Intrinsic Value per Share

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

** 1,50,000 X (14% / 12%)= 1,75,000

(3) Purchase Consideration & manner of its discharge

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

10. The following are the summarized Balance Sheet of VT Ltd. and MG Ltd. as on 31St March, 2018:

Particulars	VT Ltd. (Rs.)	MG Ltd. (Rs.)
Equity and Liabilities		
Equity Shares of Rs. 10 each	12,00,000	6,00,000
10% Pref. Shares of Rs. 100 each	4,00,000	2,00,000
Reserve and Surplus	6,00,000	4,00,000
12% Debentures	4,00,000	3,00,000
Trade Payables	5,00,000	3,00,000
Total	31,00,000	18,00,000
Assets		
Fixed Assets	14,00,000	5,00,000
Investment	1,60,000	1,60,000
Inventory	4,80,000	6,40,000
Trade Receivables	8,40,000	4,20,000
Cash at Bank	2,20,000	80,000
Total	31,00,000	18,00,000

Details of Trade receivables and trade payables are as under :

	VT Ltd. (Rs.)	MG Ltd. (Rs.)
Trade Receivable		
Debtors	7,20,000	3,80,000
Bills Receivable	1,20,000	40,000
	8,40,000	4,20,000

Trade Payables		
Sundry Creditors	4,40,000	2,50,000
Bills Payable	60,000	50,000
	5,00,000	3,00,000

- Fixed Assets of both the companies are to be revalued at 15% above book value.
- Inventory in Trade and Debtors are taken over 5% lesser than their book value.
- Both the companies are to pay 10% equity dividend, Preference dividend having been already paid.

After the above transactions are given effect to, VT Ltd. will absorb MG Ltd. on the following terms:

(i) VT Ltd. will issue 16 Equity Shares of Rs. 10 each at par against 12 Shares of MG Ltd.
(ii) 10% Preference Shareholders of MG Ltd. will be paid at 10% discount by issue of 10% Preference Shares of Rs. 100 each at par in VT Ltd.
(iii) 12% Debenture holders of MG Ltd. are to be paid at 8% premium by 12% Debentures in VT Ltd. issued at a discount of 10%.
(iv) Rs. 60,000 is to be paid by VT Ltd. to MG Ltd. for Liquidation expenses.
(v) Sundry Debtors of MG Ltd. includes Rs. 20,000 due from VT Ltd.

You are required to prepare:
(1) Journal entries in the books of VT Ltd.
(2) Statement of consideration payable by VT Ltd.

Solution:

(1) Journal Entries in the Books of VT Ltd.

			Dr.	Cr.
(i)	Fixed Assets	Dr.	2,10,000	
	To Revaluation Reserve			2,10,000
	(Being Revaluation of fixed assets at 15% above book value)			
(ii)	Reserve and Surplus	Dr.	1,20,000	
	To Equity Dividend			1,20,000
	(Being Declaration of equity dividend @ 10%)			
(iii)	Equity Dividend	Dr.	1,20,000	
	To Bank Account			1,20,000
	(Being Payment of equity dividend)			
(iv)	Business Purchase Account	Dr.	9,80,000	
	To Liquidator of MG Ltd.			9,80,000
	(Being Consideration payable for the business taken over from MG Ltd.)			
(v)	Fixed Assets (115% of Rs. 5,00,000)	Dr.	5,75,000	
	Inventory (95% of Rs. 6,40,000)	Dr.	6,08,000	
	Debtors	Dr.	3,80,000	
	Bills Receivable	Dr.	40,000	
	Investment	Dr.	1,60,000	
	Cash at Bank	Dr.	20,000	
	(Rs. 80,000 –Rs. 60,000 dividend paid)			
	To Provision for Bad Debts (5% of Rs. 3,80,000)			19,000
	To Sundry Creditors			2,50,000
	To Bills Payable			50,000
	To Debentures holder of MG Ltd.			3,24,000
	To Business Purchase Account			9,80,000
	To Capital Reserve (Balancing figure)			1,60,000
	(Being Incorporation of various assets and liabilities taken over from MG Ltd.)			

(vi)	Liquidator of MG Ltd.	Dr.	9,80,000	
	To Equity Share Capital			8,00,000
	To 10% Preference Share Capital			1,80,000
	(Being Discharge of consideration for MG Ltd.'s business)			
(vii)	Debentures holder of MG Ltd. (Rs. 3,00,000 × 108%)	Dr.	3,24,000	
	Discount on Issue of Debentures	Dr.	36,000	
	To 12% Debentures (3,24,000/90%)			3,60,000
	(Being allotment of 12% Debentures to debenture holders of MG Ltd. at a discount of 10%)			
(viii)	Sundry Creditors A/c	Dr.	20,000	
	To Sundry Debtors A/c			20,000
	(Being Cancellation of mutual owing)			
(ix)	Capital Reserve	Dr.	60,000	
	To Bank			60,000
	(Being liquidation expenses reimbursed to MG Ltd.)			

(2) Statement of Consideration payable by VT Ltd.

ESH: Shares to be allotted (60,000/12) X 16 = 80,000 shares of VT Ltd.	
Issued 80,000 shares of Rs. 10 each i.e.	Rs. 8,00,000
PSH: For 10% preference shares, to be paid at 10% discount	
$\frac{\text{Rs. } 2,00,000 \times 90}{100}$	Rs. 1,80,000
Consideration amount [(i) + (ii)]	Rs. 9,80,000

ACCOUNTING FOR BRANCHES INCLUDING FOREIGN BRANCHES

1. KP Ltd. manufactures a range of goods which it sells to wholesale customers only from its head office. In addition, The H.O. transfers goods to a newly opened branch at factory cost plus 15%. The branch then sells these goods to the general public on only cash basis.

The selling price to wholesale customers is designed to give a factory profit which amounts to 30% of the sales value. The selling price to the general public is designed to give a gross margin (i.e., selling price less cost of goods from H.O.) of 30% of the sales value.

The company operates from rented premises and leases all other types of fixed assets. The rent and hire charges for these are included in the overhead costs shown in the trial balances.

From the information given below, you are required to prepare for the year end 31st December, 2002 in columnar form.

(a) A Profit & Loss account for (i) H.O. (ii) the branch (iii) the entire business.

(b) A Balance Sheet as on 31st December, 2002 for the entire business.

	H.O.		Branch	
	Rs.	**Rs.**	**Rs.**	**Rs**
Raw materials purchased	35,000			
Direct wages	1,08,500			
Factory overheads	39,000			
Stock on 1-1-2002				
Raw materials	1,800			
Finished goods	13,000		9,200	
Debtors	37,000			
Cash	22,000		1,000	
Administrative Salaries	13,900		4,000	
Salesmen's Salaries	22,500		6,200	
Other administrative & Selling overheads	12,500		2,300	
Inter-unit accounts	5,000			2,000
Capital		50,000		
Sundry Creditors		13,000		
Provision for Unrealized Profit in stock		1,200		
Sales		2,00,000		65,200
Goods sent to branch		46,000		
Goods Received from H.O.			44,500	
	3,10,200	**3,10,200**	**67,200**	**67,200**

Notes:-

(1) On 28th December, 2002 the branch remitted Rs. 1,500 to the H.O. and this has not yet been recorded in the H.O. books. Also on the same date, the H.O. dispatched goods to the branch invoiced at Rs. 1,500 and these too have not yet been entered into the branch books. It is the company's policy to adjust items in transit in the books of the recipient.

(2) The stock of raw materials held at the H.O. on 31st December, 2002 was valued at Rs. 2,300.

(3) You are advised that:

(a) There were no stock losses incurred at the H.O. or at the branch.

(b) It is the company's practice to value finished goods stock at the H.O. at factory cost.

(c) There was no opening or closing stock of work-in-progress.

(4) Branch employees are entitled to a bonus of Rs. 156 under a bilateral agreement.

Solution: **In the books of KP**

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

	H.O. ₹	Branch ₹	Total ₹		H.O. ₹	Branch ₹	Total ₹
To Opening stock of finished goods	13,000	9,200	22,200	By Sales	2,00,000	65,200	2,65,200
To Material consumed (W.N.1)	34,500	-	34,500				
To Wages	1,08,500	-	1,08,500	By Goods Sent to Branch	46,000	-	-
To Factory Overheads	39,000	-	39,000				
To Goods from H.O.		46,000		By Closing stock including transit (W.N.2)	15,000	9,560 (Bal Fig)	24,560
To Gross Profit c/d (W.N.3)	66,000 (Bal Fig)	19,560	85,560				
	2,61,000	74,760	2,89,760		2,61,000	74,760	2,89,760
To Admn. Salaries	13,900	4,000	17,900	By Gross Profit b/d	66,000	19,560	85,560
To Salesmen Salaries	22,500	6,200	28,700				
To Other Admn. & selling Overheads	12,500	2,300	14,800				
To Stock Reserve (W.N.4)	47	-	47				
To Bonus to Staff	-	156	156				
To Net Profit	17,053	6,904	23,957				
	66,000	19,560	85,560		66,000	19,560	85,560

Balance Sheet as on 31st Dec., 20X1

		₹	H.O. ₹	Branch ₹	Total ₹		H.O. ₹	Branch ₹	Total ₹
Capital			50,000	-	50,000	Fixed Assets	-	-	-
Profit:	H.O.	17,053				Current Assets:			
	Branch	6,904	23,957		23,957	Raw material	2,300		2,300
Trade Creditors			13,000		13,000	Finished Goods	15,000	9,560	23,313*
Bonus Payable				156	156	(Less Stock Res.)			
H.O. Account*				10,404		Debtors	37,000	-	37,000
Stock Reserve (W.N.4)			1,247			Cash (including transit item)	23,500	1,000	24,500
						Branch A/c	10,404**		
			88,204	10,560	87,113		88,204	10,560	87,113

*9,560 × 100/115 i.e., (8,313 + 15,000) = ₹ 23,313 or (15,000 + 9,560) – 1,247 (Stock reserve)

** (5,000 + 6,904) – 1500 = ₹ 10,404.

Working Notes:

(1) Material consumed

Opening raw material + Raw Material Purchased – Closing raw material

= 1,800 + 35,000 - 2,300 = 34,500

(2) Closing stock at head office

(a) Calculation of total factory cost = Material consumed + Wages + Factory overhead

= 34,500 + 1,08,500 + 39,000 = 1,82,000

(b) Cost (factory cost) of goods sold = Sales – Gross profit

= 2,00,000 – 2,00,000 x 30% = 1,40,000

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

(d) Closing stock = 13,000 (Opening Stock) + 1,82,000 – 1,40,000 – 40,000 = 15,000

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

= 65,200 x 30% = 19,560

(4) **Closing stock reserve** = 9,560 x 15/115 = 1,247

Charge to profit and loss = 1,247 – 1,200 (existing) = 47

2. On 31st March, 2000 Kanpur Branch submits the following Trial Balance to its Head Office at Lucknow:

Debit Balance	**Rs. In Lacs**
Furniture and equipment	18
Depreciation of Furniture	2
Salaries	25
Rent	10
Advertising	6
Telephone, Postage and Stationery	3
Sundry Office expenses	1
Stock on 1st April, 1999	60
Goods Received from Head Office	288
Debtors	20
Cash at Bank and in hand	8
Carriage Inwards	7
	448
Credit Balance	
Outstanding Expenses	3
Good Returned to Head Office	5
Sales	360
Head Office	80
	448

Additional Information:

Stock on 31st March, 2000 was valued at Rs. 62 lacs on 29th March, 2000. The Head Office dispatched goods costing Rs. 10 lacs to its branch. Branch did not receive these before 1st April, 2000.

Hence the figure of goods received from head office does not include these goods, Also the head office has charged the branch Rs, 1 lac for centralized services for which the branch has not passed the entry.

You are required to:

1. Pass Journal Entries in the books of the Branch to make the necessary adjustments.
2. Prepare Final Accounts of the Branch including Balance Sheet, and
3. Pass Journal Entries in the books of the Head Office to incorporate the whole of the Branch Trial balance.

Solution:

(i) **Books of Branch**

Journal Entries ***(₹ in lacs)***

		Dr.	**Cr.**
Goods in Transit A/c	Dr.	10	
To Head Office A/c			10

(Goods dispatched by head office but not receivedby branch before 1st April, 20X2)			
Expenses A/c	Dr.	1	
To Head Office A/c			1
(Amount charged by head office for centralised services)			

(ii) Trading and Profit & Loss Account of the Branch for the year ended 31st March, 20X2

	₹ in lacs		₹ in lacs
To Opening Stock	60	By Sales	360
To Goods received from Head Office 288+10		By Closing Stock including transit	72
Less: Returns (5)	293		
To Carriage Inwards	7		
To Gross Profit c/d	72		
	432		432
To Salaries	25	By Gross Profitb/d	72
To Depreciation on Furniture	2		
To Rent	10		
To Advertising	6		
To Telephone, Postage &Stationery	3		
To Sundry Office Expenses	1		
To Head Office Expenses (centralised services)	1		
To Net Profit Transferred to Head Office A/c	24		
	72		72

Balance Sheet as on 31st March, 20X2

Liabilities	***₹ in lacs***		***Assets***	***₹ in lacs***	
Head Office	80		Furniture & Equipment	20	
Add: Goods in transit	10		*Less:* Depreciation	(2)	18
Head Office Expenses	1		Stock in hand		62
Net Profit	24	115	Goods in Transit		10
Outstanding Expenses		3	Debtors		20
			Cash at bank and inhand		8
		118			118

(iii) Books of Head Office

Journal Entries

		Dr. (₹)	***Cr. (₹)***
Branch Trading Account	Dr.	365	
To Branch Account			365
(The total of the following items in branch trial balancedebited to branch trading account: ₹ in lacs			
Opening Stock 60			

Goods received from Head Office	288			
Goods purchased but not received	10			
Carriage Inwards	7)			
Branch Account		Dr.	437	
To Branch Trading Account				437
(Total sales, closing stock and goods returned to Head Office credited to branch trading account, individual amount being as follows:				
	₹ in lacs			
Sales	360			
Closing Stock	62			
Goods in transit	10			
Goods returned to Head Office	5)			
Branch Trading Account		Dr.	72	
To Branch Profit and Loss Account				72
(Gross profit earned by branch credited to Branch Profit&Loss A/c)				
Branch Profit and Loss Account		Dr.	48	
To Branch Account				48
(Total of the following branch expenses debited to Branch P & L A/c:				
	₹ in lacs			
Salaries	25			
Rent	10			
Advertising	6			
Telephone, Postage & Stationery	3			
Sundry Office Expenses	1			
Head Office Expenses	1			
Depreciation on furniture	2)			
Branch Profit & Loss Account		Dr.	24	
To Profit and Loss Account				24
(Net profit at branch credited to general Profit & LossA/c)				
Branch Furniture & Equipment		Dr.	18	
Branch Stock		Dr.	62	
Branch Debtors		Dr.	20	
Branch Cash at Bank and in Hand		Dr.	8	
Goods in Transit		Dr.	10	
To Branch				118
(Incorporation of different assets at the branch in H.O.books)				
Branch		Dr.	3	
To Branch Outstanding Expenses				3
(Incorporation of Branch Outstanding Expenses in H.O.books)				

3. Pass necessary journal entries in the books of Independent Branch of a company, wherever required, to rectify or adjust the following;

(i) Income of Rs 2,800 allocated to the Branch by Head Office but not recorded in the Branch books.

(ii) Provision for doubtful debts, whose are kept by the Head Office, not provided earlier for Rs 1,000.

(iii) Branch Paid Rs 3,000 as salary to a Head Office Manager, but the amount paid has been debited by Branch to Salaries Account.

(iv) Branch incurred travelling expenses of Rs 5,000 on behalf of other Branches, but not recorded in the books of Branch.

(v) A remittance of Rs.1, 50,000 sent by the Branch has not received by Head Office on the date of reconciliation of Accounts.

(vi) Head Office allocates Rs 75,000 to the Branch as Head Office expenses, which has not yet been recorded by the Branch.

(vii) Head Office collected Rs 30,000 directly from Branch Customer. The intimation of the facts has been received by the Branch till now.

(viii) Goods dispatched by the Head Office amounting to Rs 10,000, but not received by the Branch till date of reconciliation. The Goods have been received subsequently.

Solution: **Books of Branch**

Journal Entries

	Particulars		*Amount in* ***Rs.*** Dr.	Cr.
(i)	Head Office Account To Income Account A/c (Being the income allocated by the Head office not recorded earlier, now recorded)	Dr.	2,800	2,800
(ii)	Provision for Doubtful Debts A/c To Head Office Account (Being the provision for doubtful debts not provided earlier, now provided for)	Dr.	1,000	1,000
(iii)	Head Office Account To Salaries Account (Being rectification of salary paid on behalf of Head Office)	Dr.	3,000	3,000
(iv)	Head Office Account To Cash Account (Being expenditure incurred on account of other branch, now recorded in books)	Dr.	5,000	5,000
(v)	No entry in Branch Books is required.			
(vi)	Expenses Account To Head Office Account (Being allocated expenses of Head Office recorded)	Dr.	75,000	75,000
(vii)	Head Office Account To Debtors Account (Being adjustment entry for collection from Branch Debtors directly by Head Office)	Dr.	30,000	30,000
(viii)	Goods –in- transit Account To Head Office Account (Being goods sent by Head Office still in-transit)	Dr.	10,000	10,000

4. AFFIX Ltd. of Calcutta has a branch at Delhi to which the goods are supplied from Calcutta but the cost thereof is not recorded in the Head Office books. On 31st March, 2006 the Branch Balance Sheet was as follows:

Liabilities	*Rs.*	*Assets*	*Rs.*
Creditors Balance	40,000	Debtors Balance	2,00,000
Head Office	1,68,000	Building Extension A/c closed by transfer to H.O. A/c	
		Cash at Bank	8,000
	2,08,000		2,08,000

During the six months ending on 30-9-2006, the following transactions took place at Delhi.

	Rs.		*Rs.*
Sales	2,40,000	Manager's Salary	4,800
Purchases	48,000	Collections from Debtors	1,60,000
Wages paid	20,000	Discounts allowed	8,000
Salaries (inclusive of advance of Rs. 2,000)	6,400	Discount earned	1,200
		Cash paid to Creditors	60,000
General Expenses	1,600	Building Account (further payment)	4,000
Fire Insurance (paid for one year)	3,200	Cash in Hand	1,600
Remittance to H.O.	38,400	Cash at Bank	28,000

Set out the Head Office Account in Delhi books and the Branch Balance Sheet as on 30-9-2006. Also give journal entries in the Delhi books.

Solution: **Journal Entries**

2012		Dr.	Cr.
30 Sept.		Rs.	Rs.
(i) Salary Advance A/c	Dr.	2,000	
To Salaries A/c			2,000
(The amount paid as advance adjusted by debit to Salary Advance A/c)			
(ii) Prepared Insurance A/c	Dr.	1,600	
To Fire Insurance A/c			1,600
(Six months premium transferred to the Prepaid Insurance A/c)			
(iii) Head Office Account Dr.		88,400	
To Purchases A/c			48,000
To Wages A/c			20,000
To Salaries A/c			4,400
To General Expenses A/c			1,600
To Fire Insurance A/c			1,600
To Manager's Salary A/c			4,800
To Discount Allowed A/c			8,000
(Transfer of various revenue accounts (Dr.) to the H.O. Account for closing the accounts)			
(iv) Sales Accounts Dr.		2,40,000	
Discount Earned A/c Dr.		1,200	
To Head Office A/c			2,41,200
[Revenue accounts (Cr.) transferred to H.O.]			
(v) Head Office Account Dr.		4,000	
To Building Account			4,000
(Transfer of amounts spent on building extension to H.O. A/c)			

Head Office Account

2012		Rs.	2012		Rs.
Sep. 30	To Cash-remittance	38,400	April 1	By Balance b/d	1,68,000
	To Sundries (Revenue A/cs)	88,400	Sep. 30	By Sundries (Revenue A/cs)	2,41,200
	To Building A/c	4,000			
	To Balanced c/d	2,78,400			
		4,09,200			4,09,200

Balance Sheet of Delhi Branch as on Sept. 30, 2012

Liabilities	**Rs.**	**Assets**	**Rs.**
Creditors Balances	26,800	Debtors Balances	2,72,000
Head Office Account	2,78,400	Salary Advance	2,000
		Prepaid Insurance	1,600
		Building Extension A/c transferred to H.O.	—
		Cash in Hand	1,600
		Cash at Bank	28,000
	3,05,200		3,05,200

Cash and Bank Account

	Rs.			**Rs.**
To Balance b/d	8,000	By Wages		20,000
To Collection from Debtors	1,60,000	By Salaries		6,400
		By Insurance		3,200
		By General Exp.		1,600
		By H.O. A/c		38,400
		By Manager's Salary		4,800
		By Creditors		60,000
		By Building A/c		4,000
		By Balance c/d		
		Cash in Hand	1,600	
		Cash at Bank	28,000	29,600
	1,68,000			1,68,000

Debtors Account

	Rs.		Rs.
To Balance b/d	2,00,000	By Cash Collection	1,60,000
To Sales	2,40,000	By Discount (allowed)	8,000
By Balance c/d	2,72,000		
	4,40,000		4,40,000

Creditors Account

	Rs.		Rs.
To Cash	60,000	By Balance b/d	40,000
To Discount (earned)	1,200	By Purchases	48,000
To Balance c/d	26,800		
	88,000		88,000

5. M/s Rani & Co. has head office at Singapore and branch at Delhi (India). Delhi Branch is an Integral foreign operation of M/s Rani & Co. Delhi branch furnishes you with its trial balance as on 31st March, 2019 and the additional information given thereafter:

	Dr. (Rs. '000)	Cr. (Rs. '000)
Stock on 1st April, 2018	600	
Purchases and sales	1,600	2,400
Sundry debtors and creditors	800	600
Bills of exchange	240	480
Wages and salaries	1,120	
Rent, rates and taxes	720	
Sundry charges	320	
Computers	600	
Bank balance	520	
Singapore office A/c		3,040
	6,520	**6,520**

Additional information:

(a) Computers were acquired from a remittance of Singapore Dollar 12,000 received from Singapore head office and paid to the suppliers. Depreciate computers at the rate of 40% for the year.
(b) Closing stock of Delhi branch was Rs. 15,60,000, on 31st March, 2019.
(c) The rates of exchange may be taken as follows:
(i) On 1.4.2018@ Rs. 50 per Singapore Dollar
(ii) On 31.3.2019 @ Rs. 52 per Singapore Dollar
(iii) Average exchange rate for the year @ Rs. 51 per Singapore Dollar
(iv) Conversion in Singapore Dollar shall be made upto two decimal accuracy.
(d) Delhi branch account showed a debit balance of Singapore Dollar 59,897.43 on 31-3-2019 in the Head office books and there were no items pending for reconciliation.

In the Books of Head Office, you are required to prepare:
(i) Revenue statement for the year ended 31st March, 20019 (in Singapore Dollar)
(ii) Balance Sheet as on that date. (in Singapore Dollar)

Solution:

Books of Head Office

(i) Trading and P & L A/c/(Revenue statement) for the year ended 31st March, 20019

Particulars	Amount	Particulars	Amount
To opening Stock	12,000.00	By Sales	47,058.82
To Purchases	31,372.55	By Closing Stock	30,000.00
To Wages and Salaries	21,960.78	(15,60,000/52)	
To Gross Profit c/d	11,725.49		
	77,058.82		**77,058.82**
To Rent, rates and taxes	14,117.65	By Gross Profit b/d	11,725.49
To Sundry charges	6,274.51	By Net Loss c/d	13,466.67
To Depreciation on Computers	4,800.00		
	25,192.16		**25,192.16**

(ii) Balance Sheet as at 31-03-2019

Liabilities		Amount	Assets	Amount
Singapore office A/c	59,897.43		Computers	7,200.00
Less: Net Loss	**(13,466.67)**	46,430.76	Stock	30,000.00
Creditors		11,538.46	Debtors	15,384.61
B/P		9,230.77	B/R	4,615.38
			Bank balance	10,000.00
		67,199.99		**67,199.99**

Working Note:

Converted Trial Balance

Particulars	₹ '000'		Conversion rate	Singapore Dollar	
	Dr.	Cr.		Dr.	Cr.
Stock on 1st April, 2018	600	-	1/50	12,000.00	-
Purchases and sales	1,600	2,400	1/51	31,372.55	47,058.82
Sundry debtors and creditors	800	600	1/52	15,384.61	11,538.46
Bills of exchange	240	480	1/52	4,615.38	9,230.77
Wages and salaries	1,120	-	1/51	21,960.78	-
Rent, rates and taxes	720	-	1/51	14,117.65	-
Sundry charges	320	-	1/51	6,274.51	-
Depreciation on Computers (600 X 40%)	240		12,000 X 40%	4,800.00	-
Computers (600 – 240)	360	-	12,000 - 4,800	7,200.00	-
Bank balance	520	-	1/52	10,000.00	-
Singapore office A/c	-	3,040	H.O. Books	-	59,897.43
Total	6,520	6,520		1,27,725.48	1,27,725.48

6. An Indian company Moon Star Ltd. has a branch at Verginia (USA). The Branch is a non–integral foreign operation of the Indian Company. The trial Balance of the Branch as at 31th March, 2012 is as follows:

	Dr.	Cr.
Office equipments	48,000	
Furniture and fixtures	3,200	
Stock,(April 1, 2011)	22,400	
Purchases	96,000	
Sales		1,66,400
Goods Sent from (H.O)	32,000	
Salaries	3,200	
Carriage inward	400	
Rent, rates and taxes	800	
Insurance	400	
Trade expenses	400	
Head Office A/c		45,600
Sundry debtors	9,600	
Sundry creditors		6,800
Cash at bank	2,000	
Cash at hand	400	
US $	**2,18,800**	**2,18,800**

The following further information's are given:
(1) Salaries outstanding-$ 400.
(2) Depreciate Office equipment and Furniture and Fixtures @ 10% p.a. at written down value.
(3) The Head Office sent goods to Branch for Rs. 15,80,000.
(4) The Head Office shown an amount of Rs. 20,50,000 due from Branch.
(5) Stock on 31th March, 2013 - $ 21,500
(6) There were no transit items either at the start or at the end of the year.
(7) On April 1,2010 when the fixed assets were purchased the rate of exchange was Rs.43 to one $. On April1, 2011, the rate was Rs. 47 per $. On March 31, 2012 the rate was Rs. 50 per $. Average Rate during the year was Rs.45 to one $.

Prepare:
(a) Trial balance incorporating adjustments given converting dollars into rupees.
(b) Trading, Profit and Loss Account for the year ended 31st March,2012 and Balance Sheet as on date depicting and net position of the Branch as would appear in the books of Indian company for the purpose of incorporating in the main Balance Sheet.

Solution: **In the books of Moon Star**

Trial Balance (in Rupees) of Verginia (USA) Branch as on 31st March, 2012

	Dr.	Cr.	Conversion	Dr.	Cr.
	US $	US $	rate	Rs.	Rs.
Office Equipment	43,200		50	21,60,000	
Depreciation on Office Equipment	4,800		50	2,40,000	
Furniture and fixtures	2,880		50	1,44,000	
Depreciation on furniture and fixtures	320		50	16,000	
Stock (1st April, 2011)	22,400		47	10,52,800	
Purchases	96,000		45	43,20,000	
Sales		1,66,400	45		74,88,000
Good sent from H.O.	32,000			15,80,000	
Carriage inward	400		45	18,000	
Salaries (3,200 + 400)	3,600		45	1,62,000	
Outstanding salaries		400	50		20,000
Rent, rate and taxes	800		45	36,000	
Insurance	400		45	18,000	
Trade expenses	400		45	18,000	
Head Office A/c		45,600			20,50,000
Trade debtors	9,600		50	4,80,000	
Trade creditors		6,800	50		3,40,000

Cash and bank	2,000		50	1,00,000	
Cash in hand	400		50	20,000	
Exchange gain (bal. fig.)					4,66,800
	2,19,200	2,19,200		1,03,64,800	1.03,64,800

(b) **Trading and Profit and Loss Account of Verginia Branch for the year ended 31st March, 2012**

	Rs.		Rs.
To Opening stock	10, 52,800	By Sales	74, 88,000
To Purchases	43, 20,000	By Closing stock	10, 75,000
To Goods from Head Office	15, 80,000	(21,500 US $ × 50)	
To Carriage inward	18,000		
To Gross profit c/d	15, 92,200		
	85, 63,000		85, 63,000
To Salaries	1, 62,000	By Gross profit b/d	15, 92,200
To Rent, rates and taxes	36,000		
To Insurance	18,000		
To Trade expenses	18,000		
To Depreciation on office equipment	2, 40,000		
To Depreciation on furniture and fixtures	16,000		
To Net Profit c/d	11, 02,200		
	15, 92,200		15,92,200

Balance Sheet of Verginia Branch as on 31st March, 2012

Liabilities	Rs.	Rs.	*Assets*	Rs.	Rs.
Head Office A/c	20, 50,000		Office Equipment	24, 00,000	
Add : Net profit	11,02,200	31,52,200	*Less* : Depreciation	(2,40,000)	21,60,000
Foreign Currency Translation Reserve		4, 66,800	Furniture and fixtures	1, 60,000	
Trade creditors	3, 40,000		*Less*: Depreciation	(16,000)	1, 44,000
Outstanding salaries		20,000	Closing stock		10, 75,000
			Trade debtors		4, 80,000
			Cash in hand		20,000
			Cash at bank		1, 00,000
		39, 79,000			39, 79,000

7. Pawan, of Delhi has a branch at Jaipur. Goods are invoiced to the branch at cost plus 25%. The branch is instructed to deposit the receipts everyday in the head office account with the bank. All the expenses are paid through cheque by the head office except petty cash expenses which are paid by the Branch.
From the following information, you are required to prepare Branch Account in the books of Head office:

	Rs.
Stock at invoice price on 1.4.2012	1,64,000
Stock at invoice price on 31.3.2013	1,92,000
Debtors as on 1.4.2012	63,400
Debtors as on 31.3.2013	84,300
Furniture & fixtures as on 1.4.2012	46,800
Cash sales	8,02,600
Credit sales	7,44,200
Goods invoiced to branch by head office	12,56,000
Expenses paid by head office	2,64,000
Petty expenses paid by the branch	20,900
Furniture acquired by the branch on 1.10.2012 (payment was made by the branch from cash sales and collection from debtor	5,000

Depreciation to be provided on branch furniture & fixtures @ 10% p.a. on WDV basis.

Solution:

In the Books of Pawan Delhi (Head Office)

Jaipur Branch Account

	Rs.		Rs.
To Opening balances:		By Branch stock reserve	32,800
Branch stock A/c	1,64,000	By Bank A/c (W.N.4)	15,00,000
Branch debtors A/c	63,400	By Goods sent to branch A/c (Loading)	2,51,200
Branch furniture A/c	46,800		
To Goods sent to branch	12,56,000	By Closing Balance:	
To Bank A/c (branch expenses)	2,64,000	Branch stock A/c	1,92,000
To Branch stock reserve A/c	38,400	Branch debtors A/c	84,300
To Profit and loss A/c (Bal.Fig.)	2,74,570	Branch furniture A/c (W.N.2)	46,870
	21,07,170		21,07,170

Working Notes:

1. Depreciation on furniture

	Rs.
10% p.a. on ,46, 800	4,680
10% p.a. for 6 months on ,5, 000	250
	4,930

2. Closing balance of branch furniture as on 31.3.2013

	Rs.
Branch furniture as on 1.4.2012	46,800
Add: Acquired during the year	5,000
	51,800
Less: Depreciation (W.N.1)	(4,930)
Branch furniture as on 31.3.2013	46,870

3. Collection from branch debtors

Branch Debtors Account

	Rs.		Rs.
To Balance b/d	63,400	By Bank A/c (Bal.Fig.)	7,23,300
To Sales	7.44,200	By Balance c/d	84,300
	8,07,600		8,07,600

4. Cash remitted by the branch to head office

Cash sales + Collection from debtors – Petty expenses – Furniture acquired by branch

Rs. 8,02,600 + Rs. 7,23,300 (W.N. 3) – Rs. 20,900 – Rs. 5,000 = Rs. 15,00,000

8. M/s Marena, Delhi has a branch at Bangalore to which office goods are invoiced at cost plus 25%. The branch sells both for cash and on credit. Branch Expenses are paid direct from head office and the Branch has to remit all cash received into the Head Office Bank Account.

From the following details, relating to calendar year 20X1, prepare the accounts in the Head Office Ledger and ascertain the Branch Profit under Stock and Debtors Method'.

Branch does not maintain any books of account, but sends weekly returns to the Head Office.

		₹
Goods received from Head Office at invoice price		45,00,000
Returns to Heads Office at invoice price		90,000
Stock at Bangalore as on 1st January, 20X1		4,50,000
Sales during the year	– Cash	15,00,000
	- Credit	27,00,000
Sundry Debtors at Bangalore as on 1st January, 20X1		5,40,000
Cash received from Debtors		24,00,000
Discount allowed to Debtors		45,000
Bad Debts in the year		30,000
Sales returns at Bangalore Branch		60,000
Rent, Rates and Taxes at Branch		1,35,000
Salaries, Wages and Bonus at Branch		4,50,000
Office Expenses		45,000
Stock at Branch on 31st December, 20X1 at invoice price		9,00,000

Solution: **Bangalore Branch Stock Account**

Particulars	Amount (₹)	Particulars	Amount (₹)
To Balance b/d	4,50,000	By Goods sent to branch A/c (Returns)	90,000
To Goods sent to branch A/c	45,00,000	By Bank A/c (Cash sales)	15,00,000
To Branch debtors A/c (Returns)	60,000	By Branch debtors A/c (credit sales)	27,00,000
To Branch adjustment A/c (Surplus over invoice price)*	1,80,000	By Balance c/d	9,00,000
	51,90,000		51,90,000

***Alternatively, this may directly be transferred to Branch P&L A/c without routing it through Branch Adjustment Account.**

Bangalore Branch Adjustment Account

Particulars	Amount (₹)	Particulars	Amount (₹)
To Stock reserve - 20% of ₹ 9,00,000 (closing stock)	1,80,000	By Stock reserve - 20% of ₹ 4,50,000 (Opening stock)	90,000
To Branch profit & loss A/c (Gross profit)	9,72,000	By Goods sent to branch A/c – 20% of ₹ 44,10,000 (45,00,000 – 90,000)	8,82,000
		By Branch stock A/c	1,80,000
	11,52,000		11,52,000

Branch Profit & Loss Account

Particulars	Amount (₹)	Particulars	Amount (₹)
To Branch expenses A/c	6,30,000	By Branch adjustment A/c (Gross Profit)	9,72,000
To Branch debtors A/c (Discount)	45,000		
To Branch Debtors A/c (Bad debts)	30,000		
To Net profit (transferred to Profit & Loss A/c)	2,67,000		
	9,72,000		9,72,000

Branch Expenses Account

Particulars	Amount (₹)	Particulars	Amount (₹)
To Bank A/c (Rent, rates & taxes)	1,35,000	By Branch profit and loss A/c (Transfer)	6,30,000
To Bank A/c (Salaries, wages & bonus)	4,50,000		

To Bank A/c (Office expenses)	45,000		
	6,30,000		6,30,000

Branch Debtors Account

Particulars	***Amount (₹)***	***Particulars***	***Amount (₹)***
To Balance b/d	5,40,000	By Bank A/c	24,00,000
To Branch stock A/c	27,00,000	By Branch profit and loss A/c (Bad debts and discount)	75,000
		By Branch stock A/c (Sales returns)	60,000
		By Balance c/d (bal. fig.)	7,05,000
	32,40,000		32,40,000

Goods sent to Branch Account

Particulars	***Amount (₹)***	***Particulars***	***Amount (₹)***
To Branch stock A/c	90,000	By Branch stock A/c	45,00,000
To Branch adjustment A/c	8,82,000		
To Purchases A/c	35,28,000		
	45,00,000		45,00,000

9. From the following details of Western Branch Office of M/s. Alpha for the year ending 31st March, 2020, ascertain branch stock reserve in respect of unrealized profit in opening stock and closing stock:

(i) Goods are sent to the branch at invoice price and branch also maintains stock at the same price.

(ii) Sale price is cost plus 40%.

(iii) Invoice price is cost plus 15%.

(iv) Other information from accounts of branch:

Opening Stock as on 01-04-2019	3,45,000
Goods sent during the year by Head Office to Branch	16,10,000
Sales during the year	21,00,000
Expenses incurred at the branch	45,000

(MTP I Dec 21)

Solution: Branch Stock Reserve in respect of unrealized profit

On opening stock = ₹ 3,45,000 x (15/115) = ₹ 45,000

On closing stock = ₹ 2,30,000 x (15/115) = ₹ 30,000

Working Note:

	₹
Cost Price	100
Invoice Price	115
Sale Price	140
Calculation of closing stock at invoice price	**₹**
Opening stock at invoice price	3,45,000
Goods received during the year at invoice price	16,10,000
	19,55,000
Less: Cost of goods sold at invoice price [21,00,000 X (115/140)]	(17,25,000)
Closing stock	2,30,000

10. Following is the information of the Jammu branch of Best Ltd., New Delhi for the year ending 31st March, 2010 from the following:

(1) Goods are invoiced to the branch at cost plus 20%.
(2) The sale price is cost plus 50%.
(3) Other information:-

Stock as on 01.04.2009	2,20,000
Goods sent during the year	11,00,000
Sales during the year	12,00,000
Expenses incurred at the branch	45,000

Ascertain:-

(i) The profit earned by the branch during the year.
(ii) Branch stock reserve in respect of unrealized profit.

Solution:

(i) Calculation of profit earned by the branch In the books of Jammu Branch

Trading Account and Profit and Loss Account

Particulars	***Amount***	***Particulars***	***Amount***
To Opening stock	2,20,000	By Sales	12,00,000
To Goods received byHead office	11,00,000	By Closing stock (Refer W.N.)	3,60,000
To Expenses	45,000		
To Net profit (Bal fig)	1,95,000		
	15,60,000		15,60,000

(ii) Stock reserve in respect of unrealised profit

= ₹ 3,60,000 x (20/120) = ₹ 60,000

Working Note:

	₹	
Cost Price	100	
Invoice Price	120	
Sale Price	150	
Calculation of closing stock at invoiceprice	**₹**	
Opening stock at invoice price	2,20,000	
Goods received during the year at invoiceprice	11,00,000	
	13,20,000	
Less: Cost of goods sold at invoice price	(9,60,000)	[12,00,000 x (120/150)]
Closing stock	3,60,000	

11. Arnold Ltd. Delhi, trades in Ghee and Oil. It has a branch at Lucknow. The company despatches 25 tins of Oil @ Rs. 1,000 per tin and 15 tins of Ghee @ Rs. 1,500 per tin on 1st of every month. The branch incurs some expenditure which is met out of its collections; this is in addition to expenditure directly paid by Head Office.

Following are the other details:

		Delhi Rs.	Lucknow Rs.
Purchases	Ghee	14,75,000	-
	Oil	29,32,000	-
Direct expenses		3,83,275	-
Expenses paid by H.O.		-	14,250
Sales	Ghee	18,46,350	3,42,750
	Oil	27,41,250	3,15,730
Collection during the year (including Cash Sales)		-	6,47,330
Remittance by Branch to Head Office		-	6,13,250

(Delhi)

Balance as on:	1-1-2005	31-12-2005
Stock : Ghee	1,50,000	3,12,500
Oil	3,50,000	4,17,250
Debtors	7,32,750	-
Cash on Hand	70,520	55,250
Furniture & Fittings	21,500	19,350
Plant/Machinery	3,07,250	7,73,500

(Lucknow)

Balance as on:	**1-1-2005**	**31-12-2005**
Stock : Ghee	17,000	13,250
Oil	27,000	44,750
Debtors	75,750	-
Cash on Hand	7,540	12,350
Furniture & Fittings	6,250	5,625
Plant/Machinery	-	-

Addition to Plant/Machinery on 1-1-2005 Rs. 6,02,750.
Rate of Depreciation: Furniture / Fittings @ 10% and Plant / Machinery @ 15% (already adjusted in the above figures).
The Branch Manager is entitled to 10% commission after charging such commission whereas, the General Manager is entitled to 10% commission on overall company profits after charging such commission. General Manager is also entitled to a salary of Rs. 2000 p.m. General expenses incurred by H.O. Rs. 24,000.
Prepare Branch Account in the head office books and also prepare the company's Trading and Profit and Loss A/c (excluding branch transactions).

Solution:

In the books of Arnold
Lucknow Branch Account

	Rs.		Rs.
To Balance b/d		By Bank (Remittance to H.O.)	6,13,250
Opening stock:		By Balance c/d	
Ghee	17,000	Closing stock:	
Oil	27,000	Ghee	13,250
Debtors	75,750	Oil	44,750
Cash on hand	7,540	Debtors (W.N. 1)	86,900
Furniture & fittings		Cash on hand (W.N. 2)	12,350
To Goods sent to Branch A/c		Furniture & fittings	5,625
Ghee	2,70,000		
Oil	3,00,000		
To Bank (Expenses paid by H.O.) (Rs. 58,335 × 1/11)	5,303		
To Net Profit transferred to General P & L A/c	53,032		
	7,76,125		7,76,125

Trading and Profit and Loss account for the year ended 31st December, 2012
(Excluding branch transactions)

	Rs.		Rs.
To Opening Stock:		By Sales:	
Ghee	1,50,000	Ghee	18,46,350
Oil	3,50,000	Oil	27,41,250
To Purchases:			
Ghee 14,75,000			
Less: Goods sent to Branch (2,70,000)	12,05,000		
Oil 29,32,000			
Less: Goods sent to Branch (3,00,000)	26,32,000		
To Direct Expenses	3,83,275		
To Gross Profit	5,97,075		
	53,17,350		53,17,350
To Manager's Salary	24,000	By Gross Profit	5,97,075
To General Expenses	24,000	By Branch Profit transferred	53,032
To Depreciation			
Furniture @ 10% 2,150			
Plant & Machinery @ 15% 1,36,500 (W. N. 3)	1,38,650		
To General Manager's Commission @ 10% (*i.e.*, 4,63,457 × 1/11)	42,132		
	4,21,325		
To Net profit	6,50,107		6,50,107

Working Notes:

(1) Debtors Account

	Rs.		Rs.
To Balance b/d	75,750	By Cash Collections	6,47,330
To Sales made during the year:		By Balance c/d	86,900
Ghee	3,42,750		
Oil	3,15,730		
	7,34,230		7,34,230

(2) Branch Cash Account

	Rs.		Rs.
To Balance b/d	7,540	By Remittance	6,13,250
To Collections	6,47,330	By Exp. (Balance fig.)	29,270
		By Balance c/d	12,350
	6,54,870		6,54,870

(3) Depreciation on Plant & Machinery = 3,07,250 x 15% + 6,02,750 x 15%

INTERNAL RECONSTRUCTION

1. M/s Platinum Limited has decided to reconstruct the Balance Sheet since it has accumulated huge losses. The following is the Balance Sheet of the company as on 31st March, 2012 before reconstruction:

Liabilities	Amount (Rs.)	Assets	Amount (Rs.)
Share Capital		Goodwill	22,00,000
50,000 shares of Rs. 50 each fully paid up	25,00,000		
1,00,000 shares of Rs.50 each Rs.40 paid up	40,00,000	Land and building	42,70,000
Capital Reserve	5,00,000	Machinery	8,50,000
8% Debentures of Rs.100 each	4,00,000	Computers	5,20,000
12% Debentures of Rs.100 each	6,00,000	Stock	3,20,000
Trade Creditors	12,40,000	Trade Debtors	10,90,000
Outstanding expenses	10,60,000	Cash at Bank	2,68,000
		Profit and Loss account	7,82,000
Total	1,03,00,000	Total	1,03,00,000

Following is the interest of Mr. Shiv and Mr. Ganesh in M/s Platinum Linited:

	Mr. Shiv	**Mr. Ganesh**
8% Debentures	3,00,000	1,00,000
12% Debentures	4,00,000	2,00,000
Total	**7,00,000**	**3,00,000**

The following scheme of internal reconstruction was framed and implemented, as approved by the court and concerned parties:

(1) Uncalled capital is to be called up in full and then all the shares to be converted into Equity Shares of Rs. 40 each.

(2) The existing shareholders agree to subscribe in cash, fully paid up equity shares of Rs. 40 each for Rs. 12,50,000.

(3) Trade creditors are given option of either to accept fully paid equity shares of Rs. 40 each for the amount due to them or to accept 70% of the amount due to them in cash in fully settlement of their claim. Tread Creditors for Rs. 7,50,000 accept equity shares and rest of them opted for cash towards full and final settlement of their claim.

(4) Mr. Shiv agrees to cancel debenture amounting to Rs.2.00,000 out of total debenture due to him and agree to 15% Debenture for the balance amount due. He also agree to subscribe further 15% Debenture in cash amounting to Rs.1,00,000.

(5) Mr. Ganesh agree to cancel debenture amounting to Rs. 50,000 out of total debenture due to him and agree to accept 15% Debenture for the balance amount due.

(6) Land and Building to be revalued at Rs. 51,84,000, Machinery at Rs. 7,20,000, Computers at Rs. 4,00,000, Stock at Rs. 3,50,000 and Tread Debtors at 10% less to as they are appearing in Balance Sheet as above.

(7) Outstanding Expenses are fully paid in cash.

(8) Goodwill and Profit and Loss A/c will be written off and balance, if any, of Capital Reduction A/c will be adjusted against Capital Reserve.

You are required to pass necessary Journal Entries for all the above transactions and draft the company's Balance Sheet immediately after the reconstruction.

Solution: **Journal Entries**

1.	Equity Share final call A/c	Dr.	10,00,000	
	To Equity Share Capital A/c			10,00,000
	(Being final call made for ₹10 each on 1,00,000 shares)			
2.	Bank A/c	Dr.	10,00,000	
	To Equity Share final call A/c			10,00,000
	(Being money on final call received)			
3.	Equity share capital (₹ 50) A/c	Dr.	75,00,000	
	To Equity Share Capital (₹40) A/c			60,00,000
	To Capital Reduction A/c			15,00,000
	(Being conversion of equity share capital of ₹50 each into ₹40 each as per reconstruction scheme)			
4.	Bank A/c	Dr.	12,50,000	
	To Equity Share Capital A/c			12,50,000
	(Being new shares allotted at ₹40 each)			
5.	Trade Creditors A/c	Dr.	12,40,000	
	To Equity Share Capital A/c			7,50,000
	To Bank A/c			3,43,000
	To Capital Reduction A/c			1,47,000
	(Being payment made to creditors in shares or cash to the extent of 70% as per reconstruction scheme)			
6.	8% Debentures A/c	Dr.	3,00,000	
	12% Debentures A/c	Dr.	4,00,000	
	To 15% Debentures A/c			5,00,000
	To Capital Reduction A/c			2,00,000
	(Being cancellation of 8% and 12% debentures of Shiv, & issuance of new 15% debentures and balance transferred to capital reduction account as per reconstruction scheme)			
7.	Bank A/c	Dr.	1,00,000	
	To 15% Debentures A/c			1,00,000
	(Being new debentures subscribed by Shiv)			
8.	8% Debentures A/c	Dr.	1,00,000	
	12% Debentures A/c	Dr.	2,00,000	
	To 15% Debentures A/c			2,50,000
	To Capital Reduction A/c			50,000

	(Being cancellation of 8% and 12% debentures of Ganesh, & issuance of new 15% debentures and balance transferred to capital reduction account as per reconstruction scheme)			
9.	Land and Building (51,84,000-42,70,000)	Dr.	9,14,000	
	Stock	Dr.	30,000	
	To Capital Reduction A/c			9,44,000
	(Being value of assets appreciated)			
10.	Outstanding expenses A/c	Dr.	10,60,000	
	To Bank A/c			10,60,000
	(Being outstanding expenses paid in cash)			
11.	Capital Reduction A/c	Dr.	33,41,000	
	To Machinery A/c			1,30,000
	To Computers A/c			1,20,000
	To Trade Debtors A/c			1,09,000
	To Goodwill A/c			22,00,000
	To Profit and Loss A/c			7,82,000
	(Being amount of Capital Reduction utilized in writing off P & L A/c (Dr.) balance, goodwill and downfall in value of other assets)			
12.	Capital Reserve A/c	Dr.	5,00,000	
	To Capital reduction A/c			5,00,000
	(Being debit balance of capital reduction account adjusted against capital reserve)			

Balance Sheet (as reduced) as on 31.3.2012

Particulars	Rs.
Equity and Liabilities	
Shareholders' funds	
Share capital	
2,00,000 Equity shares of ₹ 40 each	80,00,000
Non-current liabilities	
Long-term borrowings	
15% Debentures	8,50,000
Total	88,50,000
Assets	
Non-current assets	
Property, plant and equipment	
Land and Building	51,84,000
Machinery	7,20,000
Computers	4,00,000

Current assets	
Inventory	9,81,000
Trade Receivable	3,50,000
Cash and Bank (WN 1)	12,15,000
Total	88,50,000

Working Notes:

1. Cash at Bank Account

	Particulars	₹		Particulars	₹
To	Balance b/d	2,68,000	By	Trade Creditors A/c	3,43,000
To	Equity Share final call A/c	10,00,000	By	Outstanding expenses A/c	10,60,000
To	Equity Share Capital A/c	12,50,000	By	Balance c/d (bal. fig.)	12,15,000
To	15% Debentures A/c	1,00,000			
		26,18,000			26,18,000

2. Capital Reduction Account

	Particulars	₹		Particulars	₹
To	Machinery A/c	1,30,000	By	Equity Share Capital A/c	15,00,000
To	Computers A/c	1,20,000	By	Trade Creditors A/c	1,47,000
To	Trade Debtors A/c	1,09,000	By	8% and 12% Debentures A/c	2,00,000
To	Goodwill A/c	22,00,000	By	8% and 12% Debentures A/c	50,000
To	Profit and Loss A/c	7,82,000	By	Land & Building	9,14,000
			By	Stock	30,000
			By	Capital Reserve A/c	5,00,000
		33,41,000			33,41,000

2. The Balance sheet of Vaibhav Ltd. as on 31st March 2014 is as follows:

Liabilities	Rs.	Assets	Rs.
Equity Shares of Rs. 100 each	2,00,00,000	Fixed Assets	2,50,00,000
6% Cumulative Preference Shares of Rs. 100 Each	1,00,00,000	Investments (Market Value Rs. 19.00,000)	20,00,000
5% Debentures of Rs. 100 each	80,00,000	Current Assets	2,00,00,000
Sundry Creditors	1,00,00,000	P & L A/c	12,00,000
Provision for Taxation	2,00,000		
TOTAL	4,82,00,000	TOTAL	4,82,00,000

The following scheme of Internal Reconstruction is sanctioned:

(i) All the existing equity shares are reduced to Rs. 40 each .

(ii) All preference shares are reduced to Rs. 60 each.

(iii) The rate of Interest on Debentures is increased to 6%. The Debenture holders surrender their existing debentures of Rs. 100 each and exchange the same for fresh debentures of Rs. 70 each for every debenture held by them.

(iv) Fixed assets are to be written down by 20%

(v) Current assets are to be revalued at Rs. 90,00,000
(vi) Investments are to be brought to their market value.
(vii) Ones of the creditors of the company to whom the company owes Rs. 40,00,000 decides to forgo 40% of his claim. The Creditor is allotted with 60000 equity shares of Rs. 40 each in full and final settlement of his claim.
(viii) The taxation liability is to be settled at Rs. 3,00,000.
(ix) It is decided to write off the debit balance of Profit & Loss A/c.

Pass journal entries and show the Balance Sheet of the Company after giving effect to the above.

Solution:

Journal Entries in the books of Vaibhav Ltd.

		Rs.	Rs.
(i)	Equity share capital (Rs. 100) A/c Dr.	2,00,00,000	
	To Equity Share Capital (Rs. 40) A/c		80,00,000
	To Capital Reduction A/c		1,20,00,000
	(Being conversion of equity share capital of Rs. 100 each into Rs.40 each as per reconstruction scheme)		
(ii)	6% Cumulative Preference Share capital (Rs. 100) A/c Dr.	1,00,00,000	
	To 6% Cumulative Preference Share Capital (Rs. 60)A/c		60,00,000
	To Capital Reduction A/c		40,00,000
	(Being conversion of 6% cumulative preference share capital of Rs. 100 each into Rs. 60 each as per reconstruction scheme)		
(iii)	5% Debentures (Rs. 100) A/c Dr.	80,00,000	
	To 6% Debentures (Rs. 70) A/c		56,00,000
	To Capital Reduction A/c		24,00,000
	(Being 6% debentures of Rs. 70 each issued to existing 5% debenture holders. The balance transferred to capital reduction account as per reconstruction scheme)		
(iv)	Sundry Creditors A/c Dr.	40,00,000	
	To Equity Share Capital (Rs. 40) A/c		24,00,000
	To Capital Reduction A/c		16,00,000
	(Being a creditor of Rs. 40,00,000 agreed to surrender his claim by 40% and was allotted 60,000 equity shares of Rs. 40 each in full settlement of his dues as per reconstruction scheme)		
(v)	Provision for Taxation A/c Dr.	2,00,000	
	Capital Reduction A/c Dr.	1,00,000	
	To Liability for Taxation A/c		3,00,000
	(Being conversion of the provision for taxation into liability for taxation for settlement of the amount due)		
(vi)	Capital Reduction A/c Dr.	199,00,000	
	To P & L A/c		12,00,000

	To Property, Plant and Equipment A/c		50,00,000
	To Current Assets A/c		110,00,000
	To Investments A/c		1,00,000
	To Capital Reserve A/c (Bal. fig.)		26,00,000
	(Being amount of Capital Reduction utilized in writing off P & L A/c (Dr.) Balance, PPE, Current Assets, Investments and the Balance transferred to Capital Reserve)		
(vii)	Liability for Taxation A/c Dr.	3,00,000	
	To Current Assets (Bank A/c)		3,00,000
	(Being the payment of tax liability)		

Balance Sheet of Vaibhav Ltd. (and reduced) as at 31st March, 20X1

Particulars	Notes	Rs.
Equity and Liabilities		
Shareholders' funds		
Share capital	1	164,00,000
Reserves and Surplus	2	26,00,000
Non-current liabilities		
Long-term borrowings	3	56,00,000
Current liabilities		
Trade Payables (1,00,00,000 less 40,00,000)		60,00,000
Total		3,06,00,000
Assets		
Non-current assets		
Property, plant and equipment	4	2,00,00,000
Investments	5	19,00,000
Current assets	6	87,00,000
Total		3,06,00,000

Notes to accounts

		Rs.
1. Share Capital **Equity share capital** **Issued, subscribed and paid up** 2,60,000 equity shares of Rs. 40 each (of the above 60,000 shares have been issued for consideration other than cash)		1,04,00,000

	Preference share capital		
	Issued, subscribed and paid up		
	1,00,000 6% Cumulative Preference shares of Rs. 60 each		60,00,000
	Total		1,64,00,000
2.	**Reserves and Surplus**		
	Capital Reserve		26,00,000
3.	**Long-term borrowings**		
	Secured		
	6% Debentures		56,00,000
4.	**Property, Plant and Equipment**		
	Carrying value	2,50,00,000	
	Adjustment under scheme of reconstruction	(50,00,000)	2,00,00,000
5.	**Investments**	20,00,000	
	Adjustment under scheme of reconstruction	(1,00,000)	19,00,000
6.	**Current assets**	2,00,00,000	
	Adjustment under scheme of reconstruction	(1,10,00,000)	
		90,00,000	
	Taxation liability paid	(3,00,000)	87,00,000

Working Note:

Capital Reduction Account

To	Liability for taxation A/c	1,00,000	By	Equity share capital	1,20,00,000
To	P & L A/c	12,00,000	By	6% Cumulative preferences	
To	Property, plant and equipment	50,00,000			
To	Current assets	1,10,00,000		Share capital	40,00,000
To	Investment	1,00,000	By	5% Debentures	24,00,000
To	Capital Reserve (Bal. fig.)	26,00,000	By	Sundry creditors	16,00,000
		2,00,00,000			2,00,00,000

3. The Balance Sheet of M/s Clean Ltd. as on 31st March. 2015 was summarized as follow :

Liabilities	Amount(Rs.)	Assets	Amount(Rs.)
Share Capital : Equity Shares of Rs.50 Each fully paid up	60,00,000	Land & Building	75,00,000
		Plant & Machinery	22,00,000
9% Preference Shares of Rs.10 each fully paid up	40,00,000	Trade Investment	16,50,000
		Inventories	9,50,000
7% Debentures (secured by plant & machinery)	23,00,000	Trade Receivables	18,00,000
		Cash and Bank Balances	3,60,000
8% Debentures	17,00,000	Profit & Loss Account	2,15,000
Trade Payables	6,00,000		
Provision for Tax	75,000		
	1,46,75,000		1,46,75,000

The Board of Directors of the company decided upon the following scheme of reconstruction duly approved by all concerned parties:

(1) The equity shareholders agreed to receive in lieu of their present holding of 1,20,000 shares of Rs.50 each as under:
(a) New fully paid equity shares of Rs.10 each equal to 2/3rd of their holding.
(b) 9% preference shares of Rs.8 each to the extent of 25% of the above new equity share capital.
(c) Rs.2, 80,000, 10% debentures of Rs.80 each.
(2) The preference shareholders agreed that their Rs.10 shares should be reduced to Rs. 8 by cancellation of Rs.2 per share. They also agreed to subscribe for two new equity shares of Rs.10 each every five preference shares held.
(3) The taxation liability of the company is settled at Rs. 66,000 and the same is paid immediately.
(4) One of the trade creditors of the company to whom the company owes Rs.1,00,000 decides to forgo 30% of his claim. He is allotted equity shares of Rs. 10 each in full satisfaction of his balance claim.
(5) Other trade creditors of Rs.5,00,000 are given option of either to accept fully paid 9% preference shares of Rs 8 each for the amount due to them or to accept 80% of the amount due to them in cash in full settlement of their claim. Trade creditors for Rs.3,50,000 accepted preference shares option and rest of them opted for cash towards full settlement of their claim.
(6) Company's contractual commitments amounting to Rs.6,50,000 have been settled by paying 4% penalty of contract value.
(7) Debenture holders having charge on plant and machinery accepted plant and machinery in full settlement of their dues.
(8) The rate of interest on 8% debentures is increased to 10%. The debenture holders surrender their existing debenture of Rs50 each & agreed to accept 10%debenture of Rs80 each for every 2 debentures held by them.
(9) The land and building to be depreciated by 5%.
(10) The debit balance of profit and loss account is to be eliminated.
(11) 1/4th of trade receivables and 1/5th of inventory to be written off.

Pass journal Entries and prepare Balance Sheet after completion of the reconstruction scheme in the books of M/s Clean Ltd. as per Schedule III to the Companies Act, 2013.

Solution:

1. Journal Entries in the books of clean Ltd

S.N.	Particulars	Dr.(Rs)	Cr.(Rs)
1.	Equity share Capital Capital (Rs50) A/c Dr.	60,00,000	
	To Equity share Capital(Rs 10) A/c (1,20,000 X 2/3) X Rs. 10		8,00,000
	To 9%Prefernce Share Capital (Rs8) A/C (for 25%of Rs. 8,00,000)		2,00,000
	To 10%Debentures (Rs 80)A/c		2,80,000
	To Capital Reconstruction A/c (Balancing Figure)		47,20,000
	(Being Equity share capital restated)		

2.	9%Preference Share Chare Capital (Rs. 10 X 4,00,000) A/c Dr. To 9%Preference Share Capital (Rs. 8 X 4,00,000)A/c To Capital Reconstruction A/c (B/F) (Being 9%Prefernce share capital restated)	40,00,000	 32,00,000 8,00,000
3.	Bank A/c Dr. To Equity Share Capital A/c(4,00,000 X 2/5) X Rs. 10 (Being Equity share capital issued)	16,00,000	 16,00,000
4.	Provision for Tax A/c Dr. To Cash & Bank A/c To Capital Reconstruction A/c (B/F) (Being Taxation Liability of the Company settled at Rs 66,000.)	75,000	 66,000 9,000
5.	Trade Creditors / payables A/c Dr. To Equity Share Capital (Rs10) A/c To Capital Reconstruction A/c (Being trade creditor of Rs. 1,00,000 settled)	1,00,000	 70,000 30,000
6.	Trade Creditors /Payables A/c Dr. To 9%Preference Share Capital (Rs8) A/c To Cash & Bank A/c (1,50,000 X 80%) To Capital Reconstruction A/c (1,50,000 X 20%) (Being 9% Preference Shares of Rs.8 each issued to Trade Creditors of Rs.3,50,000 and balance 80% of Claims settled in cash)	5,00,000	 3,50,000 1,20,000 30,000
7.	Capital Reconstruction A/c Dr. To Cash & Bank A/c (Being payment of Penalty for setting Contractual Obligation)	26,000	 26,000
8.	7% Debentures A/c Dr. To Plant and Machinery A/c To Capital Reconstruction A/c (Being takeover of Plant and Machinery by 7% Debenture holders)	23,00,000	 22,00,000 1,00,000
9.	8% Debentures (Rs.50 each) A/c Dr. To 10% Debentures A/c (Rs.80 each) [{(17,00,000)/50}/2] X 80 To Capital Reconstruction A/c (B/F) (Being 8% Debenture settled)	17,00,000	 13,60,000 3,40,000
10.	Capital Reconstruction A/c Dr. To Land and Building A/c (75,00,000 X 5%) To Profit and loss A/c To Trade Receivables A/c (1/4th x Rs.18,00,000) To inventories A/c (1/5th x Rs.9,50,000) (Being sundry assets reduced and losses written off)	12,30,000	 3,75,000 2,15,000 4,50,000 1,90,000
11.	Capital Reconstruction A/c Dr. To Capital Reserve A/c (Being balance in Reconstruction A/c transferred to Capital Reserve WN 1)	47,73,000	 47,73,000

II. Balance Sheet of Clean Ltd. and Reduced as at 1st April 2015

	Particulars as at 31st March	Note	Current Year
I	Equity AND LIABILITIES:		
(1)	Shareholders' Funds:		
	(a) Share Capital	1	62,20,000
	(b) Reserve and Surplus		47,73,000
	Capital Reserve (on Reconstruction) (WN 2)		
(2)	None-Current Liabilities:		
	Long Team Borrowings: 10% Debentures (2,80,000 + 13,60,000)		16,40,000
	Total		1,26,33,000
II	ASSETS		
(1)	None-Current Assets		
	(a) Property, Plant and Equipment:		
	Land and Building (75,00,000 – 5%)		71,25,000
	(b) None-Current Investments		16,50,000

(2)	Current Assets: (a) Trade Receivables (18,00,000 – 4,50,000) (b) Inventories (9,50,000 – 1,90,000) (c) Cash and Cash Equivalents - (WN 3		13,50,000 7,60,000 17,48,000
	Total		1,26,33,000

Note 1: Share Capital

Particulars	Amount
Authorised:……Equality Shares of Rs.10 each & …….9% Preference Share of Rs.8 each	
Issued, Subscribed & Paid up: 2,47,000 Equity Shares of Rs10each 4,68,750 9% Preference Shares of Rs.8 each (all the above Shares are issued as per approved scheme of reconstruction)	24,70,000 37,50,000
Total	62,20,000

Working Notes:

1 Capital Reconstruction A/c

Particulars	**Rs.**	**Particulars**	**Rs.**
To Cash / Bank A/c (Penalty on Contract)	26,000	By Equity Share Capital A/c	47,20,000
To Land and Building A/c	3,75,000	By 9% Preference Share Capital A/c	8,00,000
To Profit and Loss A/c (Debit balance)	2,15,000	By Provision for Tax A/c	9,000
To Trade Receivables	4,50,000	By Trade Creditors A/c (30,000 + 30,000)	60,000
To Inventories	1,90,000	By 7% Debentures A/c	1,00,000
To Capital Reserve (balancing figure)	47,73,000	By 8% Debentures A/c	3,40,000
Total	**60,29,000**	**Total**	**60,29,000**

2. Cash and Bank A/c

Particulars	**Rs.**	**Particulars**	**Rs.**
To balance b/d	3,60,000	By Provision for Tax	66,000
To Equity share capital A/c	16,00,000	By Trade Creditors A/c	1,20,000
		By Capital Reconstruction A/c	26,000
		By balance c/d (balancing figure)	17,48,000
Total	**19,60,000**	**Total**	**19,60,000**

Note:- Trade Investments are assumed as Long Term. Alternatively, it can be assumed as Investments held for trading purposes, and classified under Current Investments Category.

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

Particulars	Notes	Amount in ₹
I. Equity and Liabilities		
(1) Shareholders' Funds		
(a) Share Capital	1	15,00,000
(b) Reserves & Surplus	2	(3,00,000)
(2) Current Liabilities		
(a) Trade Payables		2,20,000
(b) Short Term Borrowings – Bank Overdraft		2,00,000
Total		16,20,000
II. Assets		
(1) Non-Current Assets		
(a) Property, Plant and Equipment	3	10,20,000
(b) Intangible Assets	4	1,20,600

(2) Current Assets		
(a) Inventories		1,70,000
(b) Trade Receivables		3,01,800
(c) Cash and cash equivalents		7,600
Total		16,20,000

Notes to Accounts

	₹	₹
(1) Share Capital		
90,000 Equity Shares of ₹ 10 each fully paid	9,00,000	
6% Preference Share Capital	6,00,000	15,00,000
(2) Reserves & Surplus		
Profit & Loss account		(3,00,000)
(3) Property, Plant and Equipment		
Land and Building	5,40,000	
Plant and Machinery	4,80,000	10,20,000
(4) Intangible Assets		
Goodwill	84,600	
Patents	36,000	1,20,600

Dividends on preference shares are in arrears for 3 years.

On the above date, the company adopted the following scheme of reconstruction:

(i) The preference shares are converted from 6% to 8% but revalued in a manner in which the total return on them remains unaffected.
(ii) The value of equity shares is brought down to ₹ 8 per share.
(iii) The arrears of dividend on preference shares are cancelled.
(iv) The debit balance of Goodwill account is written off entirely.
(v) Land and Building and Plant and Machinery are revalued at 85% and 80% of their respective book values.
(vi) Book debts amounting to ₹ 14,400 are to be treated as bad and hence to be written off.
(vii) The company expects to earn a profit at the rate of ₹ 90,000 per annum from the current year which would be utilized entirely for reducing the debit balance of Profit and loss accounts for 3 years. The remaining balance of the said account would be written off at the time of capital reduction process.
(viii) The balance of total capital reduction is to be utilized in writing down Patents.
(ix) A secured loan of ₹ 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		Debit	Credit
1.	6% Preference share capital A/c	Dr.	6,00,000	
	To 8% Preference share capital A/c			4,50,000
	To Capital reduction A/c			1,50,000
	(Being 6% preference shares converted to 8% preference shares so that return to pref. shareholders remains unaffected)			

2.	Equity share capital A/c (₹ 10)	Dr.	9,00,000	
	To Equity share capital A/c (₹ 8)			7,20,000
	To Capital reduction A/c			1,80,000
	(Being equity capital reduced to nominal value of ₹ 8 each)			
3.	Capital Reduction A/c	Dr.	3,30,000	
	To Goodwill A/c			84,600
	To Land and Building A/c			81,000
	To Plant and Machinery A/c			96,000
	To Trade Receivables A/c (Book debts)			14,400
	To Patents A/c (Bal. fig.)			24,000
	To Profit and loss A/c			30,000
	(Being losses and assets written off to the extent required)			
4.	Bank A/c	Dr.	4,80,000	
	To Bank Loan A/c			4,80,000
	(Being Loan taken)			
5.	Bank overdraft A/c	Dr.	2,00,000	
	To Bank A/c			2,00,000
	(Being Bank overdraft repaid)			

Capital Reduction Account

	Particulars	₹		Particulars	₹
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	Notes	₹
		Equity and Liabilities		
1		Shareholders' funds		
	a	Share capital	1	11,70,000
	b	Reserves and surplus	2	(2,70,000)
2		Current liabilities		
	a	Short term borrowings (Secured Bank Loan)		4,80,000
	b	Trade Payables		2,20,000
		Total		16,00,000

		Assets		
1		Non-current assets		
	a	Property, plant and equipment	3	8,43,000
	b	Intangible assets	4	12,000
2		Current Assets		
	a	Inventory		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:

			₹
1.	Share Capital		
	Authorized		
	Issued, subscribed and paid up:		
	90,000 equity shares of ₹ 8 each fully paid	7,20,000	
	8% Preference share capital*	4,50,000	11,70,000
2.	Reserves and Surplus		
	Profit and Loss Account (Dr. balance)		(2,70,000)
3.	Property plant and equipment		
	Land and Building	4,59,000	
	Plant and Machinery	3,84,000	8,43,000
4.	Intangible assets		
	Patent ₹ (36,000 - 24,000)		12,000
5.	Trade Receivables		
	Sundry Debtors	3,01,800	
	Less: Bad debts	(14,400)	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 ₹ 6,00,000 = ₹ 36,000
Rate of return	:	8% on Preference Shares
Dividend	:	(8/100) x X = ₹ 36,000
		X = (36,000/8) x 100 = ₹ 4,50,000
New Preference Share Capital	=	₹ 4,50,000
Old Preference Share Capital	=	₹ 6,00,000
(6,00,000 – 4,50,000)	=	₹ 1,50,000 Amount taken to Capital Reduction A/c.

(2) Since the company expects to earn a profit of ₹ 90,000 p.a. consecutively for three years and it shall be used to write-off debit balance of P & L account, hence ₹ 2,70,000 being loss shall be shown in the Balance Sheet under Reserve & Surplus head and ₹ 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 = (80/100) x 4,80,000		= ₹ 4,59,000
Plant & Machinery Reduced by:	= (85/100) x 5,40,000	= ₹ 3,84,000
Land & Building	= (5,40,000 - 4,59,000)	= ₹ 81,000
Plant & Machinery	= (4,80,000 - 3,84,000)	= ₹ 96,000

5. 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**

		Rs.	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			3,000
(Being general reserve utilized to write off the balance in Capital reduction A/c)			

Note: In place of Capital Reduction Account, Reconstruction Account or Internal Reconstruction Account may also be used in the above journal entries.

PREPARATION OF FINANCIAL STATEMENTS

1. On 31st March, 2018, SR Ltd. provides the following ledger balances after preparing its Profit & Loss Account for the year ended 31st March, 2018.

Particulars	**Amount (Rs.)**	
	Debit	**Credit**
Equity Share Capital, fully paid shares of Rs. 50 each		80,00,000
Calls in arrear	15,000	
Land	25,00,000	
Buildings	30,00,000	
Plant & Machinery	24,00,000	
Furniture & Fixture	13,00,000	
Securities Premium		15,00,000
General Reserve		9,41,000
Profit & Loss Account		5,80,000
Loan from Public Finance Corporation (Secured by Hypothecation of Land)		26,30,000
Other Long Term Loans		22,50,000
Short Term Borrowings		4,60,000
Inventories: Finished goods	45,00,000	
Raw materials	13,00,000	
Trade Receivables	17,50,000	
Advances: Short Term	3,75,000	
Trade Payables		8,13,000
Provision for Taxation		3,80,000
Unpaid Dividend		70,000
Cash in Hand	70,000	
Balances with Banks	4,14,000	
Total	**1,76,24,000**	**1,76,24,000**

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

(1) 50,000 fully paid equity shares were allotted as consideration for land.

(2) The cost of assets were:

Building	Rs. 32,00,000
Plant and Machinery	Rs. 30,00,000
Furniture and Fixture	Rs. 16,50,000

(3) Trade Receivables for Rs. 4,86,000 due for more than 6 months.

(4) Balances with banks include Rs. 56,000, the Naya bank, which is not a scheduled bank.

(5) Loan from Public Finance Corporation repayable after 3 years.

(6) The balance of Rs. 26,30,000 in the loan account with Public Finance Corporation is inclusive of Rs. 1,34,000 for interest accrued but not due. The loan is secured by hypothecation of land.

(7) Other long term loans (unsecured) includes:

Loan taken from Nixes Bank (Amount repayable within one year Rs. 4,80,000) Rs. 13,80,000

Loan taken from Directors Rs. 8,50,000

(8) Bills Receivable for Rs. 1,60,000 maturing on 15th June, 2018 has been discounted.

(9) Short term borrowings includes:

Loan from Naya bank Rs. 1,16,000 (Secured)

Loan from directors Rs. 48,000

(10) Transfer of Rs. 35,000 to general reserve has been proposed by the Board of directors out of the profits for the year.

(11) Inventory of finished goods includes loose tools costing Rs. 5 lakhs (which do not meet definition of property, plant & equipment as per AS-10)

You are required to prepare the Balance Sheet of the Company as on March 31st 2018 as required under Part - I of Schedule III of the Companies Act, 2013. You are not required to give previous year figures.

Solution:

SR Ltd.

Balance Sheet as on 31st March, 2018

Particulars			*Notes*	*Figures at the end of current reporting period (Rs.)*
Equity and Liabilities				
1		Shareholders' funds		
	a	Share capital	1	79,85,000
	b	Reserves and Surplus	2	30,21,000
2		Non-current liabilities		
	a	Long-term borrowings	3	42,66,000
3		Current liabilities		
	a	Short-term borrowings	4	9,40,000
	b	Trade Payables		8,13,000
	c	Other current liabilities	5	2,04,000
	d	Short-term provisions	6	3,80,000
		Total		1,76,09,000
Assets				
1		Non-current assets		
		Property, Plant and Equipment	7	92,00,000
2		Current assets		
	a	Inventories	8	58,00,000
	b	Trade receivables	9	17,50,000
	c	Cash and cash equivalents	10	4,84,000
	d	Short-term loans and advances		3,75,000
		Total		1,76,09,000

Notes to accounts

			Rs.
1.	Share Capital		
	Equity share capital		
	Issued, subscribed and called up		
	1,60,000 Equity Shares of Rs. 50 each (Out of the above 50,000 shares have been issued for consideration other than cash)	80,00,000	
	Less: Calls in arrears	(15,000)	79,85,000
	Total		79,85,000
2.	Reserves and Surplus		
	General Reserve	9,41,000	
	Add: Transferred from Profit and loss account	35,000	9,76,000
	Securities premium		15,00,000
	Surplus (Profit & Loss A/c)	5,80,000	
	Less: Appropriation to General Reserve (proposed)	(35,000)	5,45,000
			30,21,000
3.	Long-term borrowings		
	Secured: Term Loans		
	Loan from Public Finance Corporation [repayable after 3 years (26,30,000 - Rs. 1,34,000 for interest accrued but not due)] Secured by hypothecation of land		24,96,000
	Unsecured		
	Bank Loan (Nixes bank) 9,00,000		
	(Rs 13,80,000-Rs. 4,80,000 repayable within 1year)		
	Loan from Directors 8,50,000		
	Others 20,000		17,70,000
	Total		42,66,000
4.	Short-term borrowings		
	Loan from Nixes bank repayable within one year (Current maturity of Long term borrowing)	4,80,000	
	Loan from Naya bank (Secured)	1,16,000	
	Loan from Directors	48,000	
	Others	2,96,000	9,40,000
5.	Other current liabilities		
	Unpaid dividend	70,000	
	Interest accrued but not due on borrowings	1,34,000	2,04,000
6.	Short-term provisions		
	Provision for taxation		3,80,000
7.	Property, Plant and Equipment		
	Land		25,00,000
	Buildings	32,00,000	
	Less: Depreciation	(2,00,000)	30,00,000

	Plant & Machinery	30,00,000	
	Less: Depreciation	(6,00,000)	24,00,000
	Furniture & Fittings	16,50,000	
	Less: Depreciation	(3,50,000)	13,00,000
	Total		92,00,000
8.	Inventories		
	Raw Material	13,00,000	
	Finished goods	40,00,000	
	Loose tools	5,00,000	58,00,000
9.	Trade receivables		
	Outstanding for a period exceeding six months		4,86,000
	Others		12,64,000
	Total		17,50,000
10.	Cash and cash equivalents		
	Balances with banks		
	with Scheduled Banks	3,58,000	
	with others banks	56,000	4,14,000
	Cash in hand		70,000
	Total		4,84,000
11.	Contingent Liabilities and Commitments (to the extent not provided for)		
	Contingent Liabilities:		
	Bills discounted but not matured		1,60,000

2. The following is the trial balance of Omega Limited as on 31.3.2012

	Debit		Credit
Land at cost	220	Equity capital [shares of Rs. 10 each)	300
Plant and machinery at cost	770	10% debentures	200
Travel receivable	96	General reserves	130
Inventories [31.3.2012]	86	Profit & loss a/c	72
Bank	20	Securities premium	40
Adjusted purchases	320	Sales	700
Factories expenses	60	Trade payables	52
Administration expenses	30	Provision depreciation	172
Selling expenses	30	Suspense a/c	4
Debenture interest	20		
Interim dividend paid	18		
	1,670		1,670

Additional information:

(1) The authorised share capital of the company is 40,000 shares of Rs 10 each.
(2) The company on the advice of independent valuer wish to revalue the land at Rs 3,60,000.
(3) Declared final dividend@10% on 2nd April 2012.
(4) Suspense a/c of Rs 4,000 represents cash received for the sale of some of the machinery on 1.4.11. The cost of machinery was Rs 10,000 and the accumulated depreciation thereon being Rs 8,000.

(5) Depreciation is to be provided on plant & machinery at 10% cost.

You are required to prepare omega limited's balance sheet as on 31.3.2012 statement of profit & loss for the year ended 31.3.2012 as per Schedule III. Ignore previous year figure &taxation.

Solution: **Balance Sheet as at 31st March, 2012**

Particulars		*Note No.*	*(Rs. in 000)*
Equity and Liabilities			
1. Shareholders' funds			
a	Share capital	1	300
b	Reserves and Surplus	2	500
2. Non-Current liabilities			
A	Long term borrowings	3	200
3. Current liabilities			
	Trade Payables		52
	Total		**1082**
Assets			
1. Non-current assets			
A	Property, Plant and Equipment	4	880
2. Current assets			
A	Inventories		86
B	Trade receivables		96
C	Cash and cash equivalents		20
	Total		**1082**

Statement of Profit and Loss for the year ended 31st March, 2012

	Particulars		*Notes*	*(Rs. in 000)*
I	Revenue from operations			700
II	Other Income		5	2
III	**Total Income**			**702**
IV	Expenses:			
	Purchases			320
	Finance costs		6	20
	Depreciation (10% of 760)			76
	Other expenses		7	120
	Total Expenses			**536**
v.	**Profit (Loss) for the period**	(III – IV)		**166**

Notes to accounts ***(Rs. in 000)***

1.	**Share Capital**			
	Equity share capital			
	Authorized			
	40,000 shares of Rs. 10 each			400
	Issued & subscribed & called up			
	30,000 shares of Rs. 10 each			300
	Total			**300**
2.	**Reserves and Surplus**			
	Securities Premium Account			40
	Revaluation reserve			140
	General reserve			130
	Profit & loss Balance			
	Opening balance	72		
	Profit for the period	166	238	
	Less: Appropriations			
	Interim Dividend		(18)	220
				500
3.	**Long term borrowing**			
	10% Debentures			200

4.	**Property, Plant and Equipment**		
	Land		
	Opening balance		220
	Add: Revaluation adjustment		140
	Closing balance		360
	Plant and Machinery		
	Opening balance	770	
	Less: Disposed off	(10)	
		760	
	Less: Depreciation (172-8+76)	(240)	
	Closing balance		520
	Total		880
5.	**Other Income**		
	Profit on sale of machinery:		
	Sale value of machinery	4	
	Less: Book value of machinery (10-8)	(2)	2
6.	**Finance costs**		
	Debenture interest		20
7.	**Other expenses:**		
	Factory expenses		60
	Selling expenses		30
	Administrative expenses		30
			120

Note: The final dividend will not be recognized as a liability at the balance sheet date (even if it is declared after reporting date but before approval of the financial statements) as per Accounting Standards. Hence, it has not been recognized in the financial statements for the year ended 31 March, 20X2. Such dividends will be disclosed in notes only.

3. On 31st March, 20X1 Bose and Sen Ltd. provides to you the following ledger balances after preparing its Profit and Loss Account for the year ended 31st March, 20X1:

Credit Balances:	**Rs.**
Equity shares capital, fully paid shares of Rs. 10 each	70,00,000
General Reserve	15,49,100
Loan from State Finance Corporation (Secured by hypothecation of Plant & Machinery Repayable within one year Rs. 2,00,000)	10,50,000
Loans: Unsecured (Long term)	8,47,000
Sundry Creditors for goods &expenses (Payable within 6 months)	14,00,000
Profit &Loss Account	7,00,000
Provision for Taxation	8,16,900
	1,33,63,000
Debit Balances:	Rs.
Calls in arrear	7,000
Land	14,00,000
Buildings	20,50,000
Plant and Machinery	36,75,000
Furniture& Fixture	3,50,000
Inventories: Finished goods	14,00,000
Raw Materials	3,50,000
Trade Receivables	14,00,000
Advances: Short-term	2,98,900
Cash in hand	2,10,000
Balances with banks	17,29,000
Preliminary Expenses	93,100
Patents & Trademarks	4,00,000
	1,33,63,000

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

(i) 4,20,000 fully paid equity shares were allotted as consideration for land & buildings.
(ii) Cost of Building Rs. 28,00,000
(iii) Cost of Plant & Machinery Rs. 49,00,000
Cost of Furniture & Fixture Rs. 4,37,500
(iv) Trade receivables for Rs. 3,80,000 are due for more than 6 months.
(v) The amount of Balances with Bank includes Rs. 18,000 with a bank which is not a scheduled Bank and the deposits of Rs. 5 lakhs are for a period of 9 months.
(vi) Unsecured loan includes Rs. 2,00,000 from a Bank and Rs. 1,00,000 from related parties.
(vii) Entire amount of Preliminary expenses to be written off, by adjusting from opening balance of General Reserve.

You are not required to give previous year figures. You are required to prepare the Balance Sheet of the Company as on 31st March, 20X1 as required under Schedule III of the Company Act, 2013.

Solution:

Bose and Sen Ltd.
Balance Sheet as on 31st March, 20X1

Particulars			*Notes*	*Figures at the end of current reporting period (Rs.)*
Equity and Liabilities				
1		**Shareholders' funds**		
	a	Share capital	1	69,93,000
	b	Reserves and Surplus	2	21,56,000
2		**Non-current liabilities**	3	16,97,000
	a	Long-term borrowings		
3		**Current liabilities**		
	a	Trade Payables	4	14,00,000
	b	Other current liabilities	5	2,00,000
	c	Short-term provisions		8,16,900
		Total		1,32,62,900
Assets				
1		**Non-current assets**		
	a	PPE	6	74,75,000
	b	Intangible assets (Patents & Trade Marks)		4,00,000
2		**Current assets**		
	a	Inventories	7	17,50,000
	b	Trade receivables	8	14,00,000
	c	Cash and bank balances	9	19,39,000
	d	Short-term loans and advances		2,98,900
		Total		1,32,62,900

Notes to accounts

			Rs.
1	**Share Capital**		
	Equity share capital		
	Issued, subscribed and called up		
	7,00,000 Equity Shares of Rs. 10 each (Out of the above 4,20,000 shares have been issued for consideration other than cash)	70,00,000	
	Less: Calls in arrears	(7,000)	69,93,000
	Total		69,93,000
2	**Reserves and Surplus**		
	General Reserve	15,49,100	
	Less: Preliminary expenses	(93,100)	14,56,000
	Surplus (Profit & Loss A/c)		7,00,000
	Total		21,56,000
3	**Long-term borrowings**		
	Secured		
	Term Loans		
	Loan from State Finance Corporation (Rs. 10,50,000 - Rs. 2,00,000) (Secured by hypothecation of Plant and Machinery)		8,50,000
	Unsecured		
	Bank Loan	2,00,000	
	Loan from related parties	1,00,000	
	Others	5,47,000	8,47,000
	Total		16,97,000
4	**Other current liabilities**		
	Current maturities of long-term debt- loan Instalment repayable within one Year		2,00,000
5	**Short-term provisions**		
	Provision for taxation		8,16,900
6	**PPE**		
	Land		14,00,000
	Buildings	28,00,000	
	Less: Depreciation	(7,50,000) (b.f.)	20,50,000
	Plant & Machinery	49,00,000	
	Less: Depreciation	(12,25,000) (b.f.)	36,75,000

	Furniture & Fittings	4,37,500	
	Less: Depreciation	(87,500) (b.f.)	3,50,000
	Total		74,75,000
7	**Inventories**		
	Raw Material		3,50,000
	Finished goods		14,00,000
			17,50,000
8	**Trade receivables**		
	Debts outstanding for a period exceeding six months		3,80,000
	Other Debts		10,20,000
	Total		14,00,000
9	**Cash and bank balances**		
	Cash and cash equivalents		
	Cash at bank with Scheduled Banks	12,11,000	
	with others	18,000	12,29,000
	Cash in hand		2,10,000
	Other bank balances		
	Bank deposits for period of 9 months	5,00,000	5,00,000
	Total		**19,39,000**

4. Due to inadequacy of profits during the year ended 31st March, 2013, XYZ Ltd. 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:

	Rs.
17,500 9% Preference shares of Rs. 100 each, fully paid up	17,50,000
8,00,000 Equity shares of Rs. 10 each, fully paid up	80,00,000
General Reserves as on 1.4.2012	25,00,000
Capital Reserves as on 1.4.2012	3,00,000
Revaluation Reserves as on 1.4.2012	3,50,000
Net profit for the year ended 31st March, 2013	3,00,000

Average rate of dividend during the last five year has been 12%.

Answer: Amount that can be drawn from reserves for 10% dividend

10% dividend on Rs. 80,00,000		Rs. 8,00,000
Profits available		
Current year profit	3,00,000	
Less: Preference dividend	(1,57,500)	(1,42,500)
Amount which can be utilized from reserves		6,57,500

Conditions as per Companies (Declaration of dividend out of Reserves) Rules, 2014:

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. 12,25,000 [10% of (80,00,000+17,50,000+25,00,000)]

Condition III: The balance of reserves after drawl Rs. 18,42,500 (Rs. 25,00,000 - Rs. 6,57,500) shall not fall below 15 % of its paid up capital ie. Rs. 14,62,500 (15% of Rs. 97,50,000]
Since all the three conditions are satisfied, the company can withdraw Rs. 6,57,500 from accumulated reserves.

5. From the following information, prepare extract of Balance Sheet of A Limited along with notes making necessary compliance of Schedule III to the Companies Act, 2013:

	Amount (₹)
Loan Funds	
(a) Secured Loans	18,12,000
(b) Unsecured Loan - Short term from bank	2,25,000
Other information is as under:	
Secured Loans	
Term Loans from:	
Banks	8,95,000
Others	9,17,000
	18,12,000
Current Maturities of long-term loan from Bank	1,24,000
Current Maturities of long- term loan from Others	85,000

There was no interest accrued / due as at the end of the year. Current maturities of long-term loans amounting ₹ 2,09,000 is included in the value of secured loans of ₹ 18,12,000.

Solution:

Extract of Balance Sheet of A Ltd.

Particulars	**Note No**	**Amount**
Non - Current Liabilities		
Long term borrowings	1	16,03,000
Current Liabilities		
Short term borrowings	2	4,34,000

Notes to Accounts

1. Long-Term Borrowings		
Term loans – Secured		
- From banks	8,95,000	
Less: Current maturities of long-term debt (Refer Note 2)	(1,24,000)	7,71,000
- From other parties	9,17,000	
Less: Current maturities of long-term debt (Refer Note 2)	(85,000)	8,32,000
		16,03,000
2. Short-Term Borrowings		
Current maturities of long-term debt-Secured		
- From banks		1,24,000
- From others		85,000
(Unsecured loan)		
- from bank		2,25,000
		4,34,000

6. You are required to prepare a Statement of Profit and Loss and Balance Sheet from the following Trial Balance extracted from the books of the International Hotels Ltd., on 31st March, 20X2:

	Dr. ₹	Cr. ₹
Authorised Capital-divided into 5,000 6% Preference Shares of ₹ 100 each and 10,000 equity Shares of ₹ 100 each		15,00,000
Subscribed Capital -		
5,000 6% Preference Shares of ₹ 100 each		5,00,000
Equity Capital		8,05,000
Purchases - Wines, Cigarettes, Cigars, etc.	45,800	
- Foodstuffs	36,200	
Wages and Salaries	28,300	
Rent, Rates and Taxes	8,900	
Laundry	750	
Sales - Wines, Cigarettes, Cigars, etc.		68,400
- Food		57,600
Coal and Firewood	3,290	
Carriage and Cooliage	810	
Sundry Expenses	5,840	
Advertising	8,360	
Repairs	4,250	
Rent of Rooms		48,000
Billiard		5,700
Miscellaneous Receipts		2,800
Discount received		3,300
Transfer fees		700
Freehold Land and Building	8,50,000	
Furniture and Fittings	86,300	
Inventory on hand, 1st April, 20X1		
Wines, Cigarettes. Cigars, etc.	12,800	
Foodstuffs	5,260	
Cash in hand	2,200	
Cash with Bankers	76,380	
Preliminary and formation expenses	8,000	
2,000 Debentures of ₹ 100 each (6%)		2,00,000
Profit and Loss Account		41,500
Trade payables		42,000
Trade receivables	19,260	
Investments	2,72,300	
Goodwill at cost	5,00,000	
General Reserve		2,00,000
	19,75,000	19,75,000

Wages and Salaries Outstanding	1,280
Inventory on 31st March, 20X2	
Wines, Cigarettes and Cigars, etc.	22,500
Foodstuffs	16,400

Depreciation : Furniture and Fittings @ 5% p.a. : Land and Building @ 2% p.a.

The Equity capital on 1st April, 20X1 stood at ₹ 7,20,000, that is 6,000 shares fully paid and 2,000 shares ₹ 60 paid. The directors made a call of ₹ 40 per share on 1st October 20X1. A shareholder could not pay the call on 100 shares and his shares were then forfeited and reissued @ ₹ 90 per share as fully paid. The Directors declared a dividend of 8% on equity shares on 2nd April, 20X2, transferring any amount that may be required from General Reserve. Ignore Taxation.

Solution: Balance Sheet of International Hotels Ltd. as at 31st March, 20X2

Particulars	***Note No***	**₹**
Equity and Liabilities		
1 Shareholders' funds		
a Share capital	1	13,00,000
b Reserves and Surplus	2	2,68,745
2 Non-current liabilities		
a Long-term borrowings	3	2,00,000
3 Current liabilities		
a Trade Payables	4	42,000
b Other current liabilities	5	13,280
Total		**18,24,025**
ASSETS		
1 Non-current assets		
i PPE	6	9,14,985
ii Intangible assets (Goodwill)		5,00,000
iii Non-current investments		2,72,300
2 Current assets		
i Inventories	7	38,900
ii Trade receivables		19,260
iii Cash and bank balances	8	78,580
Total		**18,24,025**

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

	Particulars	***Notes***	***Amount***
I.	Revenue from operations	9	1,79,700
II.	Other income	10	6,800
III.	**Total Income (I + II)**		**1,86,500**
IV.	**Expenses:**		
	Cost of materials consumed	11	25,060
	Purchases of Inventory-in-Trade	12	45,800
	Changes in inventories of finished goods work-in-progress and Inventory-in-Trade	13	(9,700)
	Employee benefits expense	14	29,580
	Other operating expenses	15	18,000
	Selling and administrative expenses	16	14,200

	Finance costs	17	12,000
	Depreciation and amortisation expense	18	21,315
	Other expenses (Preliminary expenses written off)		8,000
	Total expenses		**1,64,255**
V.	**Profit (Loss) for the period (III - IV)**		**22,245**

Notes to accounts

			₹
1	**Share Capital**		
	Equity share capital		
	Authorised		
	10,000 Equity shares of ₹ 100 each		10,00,000
	Issued & subscribed		
	8,000 Equity Shares of ₹ 100 each (A)		8,00,000
	Preference share capital		
	Authorised		
	5,000 6% Preference shares of ₹ 100 each		5,00,000
	Issued & subscribed		
	5,000 6% Preference shares of ₹ 100 each	(B)	5,00,000
	Total (A + B)		**13,00,000**
2	**Reserves and Surplus**		
	Capital reserve [100 x (90 – 40)]		5,000
	General reserve	2,00,000	
			2,00,000
	Surplus (Profit & Loss A/c)	22,245	
	Add: Balance from previous year	41,500	
			63,745
	Total		**2,68,745**
3	**Long-term borrowings**		
	Secured		
	6% Debentures		2,00,000
	Total		**2,00,000**
4	**Trade Payables**		42,000
5	**Other current liabilities**		
	Wages and Salaries Outstanding	1,280	
	Interest on debentures	12,000	13,280
	Total		**13,280**

6	**PPE**			
	Freehold land & Buildings		8,50,000	
	Less: Depreciation		(17,000)	8,33,000
	Furniture and Fittings		86,300	
	Less: Depreciation		(4,315)	81,985
		Total		**9,14,985**
7	**Inventories**			
	Wines, Cigarettes & Cigars, etc.			22,500
	Foodstuffs			16,400
		Total		**38,900**
8	**Cash and bank balances**			
	Cash and cash equivalents			
	Cash at bank			76,380
	Cash in hand			2,200
	Other bank balances			Nil
		Total		**78,580**
9	**Revenue from operations**			
	Sale of products			
	Wines, Cigarettes, Cigars etc.		68,400	
	Food		57,600	1,26,000
	Sale of services			
	Room Rent		48,000	
	Billiards		5,700	53,700
		Total		**1,79,700**
10	**Other Income**			
	Transfer fees		700	
	Miscellaneous Receipts		2,800	
	Discount received		3,300	
		Total		**6,800**
11	**Cost of materials consumed**			
	Opening Inventory		5,260	
	Add: Purchases during the year		36,200	
	Less: Closing Inventory		(16,400)	25,060
		Total		**25,060**
12	**Purchases of Inventory-in-Trade**			
	Wines, Cigarettes etc.			45,800
		Total		**45,800**

13	**Changes in inventories of finished goods work-in-progress and Inventory-in-Trade**		
	Wines, Cigarettes etc.		
	Opening Inventory	12,800	
	Less: Closing Inventory	(22,500)	(9,700)
	Total		**(9,700)**
14	**Employee benefits expense**		
	Wages and Salaries	28,300	
	Add: Wages and Salaries Outstanding	1,280	29,580
	Total		**29,580**
15	**Other operating expenses**		
	Rent, Rates and Taxes		8,900
	Coal and Firewood		3,290
	Laundry		750
	Carriage and Cooliage		810
	Repairs		4,250
	Total		**18,000**
16	**Selling and administrative expenses**		
	Advertising		8,360
	Sundry Expenses		5,840
	Total		**14,200**
17	**Finance costs**		
	Interest on Debentures (2,00,000 x 6%)		12,000
	Total		**12,000**
18	**Depreciation and amortisation expense**		
	Land and Buildings (8,50,000 x 2%)	17,000	
	Furniture & Fittings (86,300 x 5%)	4,315	21,315
	Total		**21,315**

Note: The final dividend will not be recognized as a liability at the balance sheet date (even if it is declared after reporting date but before approval of the financial statements) as per Accounting Standards. Hence, it has not been recognized in the financial statements for the year ended 31 March, 20X2. Such dividends will be disclosed in notes only.

7. Alpha Ltd. provides you the following information :

(1) Raw material stock holding period : 3 months
(2) Work – in- progress holding period : 1 month
(3) Finished goods holding period : 5 months
(4) Debtors collection period : 5 months

You are required to compute the operating cycle of Alpha Ltd. What would happen if the trade is payables of the company are paid in 13 months – whether these should be classified as current or non-current liability?

Solution: According to Schedule III to the Companies Act, 2013 "An operating cycle is the time between the acquisition of assets for processing and their realization in cash or cash equivalents".
Therefore, operating cycle of Alpha Ltd. will be computed as under:
Raw material stock holding period + Work – in – progress holding period + Finished goods holding period + Debtors collection period
= 3 + 1+ 5 + 5 = 14 months
A Liability shall be classified as current when it is expected to be settled in the Company's normal operating cycle.
Since the operating cycle of Alpha Ltd. is 14 months, trade payables expected to be paid in 13 months should be treated as current liability.

8. Sagar Ltd. has issued convertible bonds for ₹ 65 crores which are due to mature on 30th September, 2018. While preparing financial statements for the year ending 31st March, 2018, company expects that bond holders will not exercise their option of converting bonds to equity shares. How should the company classify the convertible bonds as per the requirements of Schedule-Ill to the Companies Act, 2013 as on 31st March, 2018?
Also state, whether classification of convertible Bonds as per Schedule-III to the Companies Act will change if the company expects that convertible bond holders will convert their holdings into equity shares of Sagar Ltd.
Solution: Schedule III to the companies Act, 2013 provides that:
"A liability should be classified as current when it satisfies any of the following criteria:
(a) it is expected to be settled in the company's normal operating cycle;
(b) it is held primarily for the purpose of being traded;
(c) it is due to be settled within twelve months after the reporting date; or
(d) the company does not have an unconditional right to defer settlement of the liability for at least twelve months after the reporting date. Terms of a liability that could, at the option of the counterparty, result in its settlement by the issue of equity instruments and do not affect its classification."
In the present situation, Sagar Ltd. does not have an unconditional right to defer settlement of the liability for at least 12 months after the reporting date, hence Sagar Ltd. should classify the FCCBs as current liabilities as on 31st March 2018.
The position will be same even when the bond holders are expected to convert their holdings into equity shares of Sagar Ltd. Expectations cannot be called as unconditional rights. Thus, in this situation also, Sagar Ltd. should classify the FCCBs as current liabilities as on 31st March 2018.

BUYBACK OF SECURITIES

1. Complicated Ltd. (an unlisted company) gives the following information as on 31.3.2021:

Particulars	Amount (Rs.)
Equity shares of Rs. 10 each, fully paid up	13,50,000
Share option outstanding Account	4,00,000
Revenue Reserve	15,00,000
Securities Premium	2,50,000
Profit & Loss Account	1,25,000
Capital Reserve	2,00,000
Unpaid dividends	1,00,000
12% Debentures (Secured)	18,75,000
Advance from related parties (Long term - Unsecured)	10,00,000
Current maturities of long term borrowings	16,50,000
Application money received for allotment due for refund	2,00,000
Property, plant and equipment	46,50,000
Current assets	40,00,000

The Company wants to buy back 25,000 equity shares of Rs. 10 each, on 1st April, 2021 at Rs. 15 per share. Buy back of shares is duly authorized by its Articles and necessary resolution has been passed by the Company for this. The buy-back of shares by the Company is also within the provisions of the Companies Act, 2013. The payment for buy back of shares was made by the Company out of sufficient bank balance available shown as part of Current Assets.

You are required to prepare the necessary journal entries towards buy back of shares and prepare the Balance Sheet of the company after buy back of shares.

Solution: As per the information given in the question, buy-back of 25,000 shares @ Rs. 15, as desired by the company, is within the provisions of the Companies Act, 2013.

Journal Entries for buy-back of shares

			Debit (Rs.)	*Credit* (Rs.)
(a)	Equity shares buy-back account	Dr.	3,75,000	
	To Bank account			3,75,000
	(Being buy back of 25,000 equity shares of Rs. 10 each @ Rs. 15 per share)			
(b)	Equity share capital account	Dr.	2,50,000	
	Premium payable on buyback account	Dr.	1,25,000	
	To Equity shares buy-back account			3,75,000
	(Being cancellation of shares bought back)			
(c)	Securities premium account	Dr.	1,25,000	
	To Premium payable on buyback account			1,25,000
	(Being Premium payable on buyback adjusted against securities premium account)			
(d)	Revenue reserve account	Dr.	2,50,000	
	To Capital redemption reserve account			2,50,000
	(Being transfer of free reserves to capital redemption reserve to the extent of nominal value of capital bought back through free reserves)			

Balance Sheet of Complicated Ltd. as at 1st April, 2021

Particulars	*Note No*	*Amount* Rs.
EQUITY AND LIABILITIES		
1 **Shareholders' funds**		
(a) Share capital	1	11,00,000
(b) Reserves and Surplus	2	23,50,000
2 **Non-current liabilities**		
(a) Long-term borrowings	3	28,75,000
3 **Current liabilities**		
(a) Short-term borrowings	4	16,50,000
(b) Other current liabilities	5	3,00,000
Total		82,75,000
ASSETS		
1 **Non-current assets**		
(a) Property, Plant and Equipment		46,50,000
2 Current assets (Rs. 40,00,000 – Rs. 3,75,000)		36,25,000
Total		82,75,000

Notes to Accounts

			Rs.	*Rs.*
1.	Share Capital			
	Equity share capital			
	1,10,000 Equity shares of Rs. 10 each			11,00,000
2.	Reserves and Surplus			
	Capital Reserve		2,00,000	
	Capital Redemption Reserve		2,50,000	
	Securities premium	2,50,000		
	Less: Utilization for share buy-back	(1,25,000)	1,25,000	
	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

2. Perrotte Ltd. has the following capital structure as on 31-03-09

		(Rs. In crores)
ESC(Shares of Rs. 10 each fully paid)		330
Reserve & Surplus		
General Reserve	240	
Security premium account	90	
P&L a/c	90	
Infrastructure Development Reserve	180	600
Loan funds		1,800

The shareholders of Perrotte Ltd. have on the recommendation of their Board of Directors approved on 12-9-09 a proposal to buy back the maximum permissible number of Equity shares considering the large surplus funds available at the disposal of the company.
The prevailing market value of the company's shares is Rs. 25 per share and in order to induce the existing shareholders to offer their shares for buy back, it was decided to offer a price of 20% over market.
You are also informed that the Infrastructure Reserve is created to satisfy Income-Tax requirements.
You are required to compute the maximum number of shares that can be bought back in the light of the above information and also under a situation where the loan funds of the company were either Rs. 1,200 crores or Rs. 1,500 crores.
Assuming that the entire buy back is completed by 09.12.2009, show the accounting entries in the company's books in each situation.

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

Particulars	Number of shares When loan fund is (crores)		
	Rs. 1,800	Rs. 1,200	Rs. 1,500
Shares Outstanding Test (W.N.1)	8.25	8.25	8.25
Resources Test (W.N.2)	6.25	6.25	6.25
Debt Equity Ratio Test (W.N.3)	Nil	3.75	Nil
Maximum number of shares that can be bought back [least of the above]	Nil	3.75	Nil

Journal Entries for the Buy Back (applicable only when loan fund is Rs. 1,200 crores)

			Rs. in crores	
			Debit	Credit
(a)	Equity share buy back account	Dr.	112.5	
	To Bank account			112.5
	(Being buy back of 3.75 crores equity shares of Rs. 10 each @ Rs. 30 per share)			
(b)	Equity share capital account	Dr.	37.5	
	Securities premium account	Dr.	75	
	To Equity share buy back account			112.5
	(Being cancellation of shares bought back)			
(c)	General reserve account	Dr.	37.5	
	To Capital redemption reserve account			37.5
	(Being transfer of free reserves to capital redemption reserve to the extent of nominal value of share capital bought back out of redeemed through free reserves)			

Working Notes:

1 . **Shares Outstanding Test**

Particulars	(Shares in crores)
Number of shares outstanding	33
25% of the shares outstanding	8.25

2. Resources Test

Particulars	
Paid up capital (Rs. in crores)	330
Free reserves (Rs. in crores)	420
Shareholders' funds (Rs. in crores)	750
25% of Shareholders fund (Rs. in crores)	Rs. 187.5 crores
Buy back price per share	Rs. 30
Number of shares that can be bought back (shares in crores)	6.25 crores shares

3. Debt Equity Ratio Test

	Particulars	When loan fund is(crores)		
		Rs. 1,800	Rs. 1,200	Rs. 1,500
(a)	Loan funds (Rs. in crores)	1,800	1,200	1,500
(b)	Minimum equity to be maintained **after** buy back in the ratio of 2:1 (Rs. in crores)	900	600	750
(c)	Present equity shareholders fund (Rs. in crores)	750	750	750
(d)	Future equity shareholder fund (Rs. in crores) **(See Note 2)**	N.A.	712.5 (750-37.5)	N.A
(e)	Maximum permitted buy back of Equity (Rs. in crores) [(d) – (b)] **(See Note 2)**	Nil	112.5 (by simultaneous equation)	Nil
(f)	Maximum number of shares that can be bought back @ Rs. 30 per share (shares in crores) **(See Note 2)**	Nil	3.75 (by simultaneous equation)	Nil

Note: As per Company Act. 2013, the ratio of debt owed by the company should not be more than twice the capital and its free reserve **after** such buy-back. Also as per the section, on buy-back of shares out of free reserves a sum equal to the nominal value of the share bought back shall be transferred to Capita Redemption Reserve (CRR). As per section 80, utilization of CRR is restricted to issuance of fully paid-up bonus shares only. It means CRR is not available for distribution as dividend. Hence, CRR is not a free reserve. Therefore, for calculation of future equity i.e. share capital and free reserves, amount transferred to CRR on buyback has to be excluded from present equity.
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

$$(750 - x) - 600 = y \qquad (1)$$

$$(y/30*10) = x$$

Or $3x = y$

by solving the above equation we get

x = Rs. 37.5 crores

y = Rs. 112.5 crores

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

(in lakhs ₹)

Particulars			Notes	₹
1		**Equity and Liabilities** Shareholders' funds		
	A	Share capital	1	120
	B	Reserves and Surplus	2	118

2		Non-current liabilities		
		Long term borrowings	3	4
3		Current liabilities		
	A	Trade Payables		70
		Total		312
		Assets		
1		Non-current assets		
	A	Property, plant and Equipment		50
	B	Non-current Investments		120
2		Current assets		
	A	Cash and Cash equivalents		142
		Total		312

Notes to accounts

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

(i) The company redeemed the preference shares at a premium of 10% on 1st April, 20X1.

(ii) It also bought back 3 lakhs equity shares of ₹ 10 each at ₹ 30 per share. The payment for the above was made out of huge bank balances.

(iii) Included in its investment were "investments in own debentures" costing ₹ 2 lakhs (face value ₹ 2.20 lakhs). These debentures were cancelled on 1st April, 20X1.

(iv) The company had 1,00,000 equity stock options outstanding on the above- mentioned date, to the employees at ₹ 20 when the market price was ₹30 (This was included under current liabilities). On 1.04.20X1 employees exercised their options for 50,000 shares.

(A) Pass the journal entries to record the above.

(B) Prepare Balance Sheet as at 01.04.20X1.

Solution:

(in lakhs ₹)

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

	(Being the allotment to employees, of 50,000 shares of ₹ 10 each at a premium of 20 per share in exercise of stock options by employees)			
	Securities premium A/c To Premium on redemption of preference shares A/c (Being premium on redemption of preference shares adjusted through securities premium)	Dr.	2.00	2.00

Balance Sheet of Extra Ltd. as at 01.04.20X1

(in lakhs ₹)

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

Notes to accounts

No.	***Particulars***		**₹**
1	**Share Capital**		
	Equity shares of ₹ 10 each fully paid		100
	Less: Cancellation of bought back shares		(30)
	Add: Shares issued against ESOP		5
	Total		75

2	**Reserves and Surplus**		
	Capital Reserve		
	Opening balance	8.00	
	Add: Profit on cancellation of debentures	0.20	8.20
	Revenue reserves		
	Opening balance	50.00	
	Less: Creation of Capital Redemption Reserve	(50.00)	-
	Securities Premium		
	Opening balance	60.00	
	Less: Adjustment for cancellation of equity shares	(60.00)	
	Less: Adjustment for premium on redemption of preference shares	(2.00)	
	Add: Shares issued against ESOP at premium	10.00	8.00
	Capital Redemption Reserve		50.00
	Total		66.20
3	**Long term borrowings**		
	10% Debentures		4.00
	Less: Cancellation of own debentures		(2.20)
	Total		1.80
4.	**Other Current liabilities**		
	Opening balance		70.00
	Less: Adjustment for ESOP outstanding		(5.00)
	Total		65.00
5.	**Non-current investments**		
	Opening balance		120.00
	Less: Investment in own debentures		(2.00)
	Total		118.00
6.	**Cash and Cash Equivalents**		
	Opening balance		142.00
	Less: Payment to preference shareholders		(22.00)
	Less: Payment to equity shareholders		(90.00)
	Add: Share price received against ESOP		10.00
	Total		40.00

AS 1: DISCLOSURE OF ACCOUNTING POLICIES

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

The company decides to change from FIFO method to weighted average method for ascertaining the cost of inventory from the year 2014-15. On the basis of weighted average method, closing inventory as on 31.03.2015 amounts to Rs. 1,47,000. Realisable value of the inventory as on 31.03.2015 amounts to Rs. 1,95,000.

Discuss disclosure requirement of change in accounting policy as per AS-1.

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

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

2. A Ltd. has sold its building for 50 lakhs to B Ltd. and has also given the possession to B Ltd. The book value of the building is 30 lakhs. As on 31^{st} March, 2006 the documentation and legal formalities are pending. The company has not recorded the sale and has shown the amount received as advance. Do you agree with this treatment?

Answer: As per AS-1, "Disclosure of Accounting Policies" The accounting treatment and presentation in financial statements of transactions and events should be governed by their substance and not merely by the legal form.

Treatment of 'non recording' the sale and has shown the amount received as advance by the company is not correct. In the given case "A Ltd. has sold the building for 50 lakhs to B Ltd. and has also given possession to B Ltd." It seems that the substance of the transaction has passed and thus the company should record the sale.

3. State whether the following statements are 'True' or 'False'. Also give reason for your answer.

(1) Certain fundamental accounting assumptions underline the preparation and presentation of financial statements. They are usually specifically stated because their acceptance and use are not assumed.

(2) If fundamental accounting assumptions are not followed in presentation and preparation of financial statements, a specific disclosure is not required.

(3) All significant accounting policies adopted in the preparation and presentation of financial statements should form part of the financial statements.

(4) Any change in an accounting policy, which has a material effect should be disclosed. Where the amount by which any item in the financial statements is affected by such change is not ascertainable, wholly or in part, the fact need not to be indicated.

(5) There is no single list of accounting policies which are applicable to all circumstances.

Solution:

(1) **False:** As per AS 1 "Disclosure of Accounting Policies", certain fundamental accounting assumptions underlie the preparation and presentation of financial statements. They are usually not specifically stated because their acceptance and use are assumed. Disclosure is necessary if they are not followed.

(2) **False:** As per AS 1, if the fundamental accounting assumptions, viz. Going Concern, Consistency and Accrual are followed in financial statements, specific disclosure is not required. If a fundamental accounting assumption is not followed, the fact should be disclosed.

(3) **True:** To ensure proper understanding of financial statements, it is necessary that all significant accounting policies adopted in the preparation and presentation of financial statements should be disclosed. The disclosure of the significant accounting policies as such should form part of the financial statements and they should be disclosed in one place.

(4) **False:** Any change in the accounting policies which has a material effect in the current period or which is reasonably expected to have a material effect in later periods should be disclosed. Where such amount is not ascertainable, wholly or in part, the fact should be indicated.

(5) **True:** As per AS 1, there is no single list of accounting policies which are applicable to all circumstances. The differing circumstances in which enterprises operate in a situation of diverse and complex economic activity make alternative accounting principles and methods of applying those principles acceptable.

4. XYZ Company is engaged in the business of financial services and is undergoing tight liquidity position, since most of the assets of the company are blocked in various claims/petitions in a Special Court. XYZ has accepted Inter-Corporate Deposits (ICDs) and, it is making its best efforts to settle the dues. There were claims at varied rates of interest, from lenders, from the due date of ICDs to the date of repayment. The company has provided interest, as per the terms of the contract till the due date and a note for non-provision of interest on the due date to date of repayment was affected in the financial statements. On account of uncertainties existing regarding the determination of the amount and in the absence of any specific legal obligation at present as per the terms of contracts, the company considers that these claims are in the nature of "claims against the company not acknowledged as debt", and the same has been disclosed by way of a note in the accounts instead of making a provision in the profit and loss accounts. State whether the treatment done by the Company is correct or not.

Solution : Para 17 of AS-1 'Disclosure of Accounting Policies' recognises 'prudence' as one of the major considerations governing the selection and application of accounting policies. In view of the uncertainty attached to future events, profits are not anticipated but recognised only when realised though not necessarily in cash. Provision is made for all known liabilities and losses even though the amount cannot be determined with certainty and represents only a best estimate in the light of available information.

Also as per para 10 of the AS 1, 'accrual' is one of the fundamental accounting assumptions.

Irrespective of the terms of the contract, so long as the principal amount of a loan is not repaid, the lender cannot be replaced in a disadvantageous position for non-payment of interest in respect of overdue amount. From the aforesaid, it is apparent that the company has an obligation on account of the overdue interest. In this situation, the company should provide for the liability (since it is not waived by the lenders) at an amount estimated or on reasonable basis based on facts and circumstances of each case. However, in respect of the overdue interest amounts, which are settled, the liability should be accrued to the extent of amounts settled. Non-provision of the overdue interest liability amounts to violation of accrual basis of accounting. Therefore, the treatment, done by the company, of not providing the interest amount from due date to the date of repayment is not correct.

AS 2: VALUATION OF INVENTORIES

1. Mr. Mehul gives the following information relating to items forming part of inventory as on 31-3-2017. His factory produces Product X using Raw Material A.
   (i) 600 units of Raw material A (purchased @ Rs. 120). Replacement cost of raw material A as on 31-3-2017 is Rs. 90 per unit.
   (ii) 500 units of partly finished goods in the process of producing X and cost incurred till date Rs. 260 per unit. These units can be finished next year by incurring additional cost of Rs. 60 per unit.
   (iii) 1500 units of finished Product X and total cost incurred Rs. 320 per unit. Expected selling price of Product X is Rs. 300 per unit.

   Determine how each item of inventory will be valued as on 31-3-2017. Also calculate the value of total inventory as on 31-3-2017.

   Solution: 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 realisable value, the materials are written down to net realisable value. In such circumstances, the replacement cost of the materials may be the best available measure of their net realisable value. In the given case, selling price of product X is Rs. 300 and total cost per unit for production is Rs. 320.

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

   Valuation of Total Inventory as on 31.03.2017: **(Rs.)**

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

2. 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, they were all sold after the balance sheet date at 50% of their normal selling price.
   (b) 200 skirts, which had cost Rs. 50 each. These too were found to be defective. Remedial work in April cost Rs. 2 per skirt, and selling expenses for the batch totalled Rs. 200. They were sold for Rs. 55 each.
   (c) 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?

   Solution:

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 skirts and shirts as their NRV is more than their cost which was included in value of inventory.

3. A Ltd. purchased 1,00,000 MT for Rs. 100 each MT of raw material and introduced it in the production process to get 85,000 MT as output. Normal wastage is 5%. In the process, company incurred the following expenses:

Direct Labour	Rs. 10,00,000
Direct Variable Overheads	Rs. 1,00,000
Direct Fixed Overheads	Rs. 1,00,000
(Including interest Rs. 40,625)	

Of the above 80,000 MT was sold during the year and remaining 5,000 MT remained in closing stock. Due to fall in demand in market the selling price for the finished goods on the closing day was estimated to be Rs. 105 per MT. Calculate the value of closing stock.

Answer: **Calculation of cost for closing inventory**

Particulars	Rs.
Cost of Purchase (1,00,000 x 100)	1,00,00,000
Direct Labour	10,00,000
Variable Overhead	1,00,000
Fixed Overhead (1,00,000 - 40,625)	59,375
Cost of Production for normal output i.e. 95,000 MT	1,11,59,375
Cost of closing inventory per unit (Rs. 1,11,59,375/95,000)	Rs. 117.47 (approx)
Net Realisable Value per unit	Rs. 105

Since, net realisable value is less than cost, closing inventory will be valued at Rs. 105. Therefore, closing inventory is Rs. 5,25,000 (5,000 x 105).

Note: Abnormal wastage of 10,000 MT i.e.10,000 MT x Rs. 117.47 = Rs. 11,74,670 will be separately accounted for in the books.

4. Calculate the value of raw materials and closing stock based on the following information:

Raw material X	
Closing balance	500 units
	Rs per unit
Cost price including excise duty	200
Excise duty (Cenvat credit is receivable on the excise duty paid)	10
Freight inward	20
Unloading charges	10
Replacement cost	150
Finished goods Y	
Closing Balance	1200 units
	Rs per unit
Material consumed	220
Direct Labour	60
Direct overhead	40

Total Fixed overhead for the year was Rs 2,00,000 on normal capacity of 20,000 units.

Calculate the value of the closing stock when:-

(i) Net Realizable value of the Finished Goods Y is Rs 400.

(ii) Net Realizable Value of the Finished Goods Y is Rs 300.

Solution:

Statement showing valuation of Raw Material and Finished Goods at cost

Raw Material X	**Rs.**
Cost Price	200
Less: CENVAT credit	(10)
	190
Add: Freight Inward	20
Unloading charges	10
Cost	220

Finished goods Y	**Rs.**
Materials consumed	220
Direct labour	60
Direct overhead	40
Fixed overheads (2,00,000/20,000)	10
Cost	330

(i) When Net Realisable Value (NRV) of the Finished Goods Y is Rs. 400
NRV is greater than the cost of Finished Goods Y i.e. Rs. 330
Hence, Raw Material and Finished Goods will be valued at cost
Accordingly, value of closing stock will be:

	Qty	Rate	Amount (Rs.)
Raw Material X	500	220	1,10,000
Finished Goods Y	1,200	330	3,96,000
Total cost of closing stock			5,06,000

(ii) When Net Realisable Value of the Finished Goods Y is Rs. 300
NRV is less than the cost of Finished Goods Y i.e. Rs. 330
Hence, Raw Material is to be valued at replacement cost and Finished Goods are to be valued at NRV.
Accordingly, value of closing stock will be:

		Qty	Rate	Amount (Rs.)
Raw Material	X	500	150	75,000
Finished Goods	Y	1,200	300	3,60,000
Total cost of closing stock				4,35,000

Note: It has been assumed that Raw Material X is used for production of Finished Goods Y.

5. In the following cases, find the value of closing stock as per AS 2:
   (i) Sonu is a retailer dealing in toys. During the year, he purchased items worth ₹ 1,47,000 and made a total sale ₹ 1,54,000. The average percentage of gross margin is 10% on cost. Opening stock of toys at cost was ₹ 20,000.
   (ii) On 21st March, 2023, Mohan purchased 250 chairs at ₹ 300 each. The selling price of the chair is ₹ 400 each. Owing to a manufacturing defect, net realisable value of the whole lot of chair was determined at 70% of their normal selling price. No chairs were sold during the year.

Solution:

(i) Cost of closing inventory is shown below:

	₹
Sale value of opening stock and purchases (₹ 20,000 + ₹1,47,000) x 1.10	1,83,700
Sales	(1,54,000)
Sale value of unsold stock	29,700
Less: Gross Margin (₹ 29,700 / 1.10) x 0.10	(2,700)
Cost of closing inventory	27,000

(ii)

Closing stock at cost (250X ₹ 300)	(i)	75,000
Net Realizable value of closing stock (₹ 280* × 250)	(ii)	70,000
Value of closing stock [lower of (i) and (ii)]		70,000

6. XYZ Limited is engaged in a business of manufacturing and supply of lubricants. For manufacturing of lubricant, company generally requires two types of raw material i.e. 1) Base Oil & 2) Additives.
   For Base Oil procurement, the company's cost structure per litre is as follows:
   (1) Material Cost (Base Oil) - Rs. 100 per Litre
   (2) Custom Duty – 5% on Material Cost.
   (3) Storage Tank Rent – Rs. 2 per litre.
   (4) Custom House Agent charges – Rs. 1 per litre
   (5) Inward Freight (i.e. Transportation cost for transferring the goods from Shore Tanks to Plants) – Rs. 3 per litre.

Costing manager informed you the following facts:
(1) We have purchased a 100 Litres of Base Oil from one of our Group Company situated in Singapore.
(2) Base Oil material is duly arrived at port and goods have been duly unloaded in storage tanks.
(3) Due to Covid 19 Lockdown, Base Oil is still lying in storage tanks as at 31.03.2020.
Costing Manager requires your assistance at what value Base Oil should be recorded as Inventory.
Solution:

Particulars	**Amount**	**Remarks**
Material Cost	10,000	(100 Quantity x Rs. 100)
Custom Duty	500	(5% of Material Value)
Storage Tank	200	(100 Quantity x Rs. 2)
CHA Charges	100	(100 Quantity x Rs. 1)
Inward Freight	0	<Not yet incurred>
Total	**10,800**	

As per AS 2, the cost of inventories shall comprise all costs of purchase, costs of conversion and other costs incurred in bringing the inventories to their present location and condition.
As per AS 2, the costs of purchase of inventories comprise the purchase price, import duties and other taxes (other than those subsequently recoverable by the entity from the taxing authorities), and transport, handling and other costs directly attributable to the acquisition of finished goods, materials and services. Trade discounts, rebates and other similar items are deducted in determining the costs of purchase.
In above case, all the expenses (i.e. Custom duty, Storage Tank, CHA Charges) are directly attributable to the acquisition of material. Though, inward freight cost is directly attributable to the acquisition but it will be incurred once movement of goods happened between the Storage Tanks to plant, as at year end, the goods are still lying at Shore Tanks and hence such inward freight cost is not directly attributable to the acquisition of materials and hence considered as NIL.

7. Sun Ltd. has fabricated special equipment (solar power panel) during 2014-2015 as per drawing and design supplied by the customer. However due to a liquidity crunch, the customer has requested the company for postponement in delivery schedule and requested the company to withhold the delivery of finished goods products and discontinue the production of balance items.
As a result of the above, the details of customer balance and the goods held by the company as work-in-progress and finished goods as on 31-3-2016 are as follows:

(i)	Solar power panel (WIP)	Rs. 85 lakhs
(ii)	Solar power panel (finished products)	Rs. 55lakhs
(iii)	Sundry debtors (solar power panel)	Rs. 65 lakhs

The petition for winding up against the customer has been filled during 2015-2016 by Sun Ltd.
Comment with explanation on provision to be made of Rs. 205 lakhs included in sundry Debtors, finished goods and WIP in the financial statement of 2015-16.
Solution: From the fact given in question it is obvious that Sun Ltd. is a manufacturer of solar power panel. As per AS-2, "Valuation of Inventory" Inventories are assets (a) Held for sale in the ordinary course of business; (b) in the process of production for such sale; or (c) in the form of materials /supplies to be consumed in the production process/rendering of services. Therefore, solar power panel held in its stock will be considered as its inventory. Further, as per the standard, inventory at the end of the year are to be valued at lower of cost or NRV.
As the customer has postponed the delivery schedule due to liquidity crunch the entire cost incurred for solar power panel which were to be supplied has been shown in Inventory. The solar power panel are in the possession of the Company which can be sold in the market. Hence company should value such inventory as per principle laid down in AS 2 i.e. lower of cost or NRV. Though, the goods were produced as per specifications of buyer of the company should determine the NRV of these goods in the market and value the goods accordingly. Change in value of such solar panel should be provided for in the books. In the absence of NRV of WIP and Finished product given in the question, assuming that cost is lower, the company shall value its inventory as per AS 2 for Rs. 140 lakhs [i.e. solar power panel (WIP) Rs. 85 lakhs + Solar power panel (finished products) Rs. 55 lakhs].
Alternatively, if it is assumed that there is no buyer for such fabricated solar power panel, then the NRV will be Nil. In such a case, full value of finished goods and WIP will be provided for in the books.
As regards Sundry Debtors balance, since the Company has filed a petition for winding up against the customer in 2015-16, it is probable that amount is not recoverable from the party. Hence, the provision for doubtful debts for Rs. 65 lakhs shall be made in the books against the debtors amount.

AS 4 - CONTINGENCIES AND EVENT OCCURRING AFTER BALANCE SHEET DATE

1. AS 4 prescribes that adjustments to assets and liabilities are required for events occurring after the Balance Sheet date that provide additional information materially affecting the determination of the amount relating to conditions existing at the Balance sheet date-generally called adjusting events. "Proposed Dividend" is shown and adjusted in the Balance Sheet even if it is not an adjusting event as per AS 4 because it is proposed by the Board of Directors of the company after the Balance sheet date.

Keeping this in view, is it not a violation of AS 4 to show proposed dividends as current liabilities and provisions? Comment.

Answer: As per para 8.5 of AS-4, There are events which, although they take place after the balance sheet date, are sometimes reflected in the financial statements because of statutory requirements or because of their special nature. For example, if dividends are declared after the balance sheet date but before the financial statements are approved for issue, the dividend are not recognised as a liability at the balance sheet date because no obligation exist at that time unless a statute requires otherwise. Such dividends are disclosed in notes.

Further as per Para 14 of AS-4 If an enterprise declares dividends to shareholders after the balance sheet date, the enterprise should not recognise those dividends as a liability at the balance sheet date unless a statute requires otherwise. Such dividends should be disclosed in notes.

So in the given question proposed dividend shall be disclosed into notes to account.

2. During the year 2012-2013, Raj Ltd. was sued by a competitor for Rs. 15 lakhs for infringement of a trademark. Based on the advice of the company's legal counsel, Raj Ltd. provided for a sum of Rs. 10lakhs in its financial statements for the year ended 31st March, 2013. On 18th May, 2013, the Court decided in favour of the party alleging infringement of the trademark and ordered Raj Ltd. to pay the aggrieved party a sum of Rs. 14 lakhs. The financial statements were prepared by the company's management on 30th April, 2013, and approved by the board on 30th May, 2013.

Solution: As per para 8 of AS 4 "Contingencies and Events Occurring After the Balance Sheet Date, adjustments to assets and liabilities are required for events occurring after the balance sheet date that provide additional information material y affecting the determination of the amounts relating to conditions existing at the balance sheet date.

In the given case, since Raj Ltd. was sued by a competitor for infringement of a trademark during the year 2012-13 for which the provision was also made by it, the decision of the Court on 18th May, 2013, for payment of the penalty will constitute as an adjusting event because it is an event occurred before approval of the financial statements. Therefore, Raj Ltd. should adjust the provision upward by Rs. 4 lakhs to reflect the award decreed by the Court to be paid by them to its competitor.

Had the judgment of the Court been delivered on 1st June, 2013, it would be considered as post reporting period i.e. event occurred after the approval of the financial statements. In that case, no adjustment in the financial statements of 2012-13 would have been required.

3. Neel Limited has its corporate office in Mumbai and sells its products to stockists all over India. On 31st March, 2013 the company want to recognize receipt of cheques bearing date 31st March, 2013 or before, as "Cheques in Hand" by reducing "Trade Receivables". The "Cheques in Hand" is shown in the Balance Sheet as an item of cash and cash equivalents. All cheques are presented to the bank in the month of April 2013 and are also realized in the same month in normal course after deposit in the bank. State with reasons, whether each of the following is an adjusting event and how this fact is to be disclosed by the company, with reference to the relevant accounting standard

(i) Cheques collected by the marketing personnel of the company from the stockists on or before 31st March, 2013.

(ii) Cheques sent by the stockists through Courier on or before 31st March 2013.

Answer:

(i) Cheques collected by the marketing personnel of the company is an adjusting event as the marketing personnel are employees of the company and therefore, are representatives of the company. Handing over of cheques by the stockist to the marketing employees discharges the liability of the stockist. Therefore, cheques collected by the marketing personnel of the company on or before 31st March, 2013 require adjustment from the stockists' accounts i.e. from 'Trade Receivables A/c' even though these cheques (dated on or before 31st March, 2013) are presented in the bank in the month of April, 2013 in the normal course. Hence, collection of cheques by the marketing personnel is an adjusting event as per AS 4 'Contingencies and Events Occurring after the Balance Sheet Date'. Such 'cheques in hand' will be shown in the Balance Sheet as 'Cash and Cash equivalents' *with a disclosure in the Notes to accounts about the accounting policy followed by the company for such cheques.*

(ii) Even if the cheques bear the date 31st March or before and are sent by the stockists through courier on or before 31st March, 2013, it is presumed that the cheques will be received after 31st March. Collection of cheques after 31st March, 2013 does not represent any condition existing on the balance sheet date i.e. 31st March. Thus, the collection of cheques after balance sheet date is not an adjusting event. Cheques that are received after the balance sheet date should be accounted for in the period in which they are received even though the same may be dated 31st March or before as per AS 4. Moreover, the collection of cheques after balance sheet date does not represent *any material change affecting financial position of the enterprise, so no disclosure in the Director's Report is necessary.*

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

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

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

(iii) It sends a proposal to sell an immovable property for ₹ 30 lakhs in March. The book value of the property is ₹ 20 lakhs as on year end date. However, the deed was registered as on 15th April.

(iv) The terms and conditions for acquisition of business of another company have been decided by March end. But the financial resources were arranged in April and amount invested was ₹ 40 lakhs.

(v) Theft of cash of ₹ 2 lakhs by the cashier on 31st March but was detected the next day after the financial statements have been approved by the Directors.

Answer: According to AS 4 on 'Contingencies and Events Occurring after the Balance Sheet Date', adjustments to assets and liabilities are required for events occurring after the balance sheet date that provide additional information materially affecting the determination of the amounts relating to conditions existing at the balance sheet date. However, adjustments to assets and liabilities are not appropriate for events occurring after the balance sheet date, if such events do not relate to conditions existing at the balance sheet date. —Contingencies‖ used in the Standard is restricted to conditions or situations at the balance sheet date, the financial effect of which is to be determined by future events which may or may not occur.

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

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

(iii) In the given case, proposal for deal of immovable property was sent before the closure of the books of accounts. This is a non-adjusting event as only the proposal was sent and no agreement was effected in the month of March i.e. before the balance sheet date.

(iv) As the term and conditions of acquisition of business of another company had been decided by the end of March, acquisition of business is an adjusting event occurring after the balance sheet date. Adjustment to assets and liabilities is required since the event affects the determination and the condition of the amounts stated in the financial statements for the financial year ended on 31st March.

(v) Since the financial statements have been approved before detection of theft by the cashier of ₹ 2,00,000, it becomes a non-adjusting event and no disclosure is required in the report of the Approving Authority.

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

1. A company signed an agreement with the Employees Union on 1.9.2007 for revision of wages with retrospective effect from 30.9.2006. This would cost the company an additional liability of Rs. 5,00,000 per annum. Is a disclosure necessary for the amount paid in 2007-08?
Answer:- It is given that revision of wages took place on 1st September, 2007 with retrospective effect from 30.9.2006. Therefore wages payable for the half year from 1.10.2006 to 31.3.2007 cannot be taken as an error or omission in the preparation of financial statements and hence this expenditure cannot be taken as a prior period item. Additional wages liability of Rs. 7,50,000 (for 1½ years @ Rs. 5,00,000 per annum) should be included in current year's wages.
It may be mentioned that additional wages is an expense arising from the ordinary activities of the company. Although abnormal in amount, such an expense does not qualify as an extraordinary item. However, as per para 12 of AS 5 (Revised), 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.

2. During the year 2001-2002, a medium size manufacturing company wrote down its inventories to net realizable value by Rs. 5, 00,000. Is a separate disclosure necessary?
Answer:- Although the case under consideration does not relate to extraordinary item, but the nature and amount of such item may be relevant to users of financial statements in understanding the financial position and performance of an enterprise and in making projections about financial position and performance. Para 12 of AS 5 (Revised in 1997) on Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies states that:
"When items of income and expense within profit or loss from ordinary activities are of such size, nature or incidence that their disclosure is relevant to explain the performance of the enterprise for the period, the nature and amount of such items should be disclosed separately."
Circumstances which may give to separate disclosure of items of income and expense in accordance with para 12 of AS 5 include the write-down of inventories to net realisable value as well as the reversal of such write-downs.

3. Closing stock for the year ending on 31.03.2010 is Rs. 50,000 which includes stock damaged in a fire in 2008-09. On 31.3.2009, the estimated NRV of the damaged stock was Rs. 12,000. The revised estimate of NRV of damaged goods amounting Rs. 4,000 has been included in closing stock of Rs. 50,000 as on 31.03.2010.
Find the value of closing stock to be shown in the profit & loss account.
Answer: The fall in estimated net realisable value of damaged stock ₹ 8,000 is the effect of change in accounting estimate. As per para 25 of AS 5 'Net Profit or Loss the Period, Prior Period Items and Changes in Accounting Policies', the effect of a 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. It is presumed that the loss by fire in the year ended 31.3.2009, i.e. difference of cost and NRV was shown in the profit and loss account as an extra-ordinary item. Therefore, in the year 2009-10, revision in accounting estimate should also be classified as extra-ordinary item in the profit and loss account and closing stock should be shown excluding the value of damaged stock.
Value of closing stock for the year 2009-10 will be as follows:

	₹
Closing Stock (including damaged goods)	50,000
Less: Revised value of damaged goods	(4,000)
Closing stock (excluding damaged goods)	46,000

4. Shama was working with ABC Ltd. drawing monthly salary of Rs. 25,000 per month. She went on maternity leave with pay for 7 months i.e. from 1-01-2017 to 31-7-17. Her salary for 3 months was not provided for in financial statements for F.Y. 2016-17 due to omission. When she joined after leave period, the whole salary for 7 months was paid to her. You are required to:
   (i) Pass the necessary journal entries in F.Y. 2017-18 to record the above transaction as per accounting standard-5 and state reason for the same.

(ii) Would the treatment have been different, if Shama was terminated on 01-01-2017 and was reinstated in service by the court w.e.f. 01-08-2017 with instruction to pay Shama salary for the intervening period i.e. 1-01- 2017 to 31-07-2017.

Solution: As per AS 5 "Net Profit or Loss for the Period", Prior Period Items and Changes in Accounting Policies, the term 'prior period items', refers to income or expenses which arise in the current period as a result of errors or omissions in the preparation of the financial statements of one or more prior periods. The nature and amount of prior period items should be separately disclosed in the statement of profit and loss so that their impact on the current profit or loss can be perceived. Hence, in this case salary paid to Shama for 3 months i.e 1.1.2017 to 31.3.2017 Rs. 75,000 will be classified as prior period item in FY 2017-18 and following journal entry shall be passed:

(i) **Journal entry in FY 2017-18**

Salary A/c (Rs 25,000 x 4)	Dr.	1,00,000	
Prior period item (Rs 25,000 x 3)	Dr.	75,000	
To Bank A/c			1,75,000

(Salary related to 7 months paid out of which 3'months' salary is prior period item)

Alternative Entry

Salary A/c (prior period item)	Dr.	75,000	
To Bank A/c			75,000

(Salary related to 3 months i.e. January, 2017 to March 2017 paid in 2017-2018)

Salary A/c	Dr.	1,00,000	
To Bank A/c			1,00,000

(Salary related to 4 months paid on 1.8.2017 for April to July, 2017)

(ii) AS 5 inter alia states that the term 'prior period items' does not include other adjustments necessitated by circumstances, which though related to prior periods, are determined in the current period. Accordingly, in the second case though Shama was terminated on 1.1.2017 i.e. in 2016-2017, yet she was reinstated due to court's order in 2017-2018, with the instruction by the court to pay the salary for the intervening period i.e. with retrospective effect from January, 2017. The adjustment of salary of Rs. 75,000 (for January 2017 to March, 2017) would not be considered as prior period item and will be accounted for in the books as current year expense. Thus the entire amount of Salary of Rs. 1,75,000 for January, 2017 to July, 2017 is a current year expense only.

Salary A/c (Rs 25,000 x 7)	Dr.	1,75,000	
To Bank A/c			1,75,000

(Salary related to 7 months paid i.e. for the period 1.1.2017 to 31.7.2017)

5. State whether the following items are examples of change in Accounting Policy / Change in Accounting Estimates / Extraordinary items / Prior period items / Ordinary Activity :

(i) Actual bad debts turning out to be more than provisions.
(ii) Change from Cost model to Revaluation model for measurement of carrying amount of PPE.
(iii) Government grant receivable as compensation for expenses incurred in previous accounting period.
(iv) Treating operating lease as finance lease.
(v) Capitalisation of borrowing cost on working capital.
(vi) Legislative changes having long term retrospective application.
(vii) Change in the method of depreciation from straight line to WDV.
(viii) Government grant becoming refundable.
(ix) Applying 10% depreciation instead of 15% on furniture.
(x) Change in useful life of fixed assets.

Solution: Classification of given items is as follows:

Sr. No.	Particulars	Remarks
(i)	Actual bad debts turning out to be more than provisions	Change in Accounting Estimates
(ii)	Change from Cost model to Revaluation model for measurement of carrying amount of PPE	Change in Accounting Policy
(iii)	Government grant receivable as compensation for expenses incurred in previous accounting period	Extra -ordinary Items
(iv)	Treating operating lease as finance lease.	Prior- period Items

(v)	Capitalisation of borrowing cost on working capital	Prior-period Items (as interest on working capital loans is not eligible for capitalization)
(vi)	Legislative changes having long term retrospective application	Ordinary Activity
(vii)	Change in the method of depreciation from straight line to WDV	Change in Accounting Estimates
(viii)	Government grant becoming refundable	Extra -ordinary Items
(ix)	Applying 10% depreciation instead of 15% on furniture	Prior- period Items
(x)	Change in useful life of fixed assets	Change in Accounting Estimates

6. The Accountant of Mobile Limited has sought your opinion with relevant reasons, whether the following transactions will be treated as change in Accounting Policy or not for the year ended 31st March, 2021. Please advise him in the following situations in accordance with the provisions of relevant Accounting Standard;
   (i) Provision for doubtful debts was created @ 2% till 31st March, 2020. From the Financial year 2020-2021, the rate of provision has been changed to 3%.
   (ii) During the year ended 31st March, 2021, the management has introduced a formal gratuity scheme in place of ad-hoc ex-gratia payments to employees on retirement.
   (iii) Till the previous year the furniture was depreciated on straight line basis over a period of 5 years. From current year, the useful life of furniture has been changed to 3 years.
   (iv) Management decided to pay pension to those employees who have retired after completing 5 years of service in the organization. Such employees will get pension of Rs. 20,000 per month. Earlier there was no such scheme of pension in the organization.
   (v) During the year ended 31st March, 2021, there was change in cost formula in measuring the cost of inventories.

   Solution:
   (i) In the given case, Mobile limited created 2% provision for doubtful debts till 31st March, 2020. Subsequently in 2020-21, the company revised the estimates based on the changed circumstances and wants to create 3% provision. Thus change in rate of provision of doubtful debt is change in accounting estimate and is not a change in accounting policy. This change will affect only current year.
   (ii) As per AS 5, the adoption of an accounting policy for events or transactions that differ in substance from previously occurring events or transactions, will not be considered as a change in accounting policy. Introduction of a formal retirement gratuity scheme by an employer in place of ad hoc ex-gratia payments to employees on retirement is a transaction which is substantially different from the previous policy, will not be treated as change in accounting policy.
   (iii) Change in useful life of furniture from 5 years to 3 years is a change in accounting estimate and is not a change in accounting policy.
   (iv) Adoption of a new accounting policy for events or transactions which did not occur previously should not be treated as a change in an accounting policy. Hence the introduction of new pension scheme is not a change in accounting policy.
   (v) Change in cost formula used in measurement of cost of inventories is a change in accounting policy.

AS 7: CONSTRUCTION CONTRACTS

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

(Amount ₹ in lacs)

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

*Includes ₹ 100 lacs for standard materials stored at the site to be used in year 3 to complete the work.
**Excludes ₹ 100 lacs for standard material brought forward from year 2. The variation in cost and revenue in year 2 has been approved by customer.
Compute year wise amount of revenue, expenses, contract cost to complete and profit or loss to be recognized in the Statement of Profit and Loss as per AS-7 (revised).

Solution:

The amounts of revenue, expenses and profit recognized in the statement of profit and loss in three years are computed below: **(Amount in ₹ lakhs)**

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

Working Note:

	Year 1	***Year 2***	***Year 3***
Revenue after considering variations	9,000	9,200	9,200
Less: Estimated profit for wholecontract	950	1,000	1,000
Estimated total cost of the contract(A)	8,050	8,200	8,200
Actual cost incurred upto the reporting date (B)	2,093	6,068 (6,168-100)	8,200 (8,100+100)
Degree of completion (B/A)	26%	74%	100%

2. 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 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 the contract Rs. 6 crores
Escalation in cost by 5% and accordingly the contract price is increased by 5%.

You are required to ascertain the state of completion and state the revenue and profit to be recognised for the year as per AS-7.

Answer: ***As per AS 7 'Construction Contracts'*** the amount of revenue agreed in a fixed price contract may increase as a result of cost. So in the given question:

Contact price will be Rs. 12 crores plus 5%= Rs. 12.60 Crores

Percentage of completion method = (Actual cost/Total estimated cost) x100		
= 4 crores/10 crores	=	40%
Revenue to be recognised= (12crores+5%) =12.60crores X 40%	=	5.04 Crores
Less:- Actual cost has been incurred		(4.00) Crores
Profit recognised.		1.04 crores

3. Akar Ltd. Signed on 01/04/16, a construction contract for Rs 1,50,00,000.

Following particulars are extracted in respect of contract, for the period ending 31/03/17.

- Materials issued Rs. 75, 00,000
- Labour charges paid Rs. 36, 00,000
- Hire charges of plant Rs. 10,00,000
- Other contract cost incurred Rs.15,00,000
- Out of material issued, material lying unused at the end of period is Rs. 4,00,000
- Labour charges of Rs. 2,00,000 are still outstanding on 31.3.17.
- It is estimated that by spending further Rs. 33,50,000 the work can be completed in all respect.

You are required to compute profit/loss to be taken to profit & Loss Account and additional provision for foreseeable loss as per AS-7.

Answer:- As per AS-7, "Construction Contracts" profit/loss to be taken to profit & Loss Account and additional provision for foreseeable loss is calculated as follows:-

(i) **Calculation of % of Completion:-**

$$\frac{\text{Cost incurred upto date}}{\text{Total Estimated cost}} \text{x}100$$

$$\frac{13,40,0000}{1,67,50,000} \text{x}100 = 80\%$$

(1) Calculation the Total Cost Incurred upto date:

Material : Issued		75,00,000	
Less:- Closing		(4,00,000)	71,00,000
Labour :	Paid	36,00,000	
	+O/S	2,00,000	38,00,000
Hire Charges			10,00,000
Other cost incurred			15,00,000
			1,34,00,000

(2) Total Estimated Cost :-

Cost incurred upto date:	1,34,00,000
+Further estimated cost to be incurred	33,50,000
	1,67,50,000

(ii) Calculation of revenue to be recognized

Contract Price X % of Stage of completion = 80% x 1,50,00,000 = 1,20,00,000

(iii) Calculation of loss recognised on contract

Contract Revenue recognised	1,20,00,000
Less:- Total cost incurred	(1,34,00,000)
	14,00,000

(iv) Calculation of total expected loss on contract

Contract Price	1,50,00,000
Less:- Total estimated cost to be incurred	(1,67,50,000)
Total Expected loss on contract	17,50,000

(v) Calculation of provision for expected loss:-

Total Expected loss on contract	17,50,000
Less: Total loss recognised on contract	14,00,000
Provision for expected loss	3,50,000

(vi) Loss of 17,50,000 (14,00,000 + 3,50,000) is be to recognized immediately by debiting into profit & loss account.

4. Sarita Construction Co. obtained a contract for construction of a dam. The following details are available in records of company for the year ended 31st March, 2018:

	₹ In Lakhs
Total Contract Price	12,000
Work Certified	6,250
Work not certified	1,250
Estimated further cost to completion	8,750
Progress payment received	5,500
Progress payment to be received	1,500

Applying the provisions of Accounting Standard 7 "Accounting for Construction Contracts" you are required to compute:

(i) Profit/Loss for the year ended 31st March, 2018.
(ii) Contract work in progress as at end of financial year 2017-18.
(iii) Revenue to be recognized out of the total contract value.
(iv) Amount due from/to customers as at the year end.

Solution:

(i) Loss for the year ended, 31st March, 2018 **(₹ in lakhs)**

Amount of foreseeable loss	
Total cost of construction (6,250 + 1,250 + 8,750)	16,250
Less: Total contract price	(12,000)
Total foreseeable loss to be recognised as expense	4,250

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

Loss for the year ended, 31st March, 2018 amounting ₹ 4,250 will be recognized.

(ii) Contract work-in-progress as on 31.3.18(₹ in lakhs): Contract work-in-progress i.e. cost incurred to date are ₹ 7,500 lakhs:

Work certified	6,250
Work not certified	1,250
	7,500

(iii) Proportion of total contract value recognised as revenue

Cost incurred till 31.3.18 is 46.15% (7,500/16,250 X 100) of total costs of construction.

Proportion of total contract value recognised as revenue: 46.15% of ₹ 12,000 lakhs = ₹ 5,538 lakhs

(iv) Amount due from/to customers at year end

(Contract costs + Recognised profits – Recognised Losses) – (Progress payments received + Progress payments to be received)

= (7,500 + Nil – 4,250) – (5,500 + 1,500) ₹ in lakhs

= [3,250 – 7,000] ₹ in lakhs Amount due to customers

= ₹ 3,750 lakhs

5. AP Ltd., a construction contractor, undertakes the construction of commercial complex for Kay Ltd. AP Ltd. submitted separate proposals for each of 3 units of commercial complex. A single agreement is entered into between the two parties. The agreement lays down the value of each of the 3 units, i.e. Rs. 50 Lakh, Rs. 60 Lakh and Rs. 75 Lakh respectively. Agreement also lays down the completion time for each unit.

Comment, with reference to AS-7, whether AP Ltd., should treat it as a single contract or three separate contracts.

Solution:

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

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

In the given case, each unit is submitted as a separate proposal, 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 AP 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.

AS 9: REVENUE RECOGNITION

1. Sarita Publications publishes a monthly magazine on the 15th of every month. It sells advertising space in the magazine to advertisers on the terms of 80% sale value payable in advance and the balance within 30 days of the release of the publication. The sale of space for the March 2014 issue was made in February 2014. The magazine was published on its scheduled date. It received Rs. 2,40,000 on 10.3.2014 and Rs. 60,000 on 10.4.2014 for the March 2014 issue. Discuss in the context of AS 9 the amount of revenue to be recognized and the treatment of the amount received from advertisers for the year ending 31.03.2014. What will be the treatment if the publication is delayed till 02.04.2014.

Answer:-As per AS – 9 ,"Revenue Recognition" Revenue from a transaction involving the sale of goods is recorded when the transfer of significant risks and rewards of ownership with ownership is transferred to the buyer . Further there should be certainty of collection and consideration.

In the given case Sarita Publications recorded the sale of Rs. 3,00,000 in the year ended 31/03/2014. And advance received Rs. 2,40,000 is adjusted with sale value and balance due Rs. 60,000 is shown as trade receivable.

If the publication is continued or delayed till 02/04/2014 then revenue should not be recognised and advance of Rs. 2,40,000 should be shown as advance from customer as current liability.

2. Moon Ltd. entered into agreement with Sun Ltd. for sale of goods of Rs. 8 lakhs at a profit of 20% on cost. The sale transaction took place on 1st February, 2011. On the same day Sun Ltd. entered into another agreement with Moon Ltd. to resell the same goods at Rs. 10.80 lakhs on 1st August, 2011. State the treatment of this transaction in the financial statements of Moon Ltd. as on 31.03.11. The pre-determined re-selling price covers the holding cost of Sun Ltd.

Give the Journal Entries as on 31.03.11 in the books of Moon Ltd.

Answer: In the given case, Moon Ltd. concurrently agreed to repurchase the same goods from Sun Ltd. on 1st Feb., 2011. Also the re-selling price is pre-determined and covers purchasing and holding costs of Sun Ltd. Hence, the transaction between Moon Ltd. and Sun Ltd. on 1st Feb., 2011 should be accounted for as financing rather than sale. The resulting cash flow of Rs. 9.60 lakhs received by Moon Ltd., cannot be considered as revenue as per AS 9 "Revenue Recognition".

Journal Entries in the books of Moon Ltd.

(Rs. in lakhs)

1.02.11	Bank Account	Dr.	9.60	
	To Advance from Sun Ltd*.			9.60
	(Being advance received from Sun Ltd amounting [Rs. 8 lakhs + 20% of Rs. 8 lakhs= 9.60 lakhs] under sale and re-purchase agreement)			
31.03.11	Financing Charges Account	Dr.	0.40	
	To Sun Ltd.			0.40
	(Financing charges for 2 months at Rs. 1.20 lakhs [10.80 – 9.60] i.e. 1.2 lakhs x 2/6)			
31.03.11	Profit and Loss Account	Dr.	0.40	
	To Financing Charges Account			0.40
	(Being amount of finance charges transferred to P& L Account)			

* The balance of Sun Ltd. account will be disclosed as an advance under the heading liabilities in the balance sheet of Moon Ltd. as on 31st March, 2011.

3. Raj Ltd. entered into an agreement with Heena Ltd. to dispatch goods- valuing Rs 5, 00,000 every month for next 6 months on receipt of entire payment. Heena Ltd. accordingly made the entire payment of Rs. 30,00,000 and Raj Ltd. started dispatching the goods. In fourth month, due to fire in premise of Heena Ltd., Henna Ltd. requested to Raj Ltd. not to dispatch goods untill further notice. Due to this, Raj Ltd. is holding the remaining goods worth Rs 15, 00,000 ready for dispatch. Raj Ltd. accounted Rs 15, 00,000 as sales and transferred the balance to Advance received against Sales account. Comment upon the above treatment by Raj Ltd. with reference to the provision of AS -9.

Answer:- As per AS-9, "Revenue recognition" In a transaction involving the sale of goods, performance should be regarded as being achieved when the following conditions have been fulfilled:

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

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

Further as per Point 1 of Appendix of AS-9 Revenue should be recognised notwithstanding that physical delivery has not been completed so long as there is every expectation that delivery will be made. However, the item must be on hand, identified and ready for delivery to the buyer at the time the sale is recognised rather than there being simply an intention to acquire or manufacture the goods in time for delivery.

In the given case, transfer of property in goods results in or coincides with the transfer of significant risk and rewards of ownership to the buyer. Also, the sale price has been recovered by the seller. Hence, the sale is complete but delivery has been postponed at buyer's request. A Ltd. should be recognized the entire sale of Rs. 30,00,000 (Rs.5,00,000 x6) and no part of the same is to be treated as Advance Receipt against Sales.

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

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

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

Solution:

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

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

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

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

(ii) No significant uncertainty exists regarding the amount of the consideration that will be derived from the sale of the goods. AS 9 also provides that in case of retail sales offering a guarantee of 'money back, if not completely satisfied, it may be appropriate to recognize the sale but to make a suitable provision for returns based on previous experiences.

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

Working Note:

Calculation of Profit % on sales	**(Rs. in lacs)**
Sales for the year	400
Less: Cost of sales	(320)
Profit	80

Profit mark up on sales (80/400) x 100 = 20%

5. Given the following information of M/s. paper Products Ltd.
   (i) Goods of Rs 60,000 were sold on 20-3-2015 but at the request of the buyer these were delivered on10-4-2015.
   (ii) On 15-1-2015 goods of Rs 1,50,000 were sent on consignment basis of which 20%of the goods unsold are lying with the consignee as on 31-3-2015.
   (iii) Rs 1,20,00 worth of goods were sold on approval basis on 1-12-2014 The period of approval was 3 months after which they were considered sold Buyer sent approval for 75%goods up to 31-1-2015 and no approval or disapproval received for the remaining goods till 31-3-2015.
   (iv) Apart from the above, the company has made cash sales of Rs. 7,80,000(Gross) Trade discount of 5%was allowed on the cash sales.

   You are required to advise the accountant of M/s. Paper products Ltd. with valid reasons the amount to be recognized as revenue in above cases in the context of As 9 and also determine the total revenue to be recognized for the year ending 31-3-2015.

   Solution:- Calculation of total revenue Recognised as Per AS-9

Particulars	**Amount(Rs.)**
Case I:- Sale is recorded because Risk and Rewards has been transferred.	60,000
Case II:- Sale should be recorded upto 80% (1,50,000*80%)	1,20.000
Case III:- Since period of approval has expired so whole sale should be recorded.	1,20,000
Case IV:- Trade Discount shall be adjusted in cash sale (Rs. 7,80,000-5%)	7,41,000
Total Revenue to be recognized	Rs.10,41,000

6. Zigato runs a food-delivery business. As per the arrangement, Zigato allows customers to order food from local restaurants and is responsible the delivery of the food within stipulated time. During a particular year, it collects the money on orders made online as under:

Total price for the food item	-	₹ 200 lakhs
Delivery charges	-	₹ 60 lakhs
GST	-	₹ 40 lakhs
Total	-	₹ 300 lakhs

Zigato has received ₹ 300 lakhs for the above orders from customers and the orders were delivered to the customer in stipulated time.

How much revenue should be recognised by restaurants and how much revenue should be recognised by Zigato for the year?

Solution: The risks and rewards associated with the food item are not with Zigato. When a customer has ordered a food item, whether the item will be prepared or not is the responsibility of the restaurant and not Zigato. Similarly, the responsibility to deliver the food item is with Zigato and the restaurant does not undertake responsibility for the same.

Therefore, the restaurant undertakes the principal's responsibility to prepare the food and ensure its quality. Zigato, on the other hand, is only responsible to deliver the food. Thus, Zigato is acting as an agent. Hence, it can only recognize revenue relating to that activity (which it does in the ordinary course of business). The revenue for Zigato, therefore, is ₹ 60 lakhs, whereas, the revenue for restaurants will be ₹ 200 lakhs.

It may be noted that the GST of ₹ 40 lakhs is a liability payable to the Government (third party), hence it does not form part of revenue.

7. For the year ended 31st March 20X1, KY Enterprises has entered into the following transactions.

On 31 March 20X1, KY supplied two machines to its customer ST. Both machines were accepted by ST on 31 March 20X1. Machine 1 was a machine that was routinely supplied by KY to many customers and the installation process was very simple.

Machine 1 was installed on 2 April 20X1 by ST's employees.

Machine 2 being more specialised in nature requires an installation process which is more complicated, requiring significant assistance from KY. Machine 2 was installed between 2 and 5 April 20X1.

Details of costs and sales prices are as follows:

	Machine 1	Machine 2
Sale Price	3,20,000	3,00,000
Cost of production	1,60,000	1,50,000
Installation fee	nil	10,000

How should above transactions be recognized by KY Enterprises for the year ended 31st March 20X1?

Solution:

Machine 1: As the installation process is simple, revenue from Machine 1 will be recognized on 31 March 20X1.

Revenue (Machine 1)	₹ 3,20,000
Cost of Goods Sold	₹ 1,60,000
Profit during the period	₹ 1,60,000

Since the question specifies that the machine is already accepted by ST on 31 March 20X1, the revenue arising from sale of the machine needs to be recognized for the year ending 31 March 20X1. This is because acceptance of the machine indicates that the risks and rewards pursuant to the ownership are transferred to ST.

Machine 2: Installation process for Machine 2 is more complicated, requiring significant assistance from KY Ltd. However, question specifies that the machine is already accepted by ST on 31 March 20X1. Assuming that there is no further approval/acceptance required from the buyer for the Machine sold, revenue from sale of Machine 2 can be recognized for the year ending 31 March 20X1.

Revenue (Machine 2)	₹ 3,00,000
Cost of Goods Sold	₹ 1,50,000
Profit during the period	₹ 1,50,000

However, installation fee which is for rendering installation services cannot be recognized until the installation is complete. Since the machine is pending installation, the revenue in respect of installation charges ₹10,000 needs to be recognized on 5 April 20X1 once the installation process gets completed.

AS 10: PROPERTY, PLANT AND EQUIPMENT

1. ABC Ltd. Is installing a new plant at its production facility It has incurred these costs:

1.	Cost of the plant (cost per supplier's invoice plus taxes	Rs 25,00,000
2	Initial delivery and handing costs	Rs2,00,000
3	Cost of site preparation	Rs 6,00,000
4	Consultants used for advice on the acquisition of the plant	Rs 7,00,000
5	Interest charges paid to supplier of plant for deferred credit	Rs 2,00,000
6	P.V. of estimated dismantling costs to be incurred after7years	Rs 3,00,000
7	Operating losses before commercial production	Rs 4,00,000

Please advise ABC Ltd. On the costs that can be capitalized in accordance with AS 10 (Revised)

Answer: According to AS 10 (Revised), these costs can be capitalized:

1	Cost of the plant	Rs 25,00,000
2	Initial delivery and handling costs	Rs2,00,000
3	Cost of site preparation	Rs 6,00,000
4	Consultants ,fees	Rs 7,00,000
5	P.V. of estimated dismantling costs to be incurred after 7 years	Rs3,00,000
		Rs 43,00,000

Note: Interest charges paid on "Deferred credit terms" to the supplier of the plant(not a qualifying asset) of Rs 2,00,000 and operating losses before commercial production amounting to Rs 4,00,000 are not regarded as directly attributable costs and thus cannot be capitalized. They should be written off to the Statement of profit and Loss in the period they are incurred.

2. Shrishti Ltd. contracted with a supplier to purchase machinery which is to be installed in its Department A in three months' time. Special foundations were required for the machinery which were to be prepared within this supply lead time. The cost of the site preparation and laying foundations were Rs. 1,41,870. These activities were supervised by a technician during the entire period, who is employed for this purpose of Rs. 45,000 per month. The technician's services were given by Department B to Department A, which billed the services at Rs. 49,500 per month after adding 10% profit margin.
The machine was purchased at ₹1,58,34,000 inclusive of IGST@12% for which input credit is available to Shrishti Ltd. Rs. 55,770 transportation charges were incurred to bring the machine to the factory site. An Architect was appointed at a fee of Rs. 30,000 to supervise machinery installation at the factory site.
Ascertain the amount at which the Machinery should be capitalized under AS 10 considering that IGST credit is availed by the Shristhi Limited. Internally booked profits should be eliminated in arriving at the cost of machine.
Solution: Calculation of Cost of Fixed Asset (i.e. Machinery)

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

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

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

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

Solution: As per provisions of AS 10, any cost directly attributable to bring the assets to the location and conditions necessary for it to be capable of operating in the manner indicated by the management are called directly attributable costs and would be included in the costs of an item of PPE.
Management of Neon Enterprise should capitalize the costs of construction and remodelling the restaurant, because they are necessary to bring the restaurant to the condition necessary for it to be capable of operating in the manner intended by management. The restaurant cannot be opened without incurring the construction and remodelling expenditure amounting ₹ 30,00,000 and thus the expenditure should be considered part of the asset.
However, the cost of salaries of staff engaged in preparation of restaurant ₹ 7,50,000 before its opening are in the nature of operating expenditure that would be incurred if the restaurant was open and these costs are not necessary to bring the restaurant to the conditions necessary for it to be capable of operating in the manner intended by management. Hence, ₹ 7,50,000 should be expensed.

4. **With reference to AS-10, classify the 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.

ITEMS

(1) Import duties and non-refundable purchase taxes.
(2) Initial delivery and handling costs.
(3) Costs of testing whether the asset is functioning properly, after deducting the net proceeds.
(4) Initial operating losses, such as those incurred while demand for the output of an item builds up.
(5) Costs incurred while an item capable of operating in the manner intended by management has yet to be brought into use or is operated at less than full capacity.
(6) Trade discounts and rebates.
(7) Costs of relocating or reorganizing part or all of the operations of an enterprise.
(8) Installation and assembly costs.
(9) Cost of site preparation.
(10) Administration and other general overhead costs.

Solution:

Heads

(i) Purchase price of PPE
(ii) Directly attributable cost of PPE
(iii) Cost not included in determining the carrying amount of an item of PPE

S. N.	Items	Classified under Head
1	Import duties and non-refundable purchase taxes	(i)
2	Initial delivery and handling costs	(ii)
3	Costs of testing whether the asset is functioning properly, after deducting the net proceeds*	(ii)
4	Initial operating losses, such as those incurred while demand for the output of an item builds up	(iii)
5	Costs incurred while an item capable of operating in the manner intended by management has yet to be brought into use or is operated at less than full capacity.	(iii)
6	Trade discounts and rebates (deducted for computing purchase price)	(i)
7	Costs of relocating or reorganizing part or all of the operations of an enterprise.	(iii)
8	Installation and assembly costs	(ii)
9	Costs of site preparation	(ii)
10	Administration and other general overhead costs	(iii)

*Considered that this cost of testing is after deducting net proceeds from selling any items produced while bringing the asset to that location and condition otherwise if the net proceeds are after fixing the asset to its location and condition (asset ready for use), it will be classified under category (iii) i.e. Cost not included in determining the carrying amount of an item of PPE.

5. RS Ltd. has acquired a heavy plant at a cost of ₹ 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 ₹ 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 ₹ 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?

Solution:

Recognition of Asset: The new boiler will produce economic benefits to RS Ltd. & 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	₹ 2,00,00,000
Less: Accumulated depreciation [(2,00,00,000 /10) x 2]	₹ 40,00,000
Carrying value of the plant after two years	₹ 1,60,00,000
Less: Current Cost of Old Boiler to be derecognized	
i.e. WDV of Boiler (replaced) after 2 years (50,00,000/10 x 8)	40,00,000
	1,20,00,000
Add: Cost of new Boiler to be recognized	60,00,000
Revised carrying amount of Plant	1,80,00,000

6. A Ltd. had following assets. Calculate depreciation for the year ended 31st March, 2020 for each asset as per AS 10 (Revised):
   (i) Machinery purchased for ₹ 10 lakhs on 1st April, 2015 and residual value after useful life of 5 years, based on 2015 prices is ₹ 10 lakhs.
   (ii) Land for ₹ 50 lakhs.
   (iii) A Machinery is constructed for ₹ 5,00,000 for its own use (useful life is 10 years). Construction is completed on 1st April, 2019, but the company does not begin using the machine until 31st March, 2020.
   (iv) Machinery purchased on 1st April.2017 for ₹ 50,000 with useful life of 5 years and residual value is NIL. On 1st April, 2019, management decided to use this asset for further 2 years only.

Solution: Computation of amount of depreciation as per AS 10

		₹
(i)	**Machinery purchased on 1/4/15 for ₹ 10 lakhs (having residual value of ₹ 10 lakhs)** **Reason:** The company considers that the residual value, based on prices prevailing at the balance sheet date, will equal the cost. Therefore, there is no depreciable amount and depreciation is correctly zero.	Nil
(ii)	**Land (50 lakhs) (considered freehold)** **Reason:** Land has an unlimited useful life and therefore, it is not depreciated.	Nil
(iii)	**Machinery constructed for own use (₹ 5,00,000/10)** **Reason:** The entity should begin charging depreciation from the date the machine is ready for use i.e. 1st April,2019. The fact that the machine was not used for a period after it was ready to be used is not relevant in considering when to begin charging depreciation.	50,000
(iv)	**Machinery having revised useful life** **Reason:** The entity has charged depreciation using the straight-line method at ₹ 10,000 per annum i.e (50,000/5 years). On 1st April,2019 the asset's net book value is [50,000 – (10,000 x 2)] i.e. ₹ 30,000. The remaining useful life is 2 years as per revised estimate. The company should amend the annual provision for depreciation to charge the unamortized cost over the revised remaining life of 2 years. Consequently, it should charge depreciation for the next 2 years at ₹ 15,000 per annum i.e. (30,000 / 2 years).	15,000

7. In the books of Optic Fiber Ltd., plant and machinery stood at Rs. 6,32,000 on 1.4.2013. However on scrutiny it was found that machinery worth Rs. 1,20,000 was included in the purchase on 1.6.2013. On 30.6.2013 the company disposed a machine having book value of Rs. 1,89,000 on 1.4.2013 at Rs. 1,75,000 in part exchange of a new machine costing Rs. 2,56,000. The company charges depreciation @20% WDV on plant and machinery.
You are required to calculate :

(i) Depreciation to be charged to P/L
(ii) Book Value of Plant and Machinery A/c as on 31.3.2014
(iii) Loss on exchange of machinery .

Solution:

(i) Total Depreciation to be charged in the Profit and Loss Account	**Rs.**
Depreciation on old machinery in use [20% of (6,32,000-1,89,000)]	88,600
Add: Depreciation on machine included in purchase @ 20% of Rs.1,20,000 for 10 months	20,000
Add: Depreciation on new machine @ 20% of Rs. 2,56,000 for 9 months	38,400
Add: Depreciation on machine disposed of (20% on Rs. 1,89,000 for 3 months)	9,450
Total depreciation to be charged in Profit and Loss A/c	1,56,450

(ii) Book Value of Machinery in the Balance Sheet as on 31.03.2014	**Rs.**
Opening Balance	6,32,000
Less: Book value of machine sold	(1,89,000)
Add: Purchase of new machine	2,56,000
Add: Machinery included in purchase	1,20,000
Less: Depreciation on machinery in use (88,600+20,000+38,400)	(1,47,000)
	6,72,000

(iii) Loss on Exchange of Machine	**Rs.**
Book value of machine as on 1.4.2013	1,89,000
Less: Depreciation for 3 months @ 20%	(9,450)
Written Down Value as on 30.6.2013	1,79,550
Less: Exchange value	(1,75,000)
Loss on exchange of machine	4,550

8. Star Limited purchased machinery for ₹ 6,80,000 (inclusive of GST of ₹ 40,000). Input credit is available for entire amount of GST paid. The company incurred the following other expense for installation.

	₹
Cost of preparation of site for installation	21,200
Total Labour charges (200 out of the total of 500 men hours worked, were spent on installation of the machinery)	56,000
Spare parts and tools consumed in installation	5,000
Total salary of supervisor (Time spent for installation was 25% of the total time worked)	26,000
Total administrative expense (1/10 relates to the plant installation)	34,000
Test run and experimental production expenses	18,000
Consultancy charges to architect for plant set up	11,000
Depreciation on assets used for installation	12,000

The machine was ready for use on 15.01.2021 but was used from 01.02.2021. Due to this delay further expenses of ₹ 8,900 were incurred. Calculate the value at which the plant should be capitalized in the books of Star Limited.

Solution: Calculation of Cost of Plant

Particulars		**₹**
Purchase Price	Given	6,80,000
Add: Site Preparation Cost	Given	21,200
Labour charges (56,000×200/500)	Given	22,400
Spare parts		5,000
Supervisor's Salary	25% of ₹ 26,000	6,500

Administrative costs	1/10 of ₹ 34,000	3,400
Test run and experimental production charges	Given	18,000
Architect Fees for set up	Given	11,000
Depreciation on assets used for installation	Given	12,000
Total Cost of Asset		7,79,500
Less: GST credit receivable		(40,000)
Value to be capitalized		7,39,500

Note: Further Expenses of ₹ 8,900 from 15.1.2021 to 1.2.2021 to be charged to profit and loss A/c as plant was ready for production on 15.1.2021.

9. Skanda Ltd. acquired a machinery for ₹ 2,50,00,000 five years ago. Depreciation was charged at 10% p.a. on SLM basis, useful life being 10 years. At the beginning of Year 3, the machinery was revalued to ₹ 3,00,00,000 with the surplus on revaluation being credited to Revaluation Reserve. Depreciation was provided on the revalued amount over the balance useful life of 8 years. The machinery was sold in the current year for ₹ 1,12,50,000. Give the accounting treatment for the above in the Company's accounts. What will be the treatment if the machinery fetched only ₹ 42,50,000 now?

Particulars	**₹**
Original Cost of the Asset	2,50,00,000
Less: Depreciation for 2 years (₹ 2,50,00,000 x 10% x 2 years)	50,00,000
Book Value at the beginning of Year 3	2,00,00,000
Add: Revaluation Surplus (balancing figure)	1,00,00,000
Revalued Amount as given (= revised depreciable value)	3,00,00,000
Less: Depreciation for Years 3-5 (₹ 3,00,00,000 ÷ 8 yrs x 3 yrs)	1,12,50,000
Carrying Amount at the end of Year 5	**1,87,50,000**

The treatment of Gain / Loss on Disposal / Revaluation is as below:

Particulars	Disposal Proceeds = ₹ 1,12,50,000	Disposal Proceeds = ₹ 42,50,000
Book Value Less Disposal Proceeds	₹ 1,87,50,000 – ₹ 1,12,50,000	₹ 1,87,50,000 – ₹ 42,50,000
= Loss recognized in Profit or Loss	= ₹ 75,00,000 (Loss)	= ₹ 1,45,00,000 (Loss)
Revaluation Surplus directly transferred to Retained Earnings	₹ 1,00,00,000	₹ 1,00,00,000

10. On 1 April 20X1, Sun ltd purchased some land for ₹ 10 million (including legal costs of ₹ 1 million) in order to construct a new factory. Construction work commenced on 1 May 20X1. Sun ltd incurred the following costs in relation with its construction:
- Preparation and levelling of the land – ₹ 3,00,000.
- Purchase of materials for the construction – ₹ 6.08 million in total.
- Employment costs of the construction workers – ₹ 2,00,000 per month.
- Overhead costs incurred directly on the construction of the factory – ₹ 1,00,000 per month.
- Ongoing overhead costs allocated to the construction project using the company's normal overhead allocation model – ₹ 50,000 per month.
- Income received during the temporary use of the factory premises as a car park during the construction period – ₹ 50,000.
- Costs of relocating employees to work at the new factory – ₹ 300,000.
- Costs of the opening ceremony on 31 January 20X1 – ₹ 150,000.

The factory was completed on 30 November 20X1 and production began on 1 February 20X2. The overall useful life of the factory building was estimated at 40 years from the date of completion. However, it is estimated that the roof will need to be replaced 20 years after the date of completion and that the cost of replacing the roof at current prices would be 30% of the total cost of the building.

At the end of the 40 -year period, Sun ltd has a legally enforceable obligation to demolish the factory and restore the site to its original condition. The directors estimate that the cost of demolition in 40 years' time (based on prices prevailing at that time) will be ₹ 20 million. An annual risk adjusted discount rate which is appropriate to this project is 8%. The present value of ₹ 1 payable in 40 years' time at an annual discount rate of 8% is Rs. 0.046.

The construction of the factory was partly financed by a loan of ₹ 17.5 million taken out on 1 April 20X1. The loan was at an annual rate of interest of 6%. During the period 1 April 20X1 to 31 August 20X1 (when the loan proceeds had been fully utilised to finance the construction), Sun Ltd received investment income of ₹ 100,000 on the temporary investment of the proceeds.

Required: Compute the carrying amount of the factory in the Balance Sheet of Sun Ltd at 31 March 20X2. You should explain your treatment of all the amounts referred to in this part in your answer.

Solution: Computation of the cost of the factory

Description	**Included in PPE Rs 000**	**Explanation**
Purchase of land	10,000	Both the purchase of the land and the associated legal costs are direct costs of constructing the factory.
Preparation and leveling	300	A direct cost of constructing the factory
Materials	6,080	A direct cost of constructing the factory
Employment costs of construction workers	1,400	A direct cost of constructing the factory for a seven-month period
Direct overhead costs	700	A direct cost of constructing the factory for a seven-month period
Allocated overhead costs	Nil	Not a direct cost of construction
Income from use as a car park	Nil	Not essential to the construction so recognised directly in profit or loss
Relocation costs	Nil	Not a direct cost of construction
Opening ceremony	Nil	Not a direct cost of construction
Finance costs	612.5	Capitalise the interest cost incurred in a seven-month period (purchase of land would not trigger off capitalisation since land is not a qualifying asset. Infact, the construction started from 1st May, 20X1)
Investment income on temporary investment of the loan proceeds	(100)	offset against the amount capitalized
Demolition cost recognised as a provision	920	Where an obligation must recognise as part of the initial cost
Total	19,912.50	

Computation of accumulated depreciation and Carrying Amount

Total depreciable amount	9,912.50	All of the net finance cost of 512.50 (612.50 – 100) has been allocated to the depreciable amount. Also acceptable to reduce by allocating a portion to the non- depreciable land element principle
Depreciation must be in two parts: Depreciation of roof component Depreciation of remainder	 49.56 57.82	 9,912.50 x 30% x 1/20 x 4/12 9,912.50 x 70% x 1/40 x 4/12
Total depreciation	107.38	
Computation of carrying amount	19,805.12	19,912.50 – 107.38

AS 11: THE EFFECTS OF CHANGES IN FOREIGN EXCHANGE RATES

1. A company had imported raw materials worth US Dollars 6,00,000 on 5th January, 2005, when the exchange rate was Rs.43 per US Dollar. The company had recorded the transaction in the books at the above mentioned rate. The payment for the import transaction was made on 5th April, 2005 when the exchange rate was Rs.47 per US Dollar. However, on 31st March, 2005, the rate of exchange was Rs.48 per US Dollar. The company passed an entry on 31st March, 2005 adjusting the cost of raw materials consumed for the difference between Rs.47 and Rs.43 per US Dollar.
In the background of the relevant accounting standard, is the company's accounting treatment correct? Discuss.
Answer: As per AS 11 (revised 2003), 'The Effects of Changes in Foreign Exchange Rates', monetary items denominated in a foreign currency should be reported using the closing rate at each balance sheet date. The effect of exchange difference should be taken into profit and loss account. Sundry creditors is a monetary item, hence should be valued at the closing rate i.e, Rs.48 at 31st March, 2005 irrespective of the payment for the same subsequently at lower rate in the next financial year. The difference of Rs.5 (48 -43) per US dollar should be shown as an exchange loss in the profit and loss account for the year ended 31st March, 2005 and is not to be adjusted against the cost of raw- materials. In the subsequent year, the company would record an exchange gain of Re.1 per US dollar, i.e., the difference between Rs.48 and Rs.47 per Us dollar. Hence, the accounting treatment adopted by the company is incorrect.

2. ABC Ltd. borrowed US $ 5,00,000 on 01/01/2017, which was repaid as on 31/07/2017. ABC Ltd. prepares financial statement ending on 31/03/2017. Rate of Exchange between reporting currency (INR) and foreign currency (USD) on different dates are as under:

01/01/2017	1 US$ =	₹ 68.50
31/03/2017	1 US $ =	₹ 69.50
31/07/2017	1 US $ =	₹ 70.00

You are required to pass necessary journal entries in the books of ABC Ltd. as per AS 11.
Solution:

Journal Entries in the Books of ABC Ltd.

Date	Particulars	₹ (Dr.)	₹ (Cr.)
Jan. 01, 2017	Bank Account (5,00,000 x 68.50) Dr.	342,50,000	
	To Foreign Loan Account		342,50,000
Mar. 31, 2017	Foreign Exchange Difference Account Dr.	5,00,000	
	To Foreign Loan Account [5,00,000 x (69.50-68.50)]		5,00,000
Jul. 31, 2017	Foreign Exchange Difference Account [5,00,000 x (70-69.5)] Dr.	2,50,000	
	Foreign Loan Account Dr.	347,50,000	
	To Bank Account		350,00,000

3. Rau Ltd. purchased a plant for US$ 1,00,000 on 01st February 2012, payable after three months. Company entered into a forward contract for three months @ Rs. 49.15 per dollar. Exchange rate per dollar on 01st Feb. was Rs. 48.85. How will you recognize the profit or loss on forward contract in the books of Rau Ltd.
Solution

Forward Rate	Rs. 49.15
Less: Spot Rate	(Rs. 48.85)
Premium on Contract	Rs. 0.30
Contract Amount US$	1,00,000
Total Loss (1,00,000 x 0.30)	Rs. 30,000

Contract period 3 months
Two falling the year 2012-13; therefore loss to be recognized (30,000/3) x 2 = Rs. 20,000.Rest Rs. 10,000 will be recognized in the following year.

4. Mr. A bought a forward contract for three months of US$ 1,00,000 on 1st December at 1 US$ = Rs. 47.10 when exchange rate was US$ 1 = Rs. 47.02. On 31st December when he closed his books exchange rate was US$ 1 = Rs. 47.15. On 31st January, he decided to sell the contract at Rs. 47.18 per dollar. Show how the profits from contract will be recognized in the books
Answer: Since the forward contract was for speculation purpose the premium on contract i.e. the difference between the spot rate and contract rate will not be recorded in the books. Only when the contract is sold the difference between the contract rate and sale rate will be recorded in the Profit and Loss Account.

Sale Rate	Rs. 47.18
Less: Contract Rate	(Rs. 47.10)
Premium on Contract	Rs. 0.08
Contract Amount	US$ 1,00,000
Total Profit (1,00,000 x 0.08)	Rs. 8,000

5. Shan Builders Limited has borrowed a sum of US $ 10,00,000 at the beginning of Financial Year 2019-20 for its residential project at 4 %. The interest is payable at the end of the Financial Year. At the time of availment, exchange rate was Rs. 56 per US $ and the rate as on 31st March, 2020 Rs. 62 per US $. If Shan Builders Limited had borrowed the loan in India in Indian Rupee equivalent, the pricing of loan would have been 10.50%. You are required to compute Borrowing Cost and exchange difference for the year ending 31st March, 2020 as per applicable Accounting Standards.
Solution:
(i) Interest for the period 2019-20 = US $ 10 lakhs x 4% × Rs. 62 per US $ = Rs. 24.80 lakhs
(ii) Increase in the liability towards the principal amount=US $ 10 lakhs × Rs.(62 - 56)=Rs.60 lakhs
(iii) Interest that would have resulted if the loan was taken in Indian currency
= US $ 10 lakhs × Rs. 56 x 10.5% = Rs. 58.80 lakhs
(iv) Difference between interest on local currency borrowing and foreign currency borrowing
= Rs. 58.80 lakhs - Rs. 24.80 lakhs = Rs. 34 lakhs.
Therefore, out of Rs. 60 lakhs increase in the liability towards principal amount, only Rs. 34 lakhs will be considered as the borrowing cost. Thus, total borrowing cost would be Rs. 58.80 lakhs being the aggregate of interest of Rs. 24.80 lakhs on foreign currency borrowings plus the exchange difference to the extent of difference between interest on local currency borrowing and interest on foreign currency borrowing of Rs. 34 lakhs. Hence, Rs. 58.80 lakhs would be considered as the borrowing cost to be accounted for as per AS 16 "Borrowing Costs" and the remaining Rs. 26 lakhs (60-34) would be considered as the exchange difference to be accounted for as per AS 11 "The Effects of Changes in Foreign Exchange Rates".

6. Explain briefly the accounting treatment needed in the following cases as per AS 11 as on 31.3. 20X1.
Trade receivables include amount receivable from Umesh Rs. 5,00,000 recorded at the prevailing exchange rate on the date of sales, transaction recorded at US $ 1= Rs.58.50.
Long term loan taken from a U.S. Company, amounting to Rs. 60,00,000. It was recorded at US $ 1= Rs 55.60, taking exchange rate prevailing at the date of transaction. US $ 1=Rs.61.20 was on 31.3. 20X1.
Solution: 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 recognised as income or as expenses in the period in which they arise.
However, at the option of an entity, exchange differences arising on reporting of long-term foreign currency monetary items at rates different from those at which they were initially recorded during the period, or reported in previous financial statements, in so far as they relate to the acquisition of a non-depreciable capital asset can be accumulated in a "Foreign Currency Monetary Item Translation Difference Account" in the enterprise's financial statements and amortised over the balance period of such long-term asset/ liability, by recognition as income or expense in each of such periods.

Trade receivables	**Foreign Currency Rate**	**Rs.**
Initial recognition US $8,547 (5,00,000/58.50)	1 US $ = Rs. 58.50	5,00,000
Rate on Balance sheet date	1 US $ = Rs. 61.20	
Exchange Difference Gain US $ 8,547 X (61.20-58.50)		23,077
Treatment:		
Debit trade receivable		
And Credit Profit and Loss A/c by Rs. 23,077		
Long term Loan		
Initial recognition US $ 1,07,913.67 (60,00,000/55.60)	1 US $ = Rs. 55.60	60,00,000
Rate on Balance sheet date	1 US $ = Rs. 61.20	
Exchange Difference Loss US $ 1,07,913.67 X (61.20 – 55.60)		6,04,317
Treatment:		
Credit Loan A/c		
And Debit Profit and Loss A/c by Rs. 6,04,317		

Thus Exchange Difference on Long term loan amounting ₹ 6,04,317 may either be charged to Profit and Loss A/c or to Foreign Currency Monetary Item Translation Difference Account but exchange difference on debtors amounting ₹ 23,077 is required to be transferred to Profit and Loss A/c.

AS 12: ACCOUNTING FOR GOVERNMENT GRANTS

1. Darshan Ltd. purchased a Machinery on 1st April, 2016 for ₹ 130 lakhs (Useful life is 4 years). Government grant received is ₹ 40 lakhs for the purchase of above Machinery.
   Salvage value at the end of useful life is estimated at ₹ 60 lakhs. Darshan Ltd. decides to treat the grant as deferred income.
   Your are required to calculate the amount of depreciation and grant to be recognized in profit & loss account for the year ending 31st March, 2017, 31st March, 2018, 31st March, 2019 and 31st March, 2020.
   Darshan Ltd. follows straight line method for charging depreciation.
   Solution: As per 12 "Accounting for government grants", grants related to depreciable assets, if treated as deferred income are recognized in the profit and loss statement on a systematic and rational basis over the useful life of the asset.
   Amount of depreciation and grant to be recognized in the profit and loss account each year

Depreciation per year:	**₹in lakhs**
Cost of the Asset	130
Less: Salvage value	(60)
	70
Depreciation per year (70lakhs / 4)	17.50

₹ 17.50 Lakhs depreciation will be recognized for the year ending 31st March, 2017, 31st March, 2018, 31st March, 2019 and 31st March, 2020.
Amount of grant recognized in Profit & Loss account each year: 40 lakhs /4 years = ₹ 10 Lakhs for the year ending 31st March, 2017, 31st March, 2018, 31st March, 2019 and 31st March, 2020.

2. Suraj Limited provides you the following information:
   (i) It received a Government Grant @40% towards the acquisition of Machinery worth ₹ 25 Crores.
   (ii) It received a Capital Subsidy of ₹ 150 Lakhs from Government for setting up a Plant costing ₹ 300 Lakhs in a notified backward region.
   (iii) It received ₹ 50 Lakhs from Government for setting up a project for supply of arsenic free water in a notified area.
   (iv) It received ₹ 5 Lakhs from the Local Authority for providing Corona Vaccine free of charge to its employees and their families.
   (v) It also received a performance award of ₹ 500 Lakhs from Government with a condition of major renovation in the Power Plant within 3 years. Suraj Limited incurred 90% of amount towards Capital expenditure and balance for Revenue Expenditure.

   State, how you will treat the above in the books of Suraj Limited.
   Solution:
   (i) As per AS 12 "Accounting for Govt. Grants", two methods of presentation in financial statements of grants related to specific fixed assets are regarded as acceptable alternatives. Under the first alternative, the grant of ₹ 10 crores (40% of 25 crores) is shown as a deduction from the gross value of the asset concerned in arriving at its book value. The grant is thus recognized the profit and loss statement over the useful life of a depreciable asset by way of a reduced depreciation charge. Under second alternative method, grant amounting ₹ 10 crores is treated as deferred income which is recognized in the profit and loss statement on a systematic and rational basis over the useful life of the asset.

   (ii) In the given case, the grant amounting ₹ 150 lakhs received from the Central Government for setting up a plant in notified backward area may be considered as in the nature of promoters' contribution. Thus, amount of ₹ 150 lakhs should be credited to capital reserve and the plant will be shown at ₹ 300 lakhs.

   (iii) ₹ 50 lakhs received from Govt. for setting up a project for supply of arsenic free water in notified area should be credited to capital reserve.

Alternatively, if it is assumed that the project consists of capital asset only, then the amount of ₹ 50 lakhs received from Govt. for setting up a project for supply of arsenic free water should either be deducted from cost of asset of the project concerned in the balance sheet or treated as deferred income which is recognized in the profit and loss statement on a systematic and rational basis over the useful life of the asset.

(iv) ₹ 5 lakhs received from the local authority for providing corona vaccine to the employees is a grant received in nature of revenue grant. Such grants are generally presented as a credit in the profit and loss account, either separately or under a general heading 'Other Income'. Alternatively, ₹ 5 lakhs may be deducted in reporting the related expense i.e. employee benefit expenses.

(v) ₹ 500 Lakhs will be reduced from the renovation cost of power plant or will be treated as deferred income irrespective of the expenditure done by the entity out of it as it was specifically received for the purpose major renovation of power plant. However, it may be, later on, decided by the Govt. whether the grant will have to be refunded or not due to non-compliance of conditions attached to the grant.

3. Santosh Ltd. has received a grant of Rs. 8 crores from the Government for setting up a factory in a backward area. Out of this grant, the company distributed Rs. 2 crores as dividend. Also, Santosh Ltd. received land free of cost from the State Government but it has not recorded it at all in the books as no money has been spent. In the light of AS 12 examine, whether the treatment of both the grants is correct.
Answer:- As per AS 12 'Accounting for Government Grants', when government grant is received for a specific purpose, it should be utilised for the same. So the grant received for setting up a factory is not available for distribution of dividend.
In the second case, even if the company has not spent money for the acquisition of land, land should be recorded in the books of accounts at a nominal value.
The treatment of both the grants is incorrect as per AS 12.

4. Explain in brief the treatment of Refund of Government Grants in line with AS 12 in the following three situations:
(i) When Government Grant is related to revenue,
(ii) When Government Grant is related to specific fixed assets,
(iii) When Government Grant is in the nature of Promoter's contribution.
Answer:- As per AS 12, refund of Government Grant is treated in the following manner:
(i) When Government Grant is related to Revenue:
   (a) The amount of refund is first adjusted against any unamortized deferred credit balance still remaining in respect of the Grant
   (b) Any excess refund over such deferred credit balance or where no deferred credit exists, is immediately charged to Profit & Loss Account.
(ii) When Government Grant is related to specific Fixed Asset:
   (a) The amount of refund will increase the Book Value of the Asset, if at the time of receipt of Grant, the cost of asset was reduced by the amount of Grant.
   (b) If at the time of receipt, the Grant amount was credited to Deferred Grant Account, then the amount of refund will first reduce the unamortized balance of Deferred Grant Account, any excess refund will reduce the Capital Reserve.
(iii) When the Government Grant is in the nature of Promoter's Contribution: Capital Reserve will be reduced by the amount of refund.

5. Yogya Ltd. received a specific grant of Rs. 300 lakhs for acquiring the plant of Rs. 1,500 lakhs during 2013-14 having useful life of 10 years. The grant received was credited to deferred income in the balance sheet. During 2016-2017, due to non -compliance of conditions laid down for the grant of Rs. 300 lakhs, the company had to refund the grant to the Government. Balance in the deferred income on that date was Rs. 210 lakhs and written down value of plant was Rs. 1,050lakhs.
(i) What should be the treatment of the refund of the grant and the effect on cost of the fixed asset and the amount of depreciation to be charged during the year 2016-2017 in the Statement of Profit and Loss?

(ii) What should be the treatment of the refund if grant was deducted from the cost of the plant during 2013-14?

Assume depreciation is charged on assets as per Straight Line Method.

Answer. As per para 21 of AS 12, amount refundable in respect of a grant related to revenue should be applied first against any unamortised deferred credit remaining in respect of the grant. To the extent the amount refundable exceeds any such deferred credit, the amount should be charged to profit and loss statement.

(i) In this case the grant refunded is Rs. 300 lakhs and balance in deferred income is Rs. 210 lakhs, therefore, Rs. 90 lakhs shall be charged to the profit and loss account for the year 2016-2017. There will be no effect on the cost of the fixed asset and depreciation charge will be same as charged in the earlier years.

(ii) As per para 21 of AS 12, the amount refundable in respect of grant which was related to specific fixed assets should be recorded by increasing the book value of the assets by the amount refundable. 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. Therefore, in this case the book value of the plant shall be increased by Rs. 300 lakhs. The increased cost of Rs. 300 lakhs of the plant should be amortised over 7 years (residual life). Depreciation charged during the year 2016-2017 shall be 1200/10 + 300/7 = Rs. 162.86 lakhs.

6. 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.

Solution: **Journal Entries**

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

Working Note:

Depreciation for Year 2	**Rs. in lakhs**
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 15 : EMPLOYEE BENEFITS

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

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

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

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

   (c) The unamortized past service cost is ₹ 180.

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

   Solution:

   Gain from curtailment is estimated as under:

	₹
Reduction in gross obligation	600
Less: Proportion of unamortised past service cost	(18)
Gain from curtailment	582

The liability to be recognised after curtailment in the balance sheet is estimated as under:

		₹
Reduced gross obligation (90% of ₹ 6,000)	5,400	
Less: Fair value of plan assets	(5,100)	300
Less: Unamortised past service cost (90% of ₹ 180)		(162)
Liability to be recognised in the balance sheet		138

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

   Solution: According to AS 15 (Revised 2005) 'Employee Benefits', actuarial gains and losses should be recognized immediately in the statement of profit and loss as income or expense. Therefore, surplus amount of ₹ 6 lakhs is required to be credited to the profit and loss statement of the current year.

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

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

   What is the amount the company should charge in its Profit and Loss account every year as cost for the Defined Benefit obligation? Also calculate the current service cost and the interest cost to be charged per year assuming a discount rate of 8%. (P.V factor for 8% - 0.735, 0.794, 0.857, 0.926, 1)

   Solution:

   Calculation of Defined Benefit Obligation (DBO)

   Expected last drawn salary = ₹ 14,90,210 x 110% x 110% x 110% x 110% x 110%
   = ₹ 24,00,000

   Defined Benefit Obligation (DBO) = ₹ 24,00,000 x 25% x 5 = ₹ 30,00,000

   Amount of ₹ 6,00,000 will be charged to Profit and Loss Account of the company every year as cost for Defined Benefit Obligation.

Calculation of Current Service Cost

Year	Equal apportioned amount of DBO [i.e. ₹ 30,00,000/5 years]	Discounting @ 8% PV factor	Current service cost (Present Value)
a	B	C	d = b x c
1	6,00,000	0.735 (4 Years)	4,41,000
2	6,00,000	0.794 (3 Years)	4,76,400
3	6,00,000	0.857 (2 Years)	5,14,200
4	6,00,000	0.926 (1 Year)	5,55,600
5	6,00,000	1 (0 Year)	6,00,000

Calculation of Interest Cost to be charged per year

Year	*Opening balance*	*Interestcost*	*Currentservice cost*	*Closing balance*
a	**b**	**c = b x 8%**	**D**	**e = b + c + d**
1	0	0	4,41,000	4,41,000
2	4,41,000	35,280	4,76,400	9,52,680
3	9,52,680	76,214	5,14,200	15,43,094
4	15,43,094	1,23,447	5,55,600	22,22,141
5	22,22,141	1,77,859*	6,00,000	30,00,000

*Due to approximations used in calculation, this figure is adjusted accordingly.

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

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

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

Solution:

Computation of Expected Returns on Plan Assets as on 31st March, 20X2, as per AS 15

	₹
Return on opening value of plan assets of ₹ 2,00,000 (held for the year) @ 10.25%	20,500
Add: Return on net gain of ₹ 30,000 (i.e. ₹ 55,000 – ₹ 25,000) during the year i.e. held for six months @ 5% (equivalent to 10.25% annually, compounded every six months)	1,500
Expected return on plan assets as on 31st March, 20X2	22,000

Computation of Actual Returns on Plan Assets as on 31st March, 20X2, as per AS 15

	₹	₹
Fair value of Plan Assets as on 31st March, 20X2		3,00,000
Less: Fair value of Plan Assets as on 1st April, 20X1	(2,00,000)	
Add: Contribution received as on 30th September, 20X1	55,000	(2,55,000)
		45,000
Add: Benefits paid as on 30th September, 20X1		25,000
Actual returns on Plan Assets as on 31st March, 20X2		70,000

AS 16: BORROWING COSTS

1. M/s First Ltd began construction of a new factory building on 1st April, 2017. It obtained Rs. 2,00,000 as a special loan to finance the construction of the factory building on 1st April, 2017 at an interest rate of 8% per annum. Further, expenditure on construction of the factory building was financed through other non-specific loans. Detailed of other outstanding non-specific loans were:

Amounts (Rs)	Rate of Interest per annum
4,00,000	9%
5,00,000	12%
3,00,000	14%

The expenditures that were made on the factory loading construction were as follows:

Date	Amounts (Rs.)
1st April, 2017	3,00,000
31st May 2017	2,40,000
1st August, 2017	4,00,000
31st December, 2017	3.60,000

The constriction of factory building was completed by 31st March, 2018. As per the provisions of AS-16, you are required to:

(1) Calculate the amount of interest to be capitalized.

(2) Pass journal entry for capitalizing the cost and borrowing cost in respect of the factory building.

Solution: As per AS-16, "Borrowing Cost"

(1) Calculation of amount of borrowing cost capitalized

(Rs.)

Date	Amount	Nature of Borrowing	Amount of Borrowing Cost Capitalised (Periods used in Months)
01/04/2017	3,00,000	Specific Rs. 2,00,000 General Rs. 1,00,000	2,00,000 x 8% x 12/12 = Rs. 16,000 1,00,000 x 11.50% x 12/12=Rs. 11,500
31/05/2017	2,40,000	General	2,40,000 x 11.50% x 10/12=Rs. 23,000
01/08/2017	4,00,000	General	4,00,000 x 11.50% x 8/12=Rs. 30,667
31/12/2017	3,60,000	General	3,60,000 x 11.50% x 3/12=Rs. 10,350
Total	13,00,000		91,517

(2) Journal Entry

Date	Particulars		Dr. (Rs.)	Cr. (Rs.)
31.03.18	Building account	Dr.	13,91,517	
	To Bank account (13,00,000 + 91,517)			13,91,517
	(Being amount of cost of building and borrowing cost thereon capitalised)			

Working Note: Calculation of average interest rate other than for specific borrowings

$$\frac{(4,00,000 \times 9\%) + (5,00,000 \times 12\%) + (3,00,000 \times 14\%)}{4,00,000 + 5,00,000 + 3,00,000}$$

= 11.50%

2. Expert Limited issued 12% secured debentures of ₹ 100 lakhs on 01.06.2019. Money raised from debentures to be utilized as under:

Intended Purpose	Amount ₹ in lakhs
Construction of factory building	40
Working Capital	30
Purchase of Machinery	15
Purchase of Furniture	2
Purchase of truck	13

Additional Information:

(i) Interest on debentures for the Financial Year 2019-2020 was paid by the Company.

(ii) During the year, the company invested idle fund of ₹ 5 lakhs (out of the money raised from debentures) in Bank's fixed deposit and earned interest of ₹ 50,000.

(iii) In March, 2020 construction of factory building was not completed (it is expected that it will take another 6 months).

(iv) In March 2020, Machinery was installed and ready for its intended use.

(v) Furniture was put to use at the end of March 2020.

(vi) Truck is going to be received in April, 2020.

You are required to show the treatment of interest as per AS 16 in respect of borrowing cost for the year ended 31st March, 2020 in the Books of Expert Limited.

Solution: According to AS 16 "Borrowing Costs", a qualifying asset is an asset that necessarily takes a substantial period of time to get ready for its intended use. As per the Standard, borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset should be capitalized as part of the cost of that asset. The amount of borrowing costs eligible for capitalization should be determined in accordance with this Standard. Other borrowing costs should be recognized as an expense in the period in which they are incurred. It also states that to the extent that funds are borrowed specifically for the purpose of obtaining a qualifying asset, the amount of borrowing costs eligible for capitalization on that asset should be determined as the actual borrowing costs incurred on that borrowing during the period less any income on the temporary investment of those borrowings.

Thus, eligible borrowing cost = ₹10,00,000 (100 lakhs x 12% x 10/12) – ₹ 50,000 = ₹ 9,50,000

Particulars	**Nature of assets**	**Interest to be capitalized (₹)**	**Interest to be charged to Profit & Loss Account (₹)**
Construction of factory building	Qualifying Asset	9,50,000x40/100 = ₹ 3,80,000	NIL
Purchase of Machinery	Not a Qualifying Asset	NIL	9,50,000x15/100 = 1,42,500
Purchase of and furniture	Not a Qualifying Asset	NIL	9,50,000x2/100 =19,000
Purchase of truck	Not a Qualifying Asset	NIL	9,50,000x13/100 = 1,23,500
Working Capital	Not a Qualifying Asset	NIL	9,50,000x30/100 = ₹ 2,85,000
Total		₹ 3,80,000	₹ 5,70,000

3. Take Ltd. has borrowed Rs. 30 lakhs from State Bank of India during the financial year 2013-14. The borrowings are used to invest in shares of Give Ltd., a subsidiary company of Take Ltd., which is implementing a new project, estimated to cost Rs. 50 lakhs. As on 31st March, 2014, since the said project was not complete, the directors of Take Ltd. resolved to capitalize the interest accruing on borrowings amounting tò 4 lakhs and add it to the cost of investments. Comment.

Solution: As per para 9 of AS 13 "Accounting for Investments", the cost of investment includes acquisition charges such as brokerage, fees and duties. In the present case, Take Ltd. has used borrowed funds for purchasing shares of its subsidiary company Give Ltd. Rs. 4 lakhs interest payable by Take Ltd. to State Bank of India cannot be called as acquisition charges, therefore, cannot be constituted as cost of investment.

Further, as per para 3 of AS 16 "Borrowing Costs", a qualifying asset is an asset that necessarily takes a substantial period of time to get ready for its intended use or sale. Since, shares are ready for its intended use at the time of sale, it cannot be considered as qualifying asset that can enable a company to add the borrowing cost to investments. Therefore, the directors of Take Ltd. cannot capitalise the borrowing cost as part of cost of investment. Rather, it has to be charged to the Statement of Profit and Loss for the year ended 31st March, 2014.

4. 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:

(₹ in lakhs)

	Phase I ₹	Phase II ₹	Phase III ₹	Phase IV ₹
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.

Solution:

S.N.	Particulars	
1	Interest expense on loan ₹ 2,00,00,000 at 15%	30,00,000
2	Total cost of Phases I and II (₹ 34,00,000 +64,00,000)	98,00,000
3	Total cost of Phases III and IV (₹ 55,00,000 + ₹ 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 ₹ 6,65,158.50 (i.e. ₹ 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 ₹ 6,65,158.50 (i.e. ₹ 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 ₹ 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.

5. ABC Limited has started construction of an asset on 1st December, 2020, which continues till 31st March, 2021 (and is expected to go beyond a year). The entity has not taken any specific borrowings to finance the construction of the asset but has incurred finance costs on its general borrowings during the construction period. The directly attributable expenditure at the beginning of the month on this asset was ₹ 10 lakh in December 2020 and ₹ 4 lakh in each of the months of January to March 2021. At the beginning of the year, the entity had taken Inter Corporate Deposits of ₹ 20 lakh at 9% rate of interest and had an overdraft of ₹ 4 lakh, which increased to ₹ 8 lakh on 1st March, 2021. Interest was paid on the overdraft at 10% until 1st January, 2021 and then the rate was increased to 12%. You are

required to calculate the annual capitalization rate for computation of borrowing cost in accordance with AS 16 'Borrowing Costs'.

Solution: Calculation of capitalization rate on borrowings other than specific borrowings

Nature of general borrowings	**Period of outstanding Balance**	**Amount of loan (₹)**	**Rate of interest p.a.**	**Weighted average amount of interest (₹)**
	a	b	c	d = [(b x c) x (a/12)]
9% Debentures	12 months	20,00,000	9%	1,80,000
Bank overdraft	9 months	4,00,000	10%	30,000
	2 months	4,00,000	12%	8,000
	1 month	8,00,000	12%	8,000
		36,00,000		**2,26,000**

Weighted average cost of borrowings

= {20,00,000 x(12/12)} + {4,00,000 x (11/12)} + {8,00,000 x (1/12)} = 24,33,334

Capitalisation rate = [(Weighted average amount of interest / Weighted average of general borrowings) x 100] = [(2,26,000 / 24,33,334) x 100] = 9.29% p.a.

AS 17: SEGMENT REPORTING

1. M/s XYZ Ltd. has three segments namely X, Y, Z. The total Assets of the Company are ₹ 10.00 crores. Segment X has ₹ 2.00 crores, segment Y has ₹ 3.00 crores and segment Z has ₹ 5.00 crores. Deferred tax assets included in the assets of each segments are X- ₹ 0.50 crores, Y— ₹ 0.40 crores and Z— ₹ 0.30 crores. The accountant contends that all the three segments are reportable segments. Comment.
Solution According to AS 17 "Segment Reporting", segment assets do not include income tax assets. Therefore, the revised total assets are ₹ 8.8 crores [₹ 10 crores – (₹ 0.5 + ₹ 0.4 + ₹ 0.3)]. Segment X holds total assets of ₹ 1.5 crores (₹ 2 crores – ₹ 0.5 crores).
Segment Y holds ₹ 2.6 crores (₹ 3 crores – ₹ 0.4 crores); and Segment Z holds ₹ 4.7 crores (₹ 5 crores – ₹ 0.3 crores). Thus all the three segments hold more than 10% of the total assets, all segments are reportable segments.

2. 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?
Answer: 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.

3. The Chief Accountant of Sports Ltd. gives the following data regarding its six segments:

Rs. In lakhs

Particulars	M	N	O	P	Q	R	Total
Segment Assets	40	80	30	20	20	10	200
Segment Results	50	-190	10	10	-10	30	-100
Segment Revenue	300	620	80	60	80	60	1,200

The Chief accountant is of the opinion that segments "M" and "N" alone should be reported. Is he justified in his view? Discuss.
Solution: As per para 27 of AS 17 'Segment Reporting', a business segment or geographical segment should be identified as a reportable segment if:

(i) Its revenue from sales to external customers and from other transactions with other segments is 10% or more of the total revenue- external and internal of all segments; or
(ii) Its segment result whether profit or loss is 10% or more of:
(1) The combined result of all segments in profit; or
(2) The combined result of all segments in loss,
whichever is greater in absolute amount; or
(iii) Its segment assets are 10% or more of the total assets of all segments.

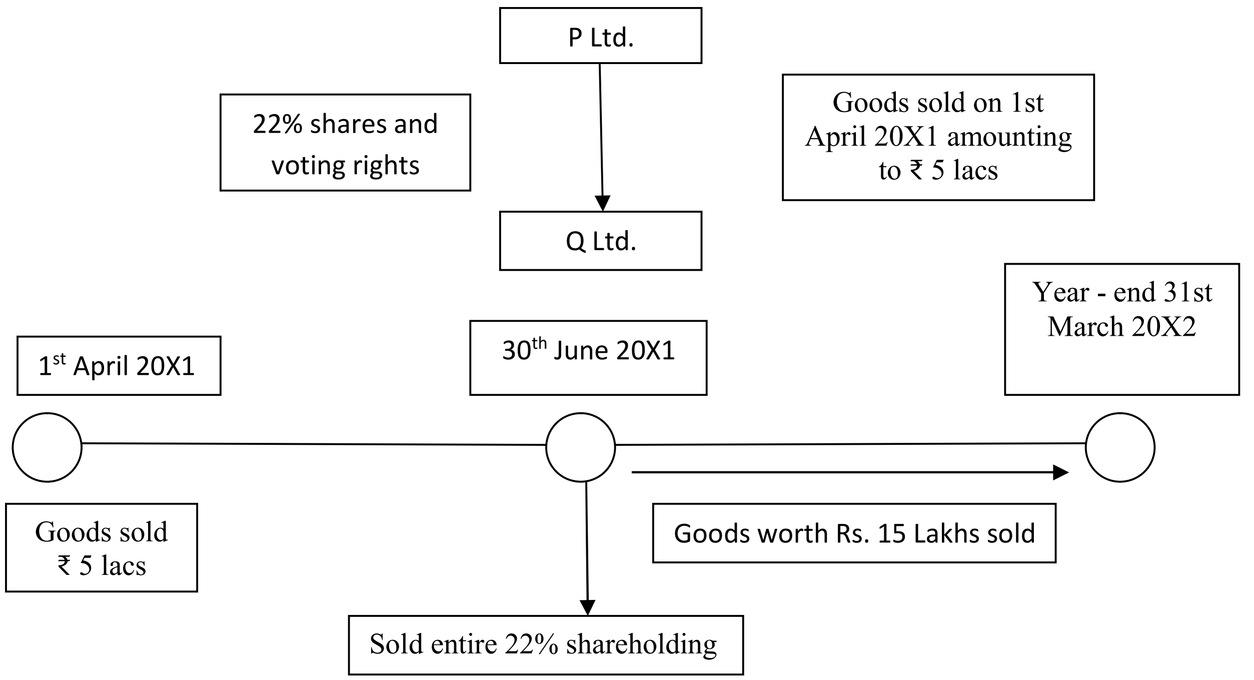
If the total external revenue attributable to reportable segments constitutes less than 75% of total enterprise revenue, additional segments should be identified as reportable segments even if they do not meet the 10% thresholds until atleast 75% of total enterprise revenue is included in reportable segments.

(a) On the basis of turnover criteria segments M and N are reportable segments.
(b) On the basis of the result criteria, segments M, N and R are reportable segments (since their results in absolute amount is 10% or more of Rs.200 lakhs).
(c) On the basis of asset criteria, all segments except R are reportable segments.

Since all the segments are covered in atleast one of the above criteria all segments have to be reported upon in accordance with Accounting Standard (AS) 17. Hence, the opinion of chief accountant is wrong.

AS 18: RELATED PARTY DISCLOSURES

1. Consider a scenario wherein:
   - P Ltd. hold 22% shares and voting rights in Q Ltd. (and hence Q Ltd. is an associate of P Ltd.)
   - On 1st April 20X1, P Ltd. sold certain goods to Q Ltd. amounting to Rs. 5 lacs
   - On 30th June 20X1, P Ltd. sold its entire 22% stake in Q Ltd. (and hence the related party relationship ceased to exist after 30th June 20X1)
   - However, P Ltd. continued supply goods to Q Ltd. subsequent to 30th June 20X1 (just like any other customer) and sold goods worth Rs. 15 lacs during 9-month period ended 31st March 20X2
   - Consider 31st March 20X2 as the year-end date for P Ltd.



Determine whether the transaction for the entire year (ending on 31st March 20X2) is required to be disclosed under AS-18 as related party transaction.

Solution: No – This is because as per AS-18, the disclosure requirements under the Standard relate only to the period during related party relationship existed.

Accordingly, only transactions between P Ltd and Q Ltd till 30th June 20X1 (being sale of goods worth Rs. 5 lacs) are required to be reported / disclosed under AS- 18.

Transactions entered into after 30th June 20X1 are NOT required to be disclosed under AS-18.

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

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

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

Solution:

(i) As Per AS-18, "Related Party Disclosure"

Reporting entity - Maya Ltd.

- Sheetal Ltd. (subsidiary) is a related party
- Fair Ltd.(subsidiary) is a related party

Reporting entity- Sheetal Ltd.

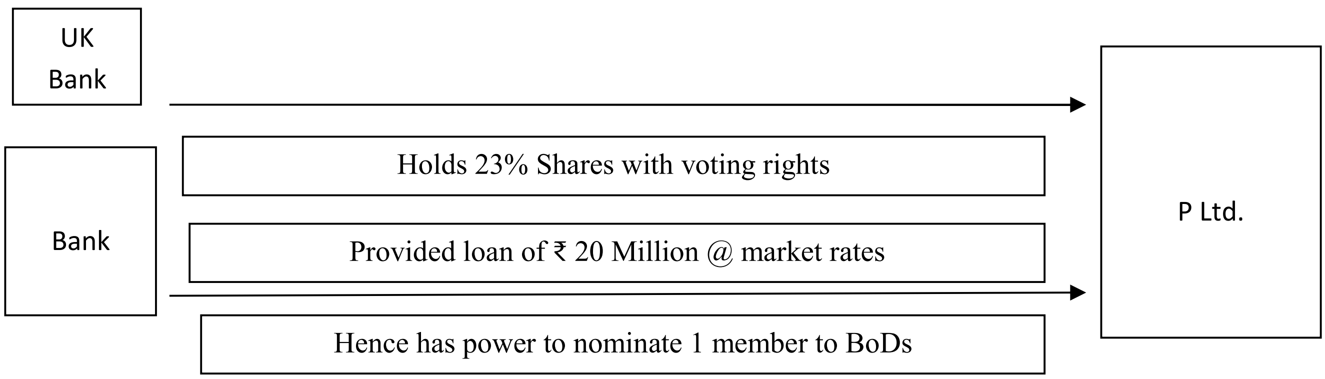
- Maya Ltd. (holding company) is a related party
- Fair Ltd. (subsidiary) is a related party

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

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

(ii) As per Para 3e of AS- 18, ""Related Party Disclosure" Enterprises over which any person described in (c) or (d) is able to exercise significant influence. This includes enterprises owned by directors or major shareholders of the reporting enterprise and enterprises that have a member of key management in common with the reporting enterprise.
In the given all parties are related to each other.

3. Consider a scenario wherein:
• UK Bank holds 23% equity shares with voting rights in P Ltd.
• The bank has provided a loan of Rs. 20 million to P Ltd. at market interest rate
• As per the terms and conditions of the loan agreement, the bank has appointed one person as its nominee to the board of directors of P Ltd. and any major transaction to be entered into by P Ltd. will require the consent of the Bank



Determine: Whether under AS-18 - UK Bank is a related party to P Ltd. (the reporting enterprise)?
Solution: In the instant case, the UK Bank holds 23% shares with voting rights in P Ltd. and hence is deemed to exercise significant influence over P Ltd.
The bank is also a provider of finance to P Ltd. (the reporting enterprise) and as per AS-18, parties like providers of finance are deemed not to be considered as a related party in the course of normal dealings with an enterprise by virtue only of those dealings. However, this exemption will not be available to UK Bank in this case – since it exercises significant influence over P Ltd. (by virtue of holding 23% shares with voting rights in P Ltd.)
Accordingly, for P Ltd. (the reporting enterprise), the UK Bank is a related party and it will be required to disclose the transactions with UK Bank in its financial statements.

AS-19: LEASES

1. AS Ltd. Leased a machine to SB Ltd. on the following terms:

	(Rs. In lakhs)
Fair value of the machine	4.00
Lease term	5 years
Lease Rental Per annum	1.00
Guaranteed Residual value	0.20
Expected Residual value	0.40
Internal Rate of Return	15%

Depreciation is provided on straight line method at 10 per cent per annum. Ascertain Unearned Financial Income. Necessary Journal entries in the books of the Lessee in first year may be shown.

Solution: As per AS 19 on Leases, unearned finance income is the difference between (a) the gross investment in the lease and (b) the present value of minimum lease payments under a finance lease from the standpoint of the lessor; and any unguaranteed residual value accruing to the lessor, at the interest rate implicit in the lease.

Where:

(a) Gross investment in the lease is the aggregate of (i) minimum lease payments from the stand point of the lessor and (ii) any unguaranteed residual value accruing to the lessor.
Gross investment = Minimum lease payments + Unguaranteed residual value
= [Total lease rent + Guaranteed residual value(GRV)] + Unguaranteed residual value (URV)
= [(₹ 1,00,000 X 5 years) + ₹ 20,000] + ₹ 20,000 = ₹ 5,40,000 (a)

(b) Table showing present value of (i) Minimum lease payments (MLP) and (ii) Unguaranteed residual value (URV).

Year	*M.L.P. inclusive of URV* ₹	*Internal rate of return (Discount factor @ 15%)*	*Present Value* ₹
1	1,00,000	0.8696	86,960
2	1,00,000	0.7561	75,610
3	1,00,000	0.6575	65,750
4	1,00,000	0.5718	57,180
5	1,00,000	0.4972	49,720
	20,000(GRV)	0.4972	9,944
	5,20,000		3,45,164 (i)
	20,000 (URV)	0.4972	9,944 (ii)
	5,40,000	(i) + (ii)	3,55,108 *(b)*

Unearned Finance Income = (a) – (b) = ₹ 5,40,000 – ₹ 3,55,108 = ₹ 1,84,892

Journal Entries in the books of SB Ltd.

		₹	₹
At the inception of lease			
	Machinery account	Dr. 3,45,164*	
	To AS Ltd.'s account		3,45,164*
	(Being lease of machinery recorded at present value of minimum lease payments)		
At the end of the first year of lease			
	Finance charges account (Refer Working Note)	Dr. 51,775	
	To AS Ltd.'s account		51,775
	(Being the finance charges for first year due)		

	AS Ltd.'s account To Bank account (Being the lease rent paid to the lessor which includes outstanding liability of ₹ 48,225 and finance charge of ₹ 51,775)	Dr. 1,00,000	1,00,000
	Depreciation account£ To Machinery account (Being the depreciation provided @ 10% p.a. on straight line method)	Dr. 34,516	34,516
	Profit and loss account To Depreciation account To Finance charges account (Being the depreciation and finance charges transferred to profit and loss account)	Dr. 86,291	34,516 51,775

Working Note: Table showing apportionment of lease payments by SB Ltd. between the finance charges and the reduction of outstanding liability

Year	*Outstanding liability (opening balance) (a)* ₹	*Minimum lease payments (b)* ₹	*Finance charges (c = a x 15%)* ₹	*Reduction in principal amount (d= b-c)* ₹	*Outstanding liability (closing balance (e = a-d)* ₹
1	3,45,164	1,00,000	51,775	48,225	2,96,939
2	2,96,939	1,00,000	44,541	55,459	2,41,480
3	2,41,480	1,00,000	36,222	63,778	1,77,702
4	1,77,702	1,00,000	26,655	73,345	1,04,357
5	1,04,357	1,00,000	15,654	84,346	20,011•

2. What do you understand by the term "Interest rate implicit on lease"? Calculate the interest rate implicit on lease from the following details:

Annual Lease Rent	₹ 80,000 at the end of each year
Lease Period	5 Years
Guaranteed Residual Value	₹ 40,000
Unguaranteed Residual Value	₹ 24,000
Fair Value at the inception of the lease	₹ 3,20,000

Discounted rates for the first 5 years are as below:
At 10% 0.909, 0.826, 0.751, 0.683, 0621
At 14% 0.877, 0.769, 0.675, 0.592, 0.519

Answer:- As per para 3 of AS 19 ' Leases' the interest rate implicit in the lease is the discount rate that, at the inception of the lease, causes the aggregate present value of

(a) the minimum lease payments under a finance lease from the standpoint of the lessor; and
(b) any unguaranteed residual value accruing to the lessor,

to be equal to the fair value of the leased asset.

Present value at discount rate of 10% and 14%

Year	Lease Payments (₹)	Disc. Factor (10%)	Present Value (₹)	Disc. Factor (14%)	PV (₹)
1	80,000	0.909	72,720	0.877	70,160
2	80,000	0.826	66,080	0.769	61,520
3	80,000	0.751	60,080	0.675	54,000

4	80,000	0.683	54,640	0.592	47,360
5	80,000	0.621	49,680	0.519	41,520
5	40,000	0.621	24,840	0.519	20,760
5	24,000	0.621	14,904	0.519	12,456
		Total	3,42,944		3,07,776

Interest Rate Implicit on Lease = 10% +[{(14% −10%)×(3,42,944 − 3,20,000)}/(3,42,944 − 3,07,776)]
= 10% + 2.609%
= 12.609% or say 12.61%

3. An Equipment having expected useful life of 5 Years, is leased for 3 years. Both the cost and the fair value of the equipment are Rs. 6,00,000. The amount will be paid in 3 equal installments and at the termination of lease, lessor will get back the equipment. The unguaranteed residual value at the end of 3rd year is Rs. 60,000. The IRR of the investment is 10%. The Present Value of annuity factor of Re. 1 due at the end of 3rd year at 10% IRR is 2.4868. The Present Value of Re. 1 due at the end of 3rd year at 10% rate of interest is 0.7513. State with reason whether the lease constitutes finance lease and also compute the unearned finance income.

Solution:

(i) Determination of Nature of Lease: It is assumed that the fair value of the leased equipments is equal to the present value of minimum lease payments.
Present value of residual value at the end of 3rd year = ₹ 60,000 x 0.7513 = ₹ 45,078
Present value of lease payments = ₹ 6,00,000 – ₹ 45,078 = ₹ 5,54,922
The percentage of present value of lease payments to fair value of the equipment is
= (₹ 5,54,922 / ₹ 6,00,000) x 100 = 92.487%.
Since, it substantially covers the major portion of the lease payments, the lease constitutes a finance lease.

(ii) Calculation of Unearned Finance Income
Annual lease payment = ₹ 5,54,922 / 2.4868 =₹ 2,23,147 (approx)
Gross investment in the lease = Total minimum lease payment + unguaranteed residual value
= (₹ 2,23,147 × 3) + ₹ 60,000 = ₹ 6,69,441 + ₹ 60,000 = ₹ 7,29,441

Unearned finance income = Gross investment - Present value of minimum lease payments and unguaranteed residual value
= ₹ 7,29,441 – ₹ 6,00,000 = ₹ 1,29,441

4. A machine was given on 3 years operating lease by a dealer of the machine for equal annual lease rentals to yield 30% profit margin on cost Rs. 1,50,000. Economic life of the machine is 5 years and output from the machine are estimated as 40,000 units, 50,000 units, 60,000 units, 80,000 units and 70,000 units consecutively for 5 years. Straight line depreciation in proportion of output is considered appropriate. Compute the following:
(i) Annual Lease Rent
(ii) Lease Rent income to be recognized in each operating year and
(iii) Depreciation for 3 years of lease.

Solution:

(i) Annual lease rent
Total lease rent
= 130% of Rs. 1,50,000 X (Output during lease period / Total output)
= 130% of Rs. 1,50,000 x (40,000 +50,000+ 60,000)/(40,000 + 50,000 + 60,000 + 80,000 + 70,000)
= 1,95,000 x 1,50,000 units/3,00,000 units = Rs. 97,500
Annual lease rent = Rs. 97,500 / 3 = Rs. 32,500

(ii) Lease rent Income to be recognized in each operating year
Total lease rent should be recognised as income in proportion of output during lease period, i.e. in the proportion of 40 : 50 : 60.
Hence income recognised in years 1, 2 and 3 will be as:

Year 1	Rs. 26,000,
Year 2	Rs. 32,500 and
Year 3	Rs. 39,000.

(iii) **Depreciation for three years of lease:** Since depreciation in proportion of output is considered appropriate, the depreciable amount Rs. 1,50,000 should be allocated over useful life 5 years in proportion of output, i.e. in proportion of 40 : 50 : 60 : 80 : 70 .
Depreciation for year 1 is Rs. 20,000, year 2 = 25,000 and year 3 = 30,000.

5. X Ltd. sold JCB Machine having WDV of Rs. 50 Lakhs to Y Ltd for Rs. 60 Lakhs and the same JCB was leased back by Y Ltd to X Ltd. The lease is operating lease
Comment according to relevant Accounting Standard if
(i) Sale price of Rs. 60 Lakhs is equal to fair value.
(ii) Fair Value is Rs. 50 Lakhs and sale price is Rs.45 Lakhs.
(iii) Fair value is Rs. 55 Lakhs and sale price isRs. 62 lakhs
(iv) Fair value is Rs. 45 Lakhs and sale price is Rs. 48 Lakhs.
Answer:- According to AS 19, following will be the treatment in the given situations:
(i) When sales price of Rs. 60 lakhs is equal to fair value, X Ltd. should immediately recognize the profit of Rs.10 lakhs (i.e. 60 – 50) in its books.
(ii) When fair value of leased JCB machine is Rs. 50 lakhs & sales price is Rs. 45 lakhs, then loss of Rs. 5 lakhs (50 – 45) to be immediately recognized by X Ltd. in its books provided loss is not compensated by future lease payments.
(iii) When fair value is Rs. 55 lakhs & sales price is Rs. 62 lakhs, profit of Rs. 5 lakhs (55 - 50) to be immediately recognized by X Ltd. in its books and balance profit of Rs. 7 lakhs (62-55) is to be amortised/deferred over lease period.
(iv) When fair value is Rs. 45 lakhs & sales price is Rs. 48 lakhs, then the loss of Rs. 5 lakhs (50- 45) to be immediately recognized by X Ltd. in its books and profit of Rs. 3 lakhs (48-45) should be amortised/deferred over lease period.

6. Classify the following into either operating or finance leases:

(i) Ownership of an assets gets vested to the leases at the end of lease term.
(ii) Lease has option to purchase the asset at lower than fair value , at the end of lease term.
(iii) Economic life of the asset is 5 years , lease term is 4-2 years, but asset is not acquired at the end of lease term.
(iv) Present value (PV) of Minimum lease payments (MLP) = "X", Fair value of the asset is Y.
(v) Economic life is 5 years lease term is 2 years, but the asset is of a special nature, and has been procured only for use of leasee.

Answer.
(i) Finance Lease.
(ii) If it become certain at the inception of lease itself that the option will be exercise by the leases, it is a Finance lease.
(iii) It will still be classified as a finance lease, since a substantial portion of the life of the asset is covered by lease term.
(iv) Where X=Y , or where X substantailly equals Y, it is a finance lease.
(v) Since the asset is procured only for the use of lessee, it is a finance lease.

AS 20: EARNINGS PER SHARE

1. X Ltd. supplied the following information. You are required to compute the basic earnings per share:
(Accounting year 1.1.20X1– 31.12.20X1)

Net Profit	: Year 20X1: ₹ 20,00,000
	: Year 20X2: ₹ 30,00,000
No. of shares outstanding prior to Right Issue	: 10,00,000 shares
Right Issue	: One new share for each four outstanding i.e., 2,50,000 shares.
Right Issue price – ₹ 20	
Last date of exercise rights– 31.3.20X2.	
Fair rate of one Equity share immediately prior to exercise of rights on 31.3.20X2	: ₹ 25

Solution:

Computation of Basic Earnings Per Share
(as per paragraphs 10 and 26 of AS 20 on Earnings Per Share)

	Year20X1 ₹	Year20X2 ₹
EPS for the year 20X1 as originally reported $\frac{\text{Net profit of the year attributable to equity shareholders}}{\text{Weighted average number of equity shares outstanding during the year}}$ = (₹ 20,00,000 / 10,00,000 shares)	2.00	
EPS for the year 20X1 restated for rights issue = [₹ 20,00,000 / (10,00,000 shares × 1.04*)]	1.92 (approx.)	
EPS for the year 20X2 including effects of rights issue $\frac{₹\ 30,00,000}{(10,00,000\text{ shares} \times 1.04 \times 3/12) + (12,50,000\text{ shares} \times 9/12)}$ $\frac{₹\ 30,00,000}{11,97,500\text{ shares}}$		2.51 (approx.)

Working Notes:

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

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

$$= \frac{(₹\ 25 \times 10,00,000\text{ shares}) + (₹\ 20 \times 2,50,000\text{ shares})}{10,00,000\text{ shares} + 2,50,000\text{ shares}}$$

= ₹ 3,00,00,000 / 12,50,000 shares

= ₹ 24

2. Computation of adjustment factor

= Fair value per share prior to exercise of rights / Theoretical ex-rights value per share

= ₹ 25 / ₹ 24 (Refer Working Note 1)

= 1.04 (approx.)

2. Net profit for the current year Rs. 1,00,00,000
No. of equity shares outstanding 50,00,000
Basic earnings per share Rs. 2.00
No. of 12% convertible debentures of Rs. 100 each 1,00,000
Each debenture is convertible into 10 equity shares
Interest expense for the current year Rs. 12,00,000
Tax relating to interest expense (30%) Rs. 3,60,000
Compute Diluted Earnings Per Share.
Solution: Adjusted net profit for the current year (1,00,00,000 + 12,00,000 – 3,60,000) = ₹ 1,08,40,000
No. of equity shares resulting from conversion of debentures: 10,00,000 Shares
No. of equity shares used to compute diluted EPS: (50,00,000 + 10,00,000) = 60,00,000 Shares
Diluted earnings per share: (1,08,40,000/60,00,000) = ₹ 1.81

3. "While calculating diluted EPS, effect is given to all dilutive potential equity shares that were outstanding during the period." Explain this statement in the light of relevant AS.
Also calculate the diluted EPS from the following information:
Net Profit for the current year (After Tax) ₹ 1,00,00,000
No. of Equity shares outstanding 10,00,000
No. of 10% Fully Convertible Debentures of ₹ 100 each 1,00,000
(Each Debenture is compulsorily & fully convertible into 10 equity shares)
Debenture interest expense for the current year ₹ 5,00,000
Assume applicable Income Tax rate @ 30%.
Solution: As per AS 20 'Earnings per Share', the net profit or loss for the period attributable to equity shareholders and the weighted average number of shares outstanding during the period should be adjusted for the effects of all dilutive potential equity shares for calculation of diluted earnings per share. Hence, "in calculating diluted earnings per share, effect is given to all dilutive potential equity shares that were outstanding during the period."

Computation of diluted earnings per share =
Adjusted net profit for the current year / Weighted average number of equity shares

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

Weighted average number of equity shares
Number of equity shares resulting from conversion of debentures
= (1,00,000 X 100) / 10 = 10,00,000 Equity shares

Weighted average number of equity shares used to compute diluted earnings per share
= [(10,00,000 x 12) + (10,00,000 x 6)]/12 = 15,00,000 equity shares

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

Note: Interest on debentures for full year amounts to ₹ 10,00,000 (i.e. 10% of ₹ 1,00,00,000). However, interest expense amounting ₹ 5,00,000 has been given in the question. It may be concluded that debentures have been issued at the mid of the year and interest has been provided for 6 months.

4. What do you mean by 'Weighted Average number of Equity Shares outstanding during the period' and why is it to be calculated?
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.
Also define Potential Equity Share.

Answer: As per AS 20, "Earnings Per Share", the weighted average number of equity shares outstanding during the period reflects the fact that the amount of shareholders' capital may have varied during the period as a result of a larger or lesser number of shares outstanding at any time.

For the purpose of calculating basic earnings per share, the number of equity shares should be the weighted average number of equity shares outstanding during the period.

The following dates should be considered for consideration of weights for 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.

A Potential Equity Share is a financial instrument or other contract that entitles, or may entitle its holder to equity shares.

5. Net profit for the year 2012 Rs. 12,00,000
Weighted average number of equity shares outstanding during the year 2012 5,00,000 shares
Average fair value of one equity share during the year 2012 Rs. 20.00
Weighted average number of shares under option during the year 2012 1,00,000 shares
Exercise price for shares under option during the year 2012 Rs. 15.00
Compute Basic and Diluted Earnings Per Share.

Solution: Computation of earnings per share

	Earnings ₹	***Shares***	***Earnings/Share*** ₹
Net profit for the year 20X1	12,00,000		
Weighted average no. of shares during year 20X1		5,00,000	
Basic earnings per share			2.40
Number of shares under option		1,00,000	
Number of shares that would have been issued at			
fair value (100,000 x 15.00)/20.00		(75,000)	
Diluted earnings per share	12,00,000	5,25,000	2.29

Note: The earnings have not been increased as the total number of shares has been increased only by the number of shares (25,000) deemed for the purpose of the computation to have been issued for no consideration.

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

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

AS 22: ACCOUNTING FOR TAXES ON INCOME

1. PQR Ltd.'s accounting year ends on 31st March. The company made a loss of Rs. 2,00,000 for the year ending 31.3.2001. For the years ending 31.3.2002 and 31.3.2003, it made profits of Rs. 1,00,000 and Rs. 1,20,000 respectively. It is assumed that the loss of a year can be carried forward for eight years and tax rate is 40%. By the end of 31.3.2001, the company feels that there will be sufficient taxable income in the future years against which carry forward loss can be set off. There is no difference between taxable income and accounting income except that the carry forward loss is allowed in the years ending 2002 and 2003 for tax purposes. Prepare a statement of Profit and Loss for the years ending 2001, 2002 and 2003.

Answer: **Statement of Profit and Loss** **(Rs.)**

	31.03.01	31.03.02	31.03.03
Profit (Loss)	(2,00,000)	1,00,000	1,20,000
Less: Current tax			(8,000)
Deferred tax:			
Tax effect of timing differences originating during the year	80,000		
Tax effect of timing differences reversed/adjusted during the Year		(40,000)	(40,000)
Profit(loss) after tax effect	(1,20,000)	60,000	72,000

2. The following particulars are stated in the Balance Sheet of Deep Limited as on 31st March, 2020:

	(Rs. In Lakhs)
Deferred Tax Liability (Cr.)	28.00
Deferred Tax Assets (Dr.)	14.00

The following transactions were reported during the year 2020 -2021:

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

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

(iii) Share issue expenses allowed under section 35(D) of the Income Tax Act, 1961 for the year 2020-21 (1/10th of Rs. 70.00 lakhs incurred in 2019-20).

(iv) Repairs to Plant and Machinery were made during the year for Rs. 140.00 Lakhs and was spread over the period 2020-21 and 2021-22 equally in the books. However, the entire expenditure was allowed for income-tax purposes in the year 2020-21.

Tax Rate to be taken at 40%.

You are required to show the impact of above items on Deferred Tax Assets and Deferred Tax Liability as on 31st March, 2021.

Solution: Impact of various items in terms of deferred tax liability/deferred tax asset on 31.3.21

Transactions	Analysis	Nature of difference	Effect	Amount (Rs.)
Difference in depreciation	Generally, written down value method of depreciation is adopted under IT Act which leads to higher depreciation in earlier years of useful life of the asset in comparison to later years.	Responding timing difference	Reversal of DTL	28 lakhs X 40% = Rs. 11.20 lakhs
Disallowances, as per IT Act, of earlier years	Tax payable for the earlier year was higher on this account.	Responding timing difference	Reversal of DTA	14 lakhs X 40% = 5.6 lakhs
Share issue expenses	Due to disallowance of full expenditure under IT Act, tax payable in the earlier years was higher.	Responding timing difference	Reversal of DTA	7 lakhs X 40% = Rs. 2.8 lakhs
Repairs to plant and machinery	Due to allowance of full expenditure under IT Act, tax payable of the current year will be less.	Originating timing difference	Increase in DTL	70 lakhs X 40% =28 lakhs

3. Milton Ltd. is a full tax free enterprise for the first 10 years of its existence and is in the second year of its operations. Depreciation timing difference resulting in a deferred tax liability in years 1 and 2 is Rs. 200 lakhs and Rs. 400 lakhs respectively. From the 3rd year onwards, it is expected that the timing difference would reverse each year by Rs.10 lakhs. Assuming tax rate @35%, find out the deferred tax liability at the end of the second year and any charge to the profit and loss account.

Answer: In the case of tax free companies, no deferred tax liability is recognized, in respect of timing differences that originate and reverse in the tax holiday period. Deferred tax liability or asset is created in respect of timing differences that originate in a tax holiday period but are expected to reverse after the tax holiday period. For this purpose, adjustments are done in accordance with the FIFO method.

Of Rs. 200 lakhs, Rs.80 lakhs will reverse in the tax holiday period. Therefore, Deferred Tax Liability will be created on Rs.120 lakhs @ 35% (i.e.) Rs.42 lakhs.

In the second year, the entire Rs.400 lakhs will reverse only after the tax holiday period.

Therefore, deferred tax charge in the Profit and Loss Account will be Rs.400 x 35% = 140 lakhs and deferred tax liability in the Balance Sheet will be (42+140) = Rs.182 lakhs.

4. From the following details of A Ltd. for the year ended 31-03-2010, calculate the deferred tax asset/liability as per AS-22

Particulars	Rs.
Accounting Profit	6,00,000
Book Profit as per MAT	3,50,000
Profit as per Income Tax Act	60,000
Tax rate	20%
MAT rate	7.50%

Solution:

Tax as per accounting profit 6,00,000 X 20%= Rs. 1,20,000

Tax as per Income-tax Profit 60,000 X 20% =Rs. 12,000

Tax as per MAT 3,50,000 X 7.50%= Rs. 26,250

Tax expense= Current Tax +Deferred Tax

Rs. 1,20,000 = Rs. 12,000+ Deferred tax

Therefore, Deferred Tax liability as on 31-03-201

= Rs. 1,20,000 – Rs. 12,000 = Rs. 1,08,000

Amount of tax to be debited in Profit and Loss account for the year 31-03-2017

Current Tax + Deferred Tax liability + Excess of MAT over current tax

= Rs. 12,000 + Rs. 1,08,000 + Rs. 14,250 (26,250 – 12,000)

= Rs. 1,34,250

5. ABC Company limited had an investment in Venture Capital amounting ₹ 10 Crores. Venture capital in turn had invested in the below portfolio companies (New Start- ups) on behalf of ABC Limited:

Portfolio Companies	**Amount of investment (₹ in Crores)**
Oscar Limited	2
Zee Limited	3
Star Limited	4
Sony Limited	1
Total	10

During the FY 2019-2020, Venture Capital had sold their investment in Star Limited and realised an amount of ₹ 8 Crores on sale of shares of star Limited and entire proceeds of ₹ 8 Crores have been transferred by Venture Capital to ABC Company Limited.

The accounts manager has received the following additional information from venture capital on 31.03.2020:

(1) 8 Crores has been deducted from the cost of investment and carrying amount of investment as at year end is 2 Crores.

(2) Company had to pay a capital gain tax @ 20% on the net sale consideration of ₹ 4 Crores.

(3) Due to COVID-19, the remaining start- ups (i.e. Oscar Limited, Zee Limited, and Sony Limited) are not performing well and will soon wind up their operations. Venture capital is monitoring the situation and if required they will provide an impairment loss in June 2020 Quarter.

You need to suggest the accounts manager what should be the correct accounting treatment as per AS 22 “Accounting for Taxes on Income”.

Solution: As company had to pay capital gain tax @ 20% on the net sale consideration as per income tax laws, the company has to recognise a current tax liability of 0.8 Crores computed as under:

Particulars	**Amount (₹ in Crores)**
Sales Consideration	8
Cost of Investment	4
Net gain on Sale	4
Tax @ 20%	0.8

As per AS 22, Timing differences are those differences between taxable income and accounting income for a period that originate in one period and are capable of reversal in one or more subsequent periods.

Particulars	**Amount (₹ in Crores)**	**Rationale**
Taxable Income	4	As per income tax laws
Accounting Income	Nil	As the same is deducted from the cost of investment
Timing Difference	4	

As per AS 22, deferred tax assets should be recognised and carried forward only to the extent that there is a reasonable certainty that sufficient future taxable income will be available against which such deferred tax assets can be realised.

Since in current scenario, due to Covid 19 the portfolio companies are not performing well, thus the company may not have sufficient future taxable income which will reverse deferred tax assets. Therefore, the company should not recognise DTA of ₹ 0.8 Crores and company should recognise only current tax liability of ₹ 0.8 Crores.

AS 24: DISCONTINUING OPERATIONS

1. A healthcare goods producer has changed the product line as follow :

	Washing soap	Bathing soap
January 2007 –september 2007 per month	2,00,000	2,00,000
October 2007 –december 2007 per month	1,00,000	3,00,000
January 2008- March 2008 per month	0	4,00,000

The company has enforced a gradual enforcement of change in product line on the basis of an overall plant capacity . The board of Directors of the company has passed a resolution in March 2007 to this effect. The companies follow calendar year as its accounting year. Should it be treated as discontinuing operation?

Answer:- Business enterprises frequently close facilities, abandon products, or even product line, and reduce the size of their work force in response to market force. These kinds of terminations, generally are not in themselves discontinuing operations unless they satisfy the definition criteria. By gradually reducing the size of operation in product line of washing soap, the company has increased its scale of operation in bathing soap. Such a change is gradual or evolutionary, phasing out of a product line or class of services does not meet definition criteria in paragraph 3(a) of AS 24 –namely , disposing substantially in its entirely a component of enterprise. Hence changeover is not a discontinuing operation.

2. Qu Ltd. in the business of manufacture of Passenger cars and commercial vehicles. The company is working on a strategic plan to shift from the passenger car segment over the coming 5 years However no specific plans have been drawn up for sale of neither the division nor its assets. As part of its plan it will reduce the production of passenger cars by 20% annually. It also plans to commence another new factory for the manufacture of commercial vehicles and transfer plus employees in a phased manner.

(i) You are required to comment if mere gradual phasing out in itself can be considered as a 'Discounting Operation' within the meaning of AS 24.

(ii) If the company passes a resolution to sell some of the assets in the passenger car division and also to transfer few other of the passenger car division to the new factory. Does this trigger the application or AS 24?

(iii) Would your answer to the above be different if the company resolves to sell the assets of the Passenger Car Division in phased but time manner?

Solution: Mere gradual phasing is not considered as discontinuing operation as defined under para 3 of AS 24, ' Discontinuing Operation'.

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) Shifting of some production or marketing activities for a particular line of business from one location to another and
(3) Closing of a facility to achieve productivity improvements or other cost savings.

A Reportable business segment or geographical segment as defined in AS-17, would normally satisfy criteria (b) of the definition.

In view of the above the answers are:

(i) No. The companys' strategic plan has no final approval from the board through a resolution and no specific time bound activities like shifting of Assets and employees and above all the new segment commercial vehicle production line and factory has started.

(ii) No. The resolution is salient about stoppage of the Car segment in definite time period. Though, some assets sales and transfer proposal was passed through a resolution to the new factory, closure road map and new segment starting road map is missing. Hence, AS-24 will not be applicable.

(iii) Yes. Phased and time bound programme resolved in the board clearly indicates the closure of the passenger car segment in a definite time frame and clear road map. Hence, this action will attract AS-24 compliance.

AS 25: INTERIM FINANCIAL REPORTING

1. Antarbarti Limited reported a Profit Before Tax (PBT) of ₹ 4 lakhs for the third quarter ending 30-09-20X1. On enquiry you observe the following. Give the treatment required under AS 25:
   (i) Dividend income of ₹ 4 lakhs received during the quarter has been recognized to the extent of ₹ 1 lakh only.
   (ii) 80% of sales promotion expenses ₹ 15 lakhs incurred in the third quarter has been deferred to the fourth quarter as the sales in the last quarter is high.
   (iii) In the third quarter, the company changed depreciation method from WDV to SLM, which resulted in excess depreciation of ₹ 12 lakhs. The entire amount has been debited in the third quarter, though the share of the third quarter is only ₹ 3 lakhs.
   (iv) ₹ 2 lakhs extra-ordinary gain received in third quarter was allocated equally to the third and fourth quarter.
   (v) Cumulative loss resulting from change in method of inventory valuation was recognized in the third quarter of ₹ 3 lakhs. Out of this loss ₹ 1 lakh relates to previous quarters.
   (vi) Sale of investment in the first quarter resulted in a gain of ₹ 20 lakhs. The company had apportioned this equally to the four quarters.

   Prepare the adjusted profit before tax for the third quarter.

   Solution: As per para 36 of AS 25 "Interim Financial Reporting", seasonal or occasional revenue and cost within a financial year should not be deferred as of interim date until it is appropriate to defer at the end of the enterprise's financial year. Therefore, dividend income, extra-ordinary gain, and gain on sale of investment received during 3rd quarter should be recognised in the 3rd quarter only. Similarly, sales promotion expenses incurred in the 3rd quarter should also be charged in the 3rd quarter only.

   Further, as per AS 10, Property, Plant and Equipment, if there is change in the depreciation method, such a change should be accounted for as a change in accounting estimate in accordance with AS 5, Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies, and applied prospectively. Therefore, no adjustment would be required due to change in the method of depreciation.

   Accordingly, the adjusted profit before tax for the 3rd quarter will be as follows:

   Statement showing Adjusted Profit Before Tax for the third quarter

	(₹ in lakhs)
Profit before tax (as reported)	4
Add: Dividend income ₹(4-1) lakhs	3
Excess depreciation charged in the 3rd quarter, due to change in the method	-
Extra ordinary gain ₹(2-1) lakhs	1
Cumulative loss due to change in the method of inventory valuation should be applied retrospectively ₹(3-2) lakhs	1
	9
Less: Sales promotion expenses (80% of ₹15 lakhs)	(12)
Gain on sale of investment (occasional gain shouldnot be deferred)	(5)
Adjusted Profit before tax for the third quarter	(8)

2. Sincere Corporation is dealing in seasonal product. Sales pattern of the product quarter-wise is as follows:

1st quarter 30th June	10%
2nd quarter 30th September	10%
3rd quarter 31st December	60%
4th quarter 31st March	20%

   Information regarding the 1st quarter ended on 30th June, 20X1 is as follows:

Sales	80 crores
Salary and other expenses	60 crores
Advertisement expenses (routine)	4 crores
Administrative and selling expenses	8 crores

   While preparing interim financial report for first quarter Sincere Corporation wants to defer ₹ 10 crores expenditure to third quarter on the argument that third quarter is having more sales, therefore, the third quarter should be debited by more expenditure. Considering the seasonal nature of business and the expenditures are uniform throughout all quarters, calculate the result of the first quarter as per AS 25. Also give a comment on the company's view.

Solution:

Particulars		**(₹ In crores)**
Result of first quarter ended 30th June, 20X1		
Turnover	80	
Other Income	Nil	
Total (a)		80
Less: Changes in inventories	Nil	
Salaries and other cost	60	
Administrative and selling Expenses (4+8)	12	
Total (b)		72
Profit (a)-(b)		8

According to AS 25, the Income and Expense should be recognized when they are earned and incurred respectively. Therefore, seasonal incomes will be recognized when they occur. Thus, the company's view is not as per AS 25.

3. An enterprise reports quarterly, estimates an annual income of ₹ 10 lakhs. Assume tax rates on 1st ₹ 5,00,000 at 30% and on the balance income at 40%. The estimated quarterly income are ₹ 75,000, ₹ 2,50,000, ₹ 3,75,000 and ₹ 3,00,000. Calculate the tax expense to be recognized in each quarter.

Solution: As per para 29 of AS 25 'Interim Financial Reporting', income tax expense is recognised in each interim period based on the best estimate of the weighted average annual income tax rate expected for the full financial year.

		₹
Estimated Annual Income	(A)	10,00,000
Tax expense:		
30% on ₹ 5,00,000		1,50,000
40% on remaining ₹ 5,00,000		2,00,000
	(B)	3,50,000

Weighted average annual income tax rate = A/B = 3,50,000 / 10,00,000 = 35%

Tax expense to be recognized in each of the quarterly reports		₹
Quarter I -	₹ 75,000 x 35%	26,250
Quarter II -	₹ 2,50,000 x 35%	87,500
Quarter III -	₹ 3,75,000 x 35%	1,31,250
Quarter IV -	₹ 3,00,000 x 35%	1,05,000
	₹ 10,00,000	3,50,000

AS 26 : INTANGIBLE ASSETS

1. A company acquired for its internal use a software on 28.01.2012 from the USA for US $ 1,00,000. The exchange rate on that date was Rs. 52 per USD. The seller allowed trade discount @ 5 %. The other expenditure were:
(i) Import Duty : 20%
(ii) Purchase Tax : 10%
(iii) Entry Tax : 5 % (Recoverable later from tax department)
(iv) Installation expenses : Rs. 25,000
(v) Profession fees for Clearance from Customs: Rs. 20,000
Compute the cost of Software to be capitalized.
Answer:- Calculation of cost of software (intangible asset) acquired for internal use

Purchase cost of the software	$ 1,00,000
Less: Trade discount @ 5%	($ 5,000)
	$ 95,000
Cost in Rs. (US $ 95,000 x Rs. 52)	49,40,000
Add: Import duty on cost @ 20% (Rs.)	9,88,000
	59,28,000
Purchase tax @ 10% (Rs.)	5,92,800
Installation expenses (Rs.)	25,000
Profession fee for clearance from customs (Rs.)	20,000
Cost of the software to be capitalized (Rs.)	65,65,800

Note: Since entry tax has been mentioned as a recoverable/refundable tax, it is not included as part of the cost of the asset.

2. U.K. International Ltd. is developing a new production process. During the financial year ending 31st March, 2011, the total expenditure incurred was Rs. 50 lakhs. This process met the criteria for recognition as an intangible asset on 1st December, 2010. Expenditure incurred till this date was Rs. 22 lakhs. Further expenditure incurred on the process for the financial year ending 31st March, 2012 was Rs. 80 lakhs. As at 31st March, 2012, the recoverable amount of know-how embodied in the process is estimated to be Rs. 72 lakhs. This includes estimates of future cash outflows as well as inflows.
You are required to calculate:
(i) Amount to be charged to Profit and Loss A/c for the year ending 31st March, 2011 and carrying value of intangible as on that date.
(ii) Amount to be charged to Profit and Loss A/c and carrying value of intangible as on 31st March, 2012.
Ignore depreciation.
Answer:- As per AS 26 'Intangible Assets'
(i) For the year ending 31.03.2011
(1) Carrying value of intangible as on 31.03.2011: At the end of financial year 31st March 2011, the production process will be recognized (i.e. carrying amount) as an intangible asset at a cost of Rs. 28 lakhs (expenditure incurred since the date the recognition criteria were met, i.e. from 1st December 2010).

(2) Expenditure to be charged to Profit and Loss account: The Rs. 22 lakhs is recognized as an expense because the recognition criteria were not met until 1st December 2011. This expenditure will not form part of the cost of the production process recognized in the balance sheet.

(ii) For the year ending 31.03.2012

(1) Expenditure to be charged to Profit and Loss account:	**(Rs. in lakhs)**
Carrying Amount as on 31.03.2011	28
Expenditure during 2011 – 2012	80
Total book cost	108
Recoverable Amount	(72)
Impairment loss	36

Rs. 36 lakhs to be charged to Profit and loss account for the year ending 31.03.2012.

(2) Carrying value of intangible as on 31.03.2012:	**(Rs. in lakhs)**
Total Book Cost	108
Less: Impairment loss	(36)
Carrying amount as on 31.03.2012	72

3. Swift Ltd. acquired a patent at a cost of ₹ 80,00,000 for a period of 5 years and the product life-cycle is also 5 years. The company capitalized the cost and started amortizing the asset at ₹ 10,00,000 per annum. The company had amortized the patent at 10,00,000 per annum in first two years on the basis of economic benefits derived from the product manufactured under the patent. After two years it was found that the product life-cycle may continue for another 5 years from then. The patent was renewable and Swift Ltd. got it renewed after expiry of five years. The net cash flows from the product during these 5 years were expected to be ₹ 36,00,000, ₹ 46,00,000, ₹ 44,00,000, ₹ 40,00,000 and ₹ 34,00,000. Find out the amortization cost of the patent for each of the years.

Solution: Swift Limited amortised ₹ 10,00,000 per annum for the first two years i.e. ₹ 20,00,000. The remaining carrying cost can be amortised 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 (₹)**	**Amortisation Ratio**	**Amortisation Amount (₹)**
I	-	0.125	10,00,000
II	-	0.125	10,00,000
III	36,00,000	0.180	10,80,000
IV	46,00,000	0.230	13,80,000
V	44,00,000	0.220	13,20,000
VI	40,00,000	0.200	12,00,000
VII	34,00,000	0.170	10,20,000
Total	2,00,00,000	1.000	80,00,000

It may be seen from above that from third year onwards, the balance of carrying amount i.e., ₹ 60,00,000 has been amortised in the ratio of net cash flows arising from the product of Swift Ltd.

4. Nirman Solutions incurred costs to develop and produce a routine, low risk Computer Software Product, as follows, as on 31.03.2016

Completion of Detailed Program Design	Rs. 15,00,000
Costs incurred for Coding and Testing to establish technological feasibility	Rs. 8,00,000
Other Coding and Testing Costs after establishment of technological feasibility	Rs. 6,50,000
Cost of producing Product Masters for Training Materials	Rs. 4,20,000
Duplication of Computer Software and Training Materials from Product Master (5,000 Units)	Rs. 2,50,000
Packaging Product (2,500 Units)	Rs. 1,50,000

Required:

(i) What amount should be capitalized as Software Cost, subject to amortization of Nirman Solutions as on 31st March 2016?

(ii) What amount should be reported in Inventory of Nirman Solutions as on 31st March 2016?

Solution:

(i) As per AS 26, costs incurred in creating a computer software product should be charged to research and development expense when incurred until technological feasibility has been established for the product. Technological feasibility has been established upon completion of detailed program design or working model. In this case, Rs. 23,00,000 would be recorded as an expense (Rs. 15,00,000 for completion of detailed program design and Rs. 8,00,000 for coding and testing to establish technological feasibility). Cost incurred from the point of technological feasibility until the time when products costs are incurred are capitalized as software cost. In this situation, Rs. 10,70,000 (i.e. Rs. 6,50,000 + Rs. 4,20,000) will be capitalized as the cost of the software.

(ii) The cost of duplication of computer software and training materials from product masters (5,000 units) amounting Rs. 2,50,000 and packaging product (2,500 units) amounting Rs. 1,50,000 should be reported as inventory cost as on 31st March, 2016 i.e. inventory value is total of Rs. 4,00,000.

5. Base Limited is showing an intangible asset at Rs. 85 lakhs as on 1-4-2011. This asset was acquired for Rs. 112 lakhs on 1-4-2008 and the same was available for use from that date. The company has been following the policy of amortization of the intangible asset over a period of 12 years on straight line basis. Comment on the accounting treatment of the above with reference to the relevant accounting standard.

Answer:- As per para 63 of AS 26 "Intangible Assets," the depreciable amount of an intangible asset should be allocated on a systematic basis over the best estimates of its useful life. There is a rebuttable presumption that the useful life of an intangible asset will not exceed ten years from the date when the asset is available for use. Amortization should commence when the asset is available for use.

Base Limited has been following the policy of amortization of the intangible asset over a period of 12 years on straight line basis. The period of 12 years is more than the maximum period of 10 years specified as per AS 26.

Accordingly, Base Limited would be required to restate the carrying amount of intangible asset as on 1.4.2011 at Rs. 112 lakhs less Rs. 33.6 lakhs (112 lakhs ×3 years/10 years) = Rs. 78.4 lakhs.

The difference of Rs. 6.6 lakhs i.e. (Rs. 85 lakhs – Rs. 78.4 lakhs) will be adjusted against the opening balance of revenue reserve.

The necessary journal entry (for rectification) will be

Revenue Reserves	Dr.	Rs. 6.6 Lakhs	
To Intangible Assets			Rs. 6.6 Lakhs
(Adjustment to reserves due to restatement of the carrying amount of intangible asset)			

The carrying amount of Rs. 78.4 lakhs would be amortized over remaining 7 years by Rs. 11.2 lakhs per year.

6. Surya Ltd. had the following transactions during the year ended 31st March, 2021.

(i) It acquired the business of Gomati Limited on a going concern basis for ₹ 25,00,000 on 1st June,2020. The fair value of the Net Assets of Gomati Limited was ₹ 18,75,000. Surya Ltd. believes that due to popularity of the products of Gomati Limited in the market, its goodwill exists.

(ii) On 20th August, 2020, Surya Ltd. incurred cost of ₹ 6,00,000 to register the patent for its product. Surya Ltd. expects the Patent's economic life to be 8 years.

(iii) On 1st October, 2020, Surya Ltd. has taken a franchise to operate an ice cream parlour from Volga Ltd. for ₹ 4,50,000 and at an Annual Fee of 10% of Net Revenues (after deducting expenditure). The franchise expires after six years. Net Revenue for the year ended 31st March, 2021 amounted to ₹ 1,50,000.

Surya Ltd. follows an accounting policy to amortize all Intangibles on Staright Line basis (SLM) over the maximum period permitted by the Accounting Standards taking a full year amortization in the year of acquisition. Goodwill on acquisition of business is to be amortized over 5 years (SLM).

Prepare an extract showing the Intangible Assets section in the Balance Sheet of Surya Ltd. as at 31st March, 2021.

Solution: **Surya Ltd.**

Balance Sheet (Extract relating to intangible asset) as on 31 st March 2021

	Note No.	₹
Assets		
(1) Non-current assets		
Intangible assets	1	14,00,000

Notes to Accounts (Extract)

		₹	₹
1.	**Intangible assets**		
	Goodwill (Refer to note 1)	5,00,000	
	Patents (Refer to Note 2)	5,25,000	
	Franchise (Refer to Note 3)	3,75,000	14,00,000

Working Notes:

		₹
(1)	Goodwill on acquisition of business	
	Cash paid for acquiring the business (purchase consideration)	25,00,000
	Less: Fair value of net assets acquired	(18,75,000)
	Goodwill	6,25,000
	Less: Amortization. over 5 years (as per SLM)	(1,25,000)
	Balance to be shown in the balance sheet	5,00,000
(2)	Patent	6,00,000
	Less: Amortization (over 8 years as per SLM)	(75,000)
	Balance to be shown in the balance sheet	5,25,000
(3)	Franchise	4,50,000
	Less: Amortization (over 6 years)	(75,000)
	Balance to be shown in the balance sheet	3,75,000

AS 28 : IMPAIRMENT OF ASSETS

1. Ergo Industries Ltd. gives the following estimates of cash flows relating to Property, Plant and Equipment on 31-12-20X1. The discount rate is 15%.

Year	Cash Flow (₹ in lakhs)
20X2	4000
20X3	6000
20X4	6000
20X5	8000
20X6	4000

Residual value at the end of 20X6	=	₹ 1,000 lakhs
Property, Plant and Equipment purchased on 1-1-20XX	=	₹ 40,000 lakhs
Useful life	=	8 years
Net selling price on 31-12-20X1	=	₹ 20,000 lakhs

Calculate on 31-12-20X1:
(a) Carrying amount at the end of 20X1
(b) Value in use on 31-12-20X1
(c) Recoverable amount on 31-12-20X1
(d) Impairment loss to be recognized for the year ended 31-12-20X1
(e) Revised carrying amount
(f) Depreciation charge for 20X2.

Note: The year 20XX is the immediate preceding year before the year 20X0.

Solution: Calculation of value in use

Year	Cash Flow	Discount as per 15%	Discounted cash flow
20X2	4,000	0.870	3,480
20X3	6,000	0.756	4,536
20X4	6,000	0.658	3,948
20X5	8,000	0.572	4,576
20X6	4,000	0.497	1,988
20X6	(residual) 1,000	0.497	497
			19,025

(a) Calculation of carrying amount:

Original cost	=	₹ 40,000 lakhs
Depreciation for 3 years = [(40,000-1000) X 3/8]	=	₹ 14,625 lakhs
Carrying amount on 31-12-20X1 = [40,000-14,625]	=	₹ 25,375 lakhs

(b) Value in use = ₹ 19,025 lakhs

(c) Recoverable amount = higher of value in use and net selling price i.e. ₹ 20,000 lakhs.
Recoverable amount = ₹ 20,000 lakhs

(d) Impairment Loss = ₹ (25,375-20,000) = ₹ 5,375 lakhs

(e) Revised carrying amount = ₹ (25,375-5,375) = ₹ 20,000 lakhs

(f) Depreciation charge for 20X2 = (20,000-1000)/5 = ₹ 3,800 lakhs

2. Great Ltd., acquired a machine on 1st April, 2012 for Rs. 7 crore that had an estimated useful life of 7 years. The machine is depreciated on straight line basis and does not carry any residual value. On 1st April, 2016, the carrying value of the machine was reassessed at Rs. 5.10 crore and the surplus arising out of the revaluation being credited to revaluation reserve. For the year ended March 2018, conditions indicating an impairment of the machine existed and the amount recoverable ascertained to be only Rs. 79 lakhs.
Calculate the loss on impairment of the machine and show how this loss is to be treated in the books of Great Ltd. Great Ltd., had followed the policy of writing down the revaluation surplus by the increased charge of depreciation resulting from the revaluation.

Solution: Statement Showing Impairment Loss

		(Rs. in crores)
Carrying amount of the machine as on 1st April, 2012 [7 crores × 4 years]		7.00
Depreciation for 4 years i.e. 2012-2013 to 2015-2016[7 years]		(4.00)
Carrying amount as on 31.03.2016		3.00
Add: Upward Revaluation (credited to Revaluation Reserve account)		2.10
Carrying amount of the machine as on 1st April 2016 (revalued)		5.10
Less: Depreciation for 2 years i.e. 2016-2017 & 2017-2018		
[5.10 crores × 2 years]		
3 years		(3.40)
Carrying amount as on 31.03.2018		1.70
Less: Recoverable amount		(0.79)
Impairment loss		0.91
Less: Balance in revaluation reserve as on 31.03.2018:		
Balance in revaluation reserve as on 31.03.2016	2.10	
Less: Enhanced depreciation met from revaluation reserve		
2016-2017 & 2017-2018 = [(1.70 – 1.00) x 2 years]	(1.40)	
Impairment loss set off against revaluation reserve balance.		(0.70)
Impairment Loss to be debited to profit and loss account		0.21

AS 29: PROVISIONS, CONTINGENT LIABILITIES AND CONTINGENT ASSETS

1. An Engineering goods company provides after sales warranty for 2 years to its customers. Based on past experience, the company has been following policy for making provision for warranties on the invoice amount, on the remaining balance warranty period:

   Less than 1 year: 2% provision
   More than 1 year: 3% provision

   The Company has raised invoices as under:

Invoice Date	Amount (Rs.)
19th January, 2011	40,000
29th January, 2012	25,000
15th October, 2012	90,000

Calculated the provision to be made for warranty under Accounting Standard 29 as at 31st March, 2012 and 31st March 2013 Also compute amount to be debited to Profit and Loss Account for the year ended 31st March, 2013

Answer:

Provision to be made for warranty under AS 29 'Provisions, Contingent Liabilities & Contingent Assets'

As at 31st March, 2012 = ₹ 40,000 x .02 + ₹ 25,000 x .03
= ₹ 800 + ₹ 750
= ₹ 1,550

As at 31st March, 2013 = ₹ 25,000 x .02 + ₹ 90,000 x .03 = ₹ 500 + ₹ 2,700 = ₹ 3,200

Amount debited to Profit and Loss Account for year ended 31st March, 2013

	₹
Balance of provision required as on 31.03.2013	3,200
Less: Opening Balance as on 1.4.2012	(1,550)
Amount debited to profit and loss account	1,650

Note: No provision will be made on 31st March, 2013 in respect of sales amounting ₹ 40,000 made on 19th January, 2011 as the warranty period of 2 years has already expired.

2. 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 at 31st Dec. 2019 it goes into Liquidation. (Balance Sheet date 31-3-19)

Solution:

(i) The construction of the oil rig creates an obligation under the terms of the license to remove the rig and restore the seabed and is thus an obligating event. At the balance sheet date, however, there is no obligation to rectify the damage that will be caused by extraction of the oil. An outflow of resources embodying economic benefits in settlement is probable. Thus, a provision is recognized for the best estimate of ninety per cent of the eventual costs that relate to the removal of the oil rig and restoration of damage caused by building it. These costs are included as part of the cost of the oil rig. However, there is no obligation to rectify the damage that will be caused by extraction of oil, as no oil has been extracted at the balance sheet date. So, no provision is required for the cost of extraction of oil at balance sheet date.
10% 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.

3. Chaos Limited is in the process of finalizing its accounts for the year ended 31st March, 2020. It seeks your advice in the following cases:
   (i) Chaos Limited has filed a court case in 2014-2015 against its competitors. It became evident to its lawyers during the year ended 31st March, 2020 that Chaos Limited may lose the case and would have to pay Rs. 3,00,000 being the cost of litigation. No entries/provisions have been made in the books.
   (ii) A new regulation has been passed in 2019-2020 by the healthcare ministry to upgrade facilities. Deadline set by the government is 31.03.2021. The company estimates an expenditure of Rs. 10,00,000 for the said upgrade.
   (iii) The company gives one year warranty for its healthcare equipment under the contract of sale that it will make good any manufacturing defect by repair or replacement. As per past experience, it is probable that there will be 1% such cases and estimated cost of repair / replacement is estimated at 10% of such sale value. During the year, the company has made a sale of Rs. 5 crores.

   Kindly give your answer for each of above with proper reasoning according to the relevant Accounting Standard. Also state the principles for recognition of provision, as per AS 29.

   Solution: Principles for recognition of provisions: As per AS 29, "a provision shall be recognised when:
   (i) an entity has a present obligation (legal or constructive) as a result of a past event;
   (ii) it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation; and
   (iii) a reliable estimate can be made of the amount of the obligation. If these conditions are not met, no provision shall be recognised."

   Accounting treatment under the given scenarios:
   (i) On 31st March, 2020, since it is evident to the lawyer that Chaos Limited may lose the case and also a reliable estimate of the outflow can be made as Rs. 3,00,000, there is a present obligation. Hence, provision should be recognised for Rs. 3,00,000 for the amount which may be required to settle the obligation.
   (ii) Under new regulation, an entity is required to upgrade its facilities by 31 st March, 2021. However, on 31st March, 2020, i.e. at the end of the reporting period, there is no obligation because there is no obligating event either for the costs of upgrading the facilities or for fines under the regulations. Hence, no provision should be recognized on 31st March, 2020 for upgrading the facilities by 31st March, 2021.
   (iii) The obligating event is the sale of health care equipment with a warranty, which gives rise to a legal obligation. Here, an outflow of resources embodying economic benefits in settlement is probable for the warranties as a whole. Hence, a provision is recognized for the best estimate of the costs of making good under the warranty products sold before the end of the reporting period as follows:
   Probability of warranty cases for the entity where repair/replacement may be required as per past experience = 1% of Rs. 5,00,00,000 = Rs. 5,00,000
   Estimated cost of repair / replacement = Rs. 5,00,000 x 10% = Rs. 50,000.

4. At the end of the financial year ending on 31st December, 2005, a company finds that there are twenty law suits outstanding which have not been settled till the date of approval of accounts by the Board of Directors. The possible outcome as estimated by the Board is as follows:

	Probability	**Loss (Rs.)**
In respect of five cases (Win)	100%	-
Next ten cases (Win)	60%	-
Lose (Low damages)	30%	1,20,000
Lose (High damages)	10%	2,00,000
Remaining five cases		
Win	50%	-
Lose (Low damages)	30%	1,00,000
Lose (High damages)	20%	2,10,000

Outcome of each case is to be taken as a separate entity. Ascertain the amount of contingent loss and the accounting treatment in respect thereof.

Solution: According to AS 29 (Revised) 'Provisions, Contingent Liabilities and Contingent Assets', contingent liability should be disclosed in the financial statements if following conditions are satisfied:

(i) There is a present obligation arising out of past events but not recognized as provision.

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

(iii) The possibility of an outflow of resources embodying economic benefits is not remote.

(iv) The amount of the obligation cannot be measured with sufficient reliability to be recognized as provision.

In this case, the probability of winning of first five cases is 100% and hence, question of providing for contingent loss does not arise. The probability of winning of next ten cases is 50% and for remaining five cases is 50%. As per AS 29 (Revised), we make a provision if the loss is probable. As the loss does not appear to be probable and the possibility of an outflow of resources embodying economic benefits is remote, therefore disclosure by way of note should be made. For the purpose of the disclosure of contingent liability by way of note, amount may be calculated as under:

Expected loss in next ten cases = 40% of ₹ 1,20,000 + 10% of ₹ 2,00,000
= ₹ 48,000 + ₹ 20,000 = ₹ 68,000

Expected loss in remaining five cases = 30% of ₹ 1,00,000 + 20% of ₹ 2,10,000
= ₹ 30,000 + ₹ 42,000 = ₹ 72,000

To disclose contingent liability on the basis of maximum loss will be highly unrealistic. Therefore, the better approach will be to disclose the overall expected loss of ₹ 10,40,000 (₹ 68,000 × 10 + ₹ 72,000 × 5) as contingent liability.

INTRODUCTION OF AS, IND AS, IAS AND IFRS
&
FRAMEWORK FOR PREPARATION & PRESENTATION OF F.S.

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

Liabilities	₹	Assets	₹
Capital	60,000	Property, Plant and Equipment	65,000
Profit and Loss Account	25,000	Stock	30,000
10% Loan	35,000	Trade receivables	20,000
Trade payables	10,000	Deferred costs	10,000
		Bank	5,000
	1,30,000		1,30,000

Additional information:

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

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

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

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

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

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

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

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

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

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

Solution: **Profit and Loss Account for the year ended 31st March, 20X2**

	Case (i)	Case (ii)		Case (i)	Case (ii)
To Opening Stock	30,000	30,000	By Sales	4,50,000	4,50,000
To Purchases	4,00,000	4,00,000	By Closing Stock	32,000	40,000
To Expenses	14,900	14,900	By Trade payables	-	600
To Depreciation	13,000	5,000			
To Provision for doubtful debts	2,000	6,000			
To Deferred cost	2,500	10,000			
To Loan penalty	-	2,500			
To Net Profit (b.f.)	19,600	22,200			
	4,82,000	4,90,600		4,82,000	4,90,600

Balance Sheet as at 31st March, 20X2

Liabilities	Case (i)	Case (ii)	Assets	Case (i)	Case (ii)
Capital	60,000	60,000	Property, Plant & Equipment	52,000	60,000
Profit & Loss A/c	44,600	47,200	Stock	32,000	40,000
10% Loan	35,000	37,500	Trade receivables (less provision)	23,000	19,000
Trade payables	12,000	11,400	Deferred costs	7,500	Nil
			Bank	37,100	37,100
	1,51,600	1,56,100		1,51,600	1,56,100

2. A Ltd. has entered into a binding agreement with Gamma Ltd. to buy a custom-made machine Rs. 1,00,000. At the end of 20X1-X2, before delivery of the machine, A Ltd. had to change its method of production. The new method will not require the machine ordered and it will be scrapped after delivery. The expected scrap value is nil.

You are required to advise the accounting treatment and give necessary journal entry in the year 20X1-X2.

Answer. A liability is recognised when outflow of economic resources in settlement of a present obligation can be anticipated and the value of outflow can be reliably measured. In the given case, A Ltd. should recognise a liability of Rs. 1,00,000 to Gamma Ltd..

When flow of economic benefit to the enterprise beyond the current accounting period is considered improbable, the expenditure incurred is recognised as an expense rather than as an asset. In the present case, flow of future economic benefit from the machine to the enterprise is improbable. The entire amount of purchase price of the machine should be recognised as an expense.

Journal entry

Loss on change in production method	Dr.	1,00,000	
To Gamma Ltd.			1,00,000
(Loss due to change in production method)			
Profit and loss A/c	Dr.	1,00,000	
To Loss on change in production method			1,00,000
(Loss transferred to profit and loss account)			

3. Opening Balance Sheet of Mr. A is showing the aggregate value of assets, liabilities and equity Rs. 8 lakh, Rs. 3 lakh and Rs. 5 lakh respectively. During accounting period, Mr. A has the following transactions:

(1) Earned 10% dividend on 2,000 equity shares held of Rs. 100 each
(2) Paid Rs. 50,000 to creditors for settlement of Rs. 70,000
(3) Rent of the premises is outstanding Rs. 10,000
(4) Mr. A withdrew Rs. 9,000 for his personal use.

You are required to show the effect of above transactions on Balance Sheet in the form of Assets - Liabilities = Equity after each transaction.

Solution: Effects of each transaction on Balance sheet of the trader is shown below:

Transactions	***Assets Rs. lakh***	–	***Liabilities Rs. lakh***	=	***Equity Rs. lakh***
Opening	8.00	–	3.00	=	5.00
(1) Dividend earned	8.20	–	3.00	=	5.20
(2) Settlement of Creditors	7.70	-	2.30	=	5.40
(3) Rent Outstanding	7.70	–	2.40	=	5.30
(4) Drawings	7.61	–	2.40	=	5.21

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

Current cost of opening stock = (Rs. 12,000 / 100) x 125 = 6,000 x Rs. 2.50 = Rs. 15,000
Current cost of closing cash = Rs. 12,000 (Rs. 18,000 – Rs. 6,000)
Opening equity at closing current costs = Rs. 15,000
Closing equity at closing current costs = Rs. 12,000
Retained Profit = Rs. 12,000 – Rs. 15,000 = (-) Rs. 3,000

The negative retained profit indicates that the trader has failed to maintain his capital. The available fund of Rs. 12,000 is not sufficient to buy 6,000 units again at increased price of Rs. 2.50 per unit. The drawings should have been restricted to Rs. 3,000 (Rs. 6,000 – Rs. 3,000). Had the trader withdrawn Rs. 3,000 instead of Rs. 6,000, he would have left with Rs.15,000, the fund required to buy 6,000 units at Rs. 2.50 per unit.

You are required to compute the Capital maintenance under all three bases ie.

(i) Historical costs,
(ii) Current purchasing power and
(iii) Physical capital maintenance.

Solution: Financial Capital Maintenance at historical costs

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

Financial Capital Maintenance at current purchasing power

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

Physical Capital Maintenance

	Rs.	*Rs.*
Closing capital (At current cost) (4,800 units)		12,000
Less: Capital to be maintained		
Opening capital (At current cost) (6,000 units)	15,000	
Introduction (At current cost)	Nil	(15,000)
Loss resulting in non-maintenances of capital		(3,000)

5. A company with a turnover of Rs. 225 crores and borrowings of Rs. 51 crore during the year ended 31st March, 2021, wants to avail the exemptions available in adoption of Accounting Standards applicable to companies for the year ended 31.3. 2021. Advise the management on the exemptions that are available as per the Companies (Accounting Standards) Rules, 2021.

Solution: The question deals with the issue of Applicability of Accounting Standards for corporate entities. The companies can be classified under two categories viz SMCs and Non-SMCs under the Companies (Accounting Standards) Rules, 2021. As per the Companies (Accounting Standards) Rules, 2021, criteria for above classification as SMCs, are:

"Small and Medium Sized Company" (SMC) means, a company-

(i) whose equity or debt securities are not listed or are not in the process of listing on any stock exchange, whether in India or outside India;

(ii) which is not a bank, financial institution or an insurance company;

(iii) whose turnover (excluding other income) does not exceed rupees two-fifty crores in the immediately preceding accounting year;

(iv) which does not have borrowings (including public deposits) in excess of rupees fifty crores at any time during the immediately preceding accounting year; and

(v) which is not a holding or subsidiary company of a company which is not a small and medium-sized company.

Since, XYZ Ltd.'s turnover was Rs. 225 crores which does not exceed Rs. 250 crores but borrowings of Rs. 51 crore are more than Rs. 50 crores, it is not a small and medium sized company (SMC). The exemptions available to SMC are not available to this company.