Contents

Accounting Standard-22 : Accounting for Taxes on Income

Minimum Tax provision needed for this chapter
(i) Treatment of Donations Paid in PGBP
(ii) Disallowance under section 43B
(iii) Depreciation allowance under section 32
(iv) Deduction for Preliminary Expenses under section 35D
(v) Carry forward of losses
(vi) MAT under Section 115JB
(vii) Tax holiday on start ups
(viii) Disallowance of Provisions under Section 36

(1) This Standard is applicable to tax effects arising due to Income Tax.
In India only Income Tax Act 1961 is applied for calculation of Tax on Income

(2) The objective of this Standard is to apply accrual Concept on tax effects. For this purpose Tax expense include Current Tax and Deferred Tax.
Also Assets and liabilities include Deferred Tax Assets or Deferred Tax liabilities

(3) Meaning
Deferred Tax Asset or liability is tax calculated on timing difference.
Deferred Tax Asset / Liab = Timing Difference × Regular Rate of Tax

Current Tax = tax calculated as per Tax laws

Tax expense = Current Tax ± Deferred Tax effects

Timing Difference are those differences in accounting Income and taxable Income, which are capable of Reversal in future. This arise due to various Tax provisions.

Permanent Differences are those differences in accounting Income and taxable Income which are NOT capable of Reversal in future. This can be due to permanent allowance or disallowance

Accounting Incomes means PBT
Taxable Income means Income as per Tax laws

④ Calculation of Deferred Tax

Deferred Tax = [Allowance/Disallowance Capable of Reversal
OR
Loss capable of setoff
OR
Difference in income as per Tax & Accounts, capable of Reversal] × Rate of Tax applicable during that year.

* Do not consider Prospective Tax Rates. Always consider Tax Rates of enacted or substantively enacted Tax Law on Balance sheet date.

⑤ Journal Entries

For creation of DT. Asset	D-Tax Asset A/c Dr To P/L (Being DTA created)
For Reversal of DTax Asset	P/L A/c Dr To D. Tax Asset (Being DTA cancelled)
For creation of liability	P/L A/c Dr To DT liability (Being DTL created)
For Reversal of liability	DTax Liab Dr To P/L (Being liab. cancelled)

* DTA/DTL will be shown in Balance sheet as non current Asset or non current liability.

Note: P/L Effects in above Journal Entries are shown in Tax Expense

Statement of P/L Extract

PBT		xxx
Less Tax Expense		
Current Tax	xxx	
± Deferred Tax	xxx	xxx
PAT		

Balance sheet

Non current Liab	
D. Tax Liab	xxx
Non current Assets	
D. Tax Asset	xxx

⑥ **Examples of Timing Difference**

- Disallowance under section 43B
- Depreciation allowance under Section 32
- Unamortised Preliminary Expenses under Section 35D
- Carry forward of losses under Section 72
- Contractor Income under Section 43CB (Though this Section is not applicable now but we are doing because ICAI question are still asked on it)
- Provisions under Section 36

⑦ **Examples of Permanent Difference**

- Donation
- Personal Expenses of Promoter etc.

⑧ **Prudence limit**

In case of DTL → No Prudence requirements

In case of DTA → DTA should be created if there is reasonable certainty that sufficient income (taxable) will arise, against which DTA can be set off.

OR

If company has carry forward of losses, then there is virtual certainty that sufficient taxable income will arise in future against which such DTA can be adjusted.

(9) DTA/DTL should not be discounted

(10) Disclosure Requirements

- Always show DTA/DTL as Non Current in Balance sheet
- Give breakup of Components of DTA/DTL in notes to A/c.

(11) Deferred Tax In case of Tax holiday

Whenever any entity has tax holiday, then

- Timing difference, which arise and get reversed within Tax holiday are not relevant

Whereas

- Timing difference which arise in tax holiday but are expected to reverse after tax holiday are relevant.
DTA DTL is calculated on this difference

Accounting Standard-23

Accounting for Investments in Associate in Consolidated financial Statements

① Meaning of Associate

Enterprise, in which investor has significant influence and which is neither subsidiary or Joint venture.

Significant influence means power to participate in financial and/or operating Decisions of investee. It can be through representation on Board of directors, policy matters etc.

It can be gained by 1) Agreement or Application of law
or
2) Share ownership for 20% or more.

Assume 20% or more as significant influence unless proved otherwise
Similarly less than 20% as not significant influence unless proved otherwise.

② Associate can be Temporary or Permanent

Temporary means where influence is acquired and held to dispose off in near future or investee operates under long term restrictions which impair its ability to transfer funds to parent.

Temporary Associates are accounted using AS-13.
Permanent Associates are accounted using AS-23.

③ Treatment of Associate in Consolidated financial Statements

1) Investments are recorded at cost and adjusted for any post acquisition gain or loss. Goodwill is calculated and Identified along with.

Journal for recording calculation
Investment in Associate Dr — Post Gain Share
To Consolidated P/L
(Being Investment Revalued)

2) Adjustment for inter company debt is not made

3) Before applying AS-23, financial statements of Associate are updated.

4) use uniform Accounting policies

5) If Associate has proposed Dividend, do not treat as appropriation. Rather Associate profit should be before deduction of Proposed Dividend.

6) If Investment in Associate becomes negative, discontinue recording further loss in Associate.

7) Post Acquisition Profit of Associate should be calculated through P/L Appropriation A/c and these should be before deducting any dividend.

Any dividend paid by associate will be Eliminated by Parent in its investment.

8) If shares are acquired in steps, that is parts, then goodwill c/r should be calculated for each part

Accounting Standard-24
Discontinuing operations

① Meaning of Discontinuing Operations

Discontinuing operation is component of an enterprise

a) That enterprise, pursuant to single Plan, is
- Disposing off in entirety by sale of Components in scheme of demerger
OR
- Disposing off in piecemeal by sale of substantially all assets of component
OR
- termination through abandonment

b) That represents separate major business or geographical area of operations
AND
c) That is financially and operationally separable in financial Statements

* If all of above (a, b, c) are satisfied, then it is considered DCO.

Note: check (i) It should be Component of Enterprise
(ii) " " " based on Single Plan approved by directors
(iii) " " " disposed off - Sale Entirety
- Sale Piecemeal
- abandonment
(iv) It should be reportable Segment under AS-17
(v) " should have information + data Separate from others

② Examples of activities which do not necessarily qualify DCO but might do so with other factors

(i) Gradual phasing out of Product Line
* If Entity is phasing out a product line, it does not represent major line/segment of Entity. Hence not DCO

(II) Gradual shifting of Production from one segment to another segment
* If shifting in resources of man and machine from one segment to another segment, it is not DCO, since segment is not being disposed off.

(III) Shifting of Location of Production activities

(IV) Closing a facility to improve production or Cost Savings (B.P.O)

(V) Discontinuation of Products in product line

③ Initial disclosure Event (IDE)

If any of following Event takes place, then such event date is called Initial disclosure event Date
(i) Entity has entered into binding sale agreement for selling Substantially all assets of component of Entity
OR
(ii) Entity has made a detailed formal plan for discontinuation and made public announcement of Plan

Note Disclosures under AS-24 starts in year in which IDE date occurs. It continues till year in which operations are actually discontinued.

④ Disclosure Requirements
(i) Description of DCO
(ii) Segment of business considered as DCO
(iii) Date of IDE
(iv) Expected period required for discontinuation of operations
(v) Carrying Amt of assets which are to be disposed off under DCO
(vi) Carrying Amt of liabilities which are to be settled under DCO
(vii) Pre tax profit/loss of DCO and tax Expense if any
(viii) Cashflows of DCO arising in operating, investing + financing activities
(ix) Revenue + Expenses of DCO in Profit + loss Account.

Accounting Standard-25 : Interim financial Reporting

① IFR is a kind of update on complete financial statement of last year. This helps users in timely, better and Reliable information.

IFR can be made in compliance with listing requirement or other reasons. Apply AS-25 in preparation of IFR

Clause 33 & 41 has no relation with IFR. It deals with Interim financial Results, though measurement and recognition principles of AS-25 are applied in clause 33 + 41 reporting.

② Interim financial Report (IFR) means financial report containing either a complete set of financial statement, or set of condensed financial statements for interim period

Interim period means financial reporting period, shorter than full financial year.

* 1st year of operations may be shorter, still it is not Interim period.

③ Contents of IFR

- Basic content should include Balance sheet
  P&L A/c
  Cashflow and
  Notes to Accounts
  for Interim Period and Comparative Period

- This Basic content can be full/complete, just like annual statements or condensed.

- If such statements are complete, consider Interim Period as complete period and prepare financial statements.

- If such statements are condensed, then Head and Subheads should be as in most recent annual financial statement.

- Selected Notes to Accounts in Condensed Statements should be of Significant Events and Transaction like
  - Decline in value of Inventory
  - Impairment losses
  - Gain/loss on sale of PPE
  - Reversal of Provision
  - Litigation settlement
  - Related party Transaction
- Also statement of Policies, Methods and computation if changed.
- Note on season, unusual Assets, Liab, Income, Expense
- " " change in estimate,
- Disclosure of EPS, segment Information
- " " Any Business Combination.

④ Period should be

Balancesheet Comparative → Year end Previous year
Interim Period → last date of Interim period

Statement of P/L
Interim Period = For interim Period
For Year to Date current Period
Comparative = For Previous Year Interim Period
For Year to Date Previous year

Cash flow statement
Interim Period = Year to date Current Year
" " " Previous Year

⑤ Recognition and measurement

- Accounting policies should be same as in most recent annual financial statements.

- Income/Revenue which is seasonal, cyclically, occasionally occurring, should not be deferred or prepost poned. Examples can be Royalty, Dividend etc.
Hence record Income/Revenue as usual. Follow Accrual concept, whereever applies.

- Expense cannot be deferred, unless appropriate. Hence all expenses, losses, which are seasonal, or infrequent cannot be deferred.

- If any change in Accounting estimates occurs during Interim period, its financial effect should be fully considered in Interim period.

- Where any Accounting policy is changed during interim period, its financial effect related to Interim period should be considered in interim period. Its Earlier effect will be adjusted in year to date statements.

⑥ Variation

If at End of financial year, financial Statements vary significantly from Interim financial Reports, then such variations considered as material, should be disclosed with reason.

⑦ Entity should make best estimate for provision at End of each interim period. Any provision made Earlier will be cancelled.

Example

Make Provision for Retirement benefits at end of each Interim period and cancel any earlier provision made.

⑧ Tax treatment

- Entity should make best estimate of its Tax Expense for Year

- It should calculate weighted Avg Tax Rate for full year and then apply this rate for interim period.

Accounting Standard-26 : Intangible Assets (I.A)

① Meaning of Intangible Assets

Intangible Assets are those assets which qualify the following conditions
- These are identifiable (i.e. can be separated from Entity and sold)
- These are non monetary (i.e. not Investments, debtor, Bank etc)
- These are not having physical substance of its own
- These are held for production of goods or rendering services

Goodwill is considered as identifiable

Other Examples are Brands
Titles
Patent
Knowhow
formulations
Software & website
Franchisee Rights (Royalty paid on these right is expense)

② As per para 56, following are not Intangible Assets. These are written off as expense

Preliminary Expenses
Underwriting commission
Discount on Issue of securities
Startup Expense / Pre operative Expenses
Advertisement Suspence
Pre Incorporation Expense
Publicity Expense of new Product
Shifting of location expense
Staff Training

③ Recognition Conditions

IA should be recognised if both of following conditions are satisfied

(a) Future Economic Benefits from IA will probably flow to Entity
and (b) Cost of IA can be reliably measured

4 Initial Recognition

- Intangible Assets obtained from Govt as Govt Grant
  ↓
  Recognise @ Nominal value as per AS-12
- Intangible Assets Exchanged with other Assets
  ↓
  Recognise at fair value of IA obtained or fair value of Asset given, whichever is more clearly Evident
- Self generated Intangible Asset
  ↓
  see point no 6
- Intangible Assets Acquired / Purchased
  ↓
  Recognise it @ Cost Incurred
  meaning of Cost in point 5

5 Meaning of Cost Incurred

Purchase Price	xxx
⊖ Trade Discount	xxx
+ Import duties	xxx
Landed Price	xxx
+ GST whose credit is not available	xxx
Cost Paid	xxx
+ Expenses incurred to obtain Title	xxx
+ " " " Install (software)	xxx
+ " " " value (Before Purchase)	xxx
+ " " " Purchase (Commission)	xxx
Cost Incurred	xxx

Note : Patent Registration Expense is also capitalised with Cost of IA

Note : Additional Import Duties are like Surcharge / Cess in Income Tax

(6) Self generated Intangible Assets

- Goodwill, Title Brands
  - ↓ Do not Recognise these as assets.
  - If Goodwill is acquired in scheme of Amalgamation it is purchased Goodwill and recorded. As per AS-14 This should be written off in 5 years.
- Other Self generated IA
  - Expense incurred during Research Phase (Para 41)
    - ↓ These are Not Capitalised. These are Expenses
  - Expense incurred during Development Phase
    - ↓ These Expense will be Capitalised as IA upto Amount of future Economic Benefits (also called Recoverable Amt)

Research Phase

Note: Research Expense include failed Research

Note: Research means to obtain knowledge. It means establishment of technical feasibility.

Note: Once any expense is written off as research, it can never be capitalised again

Development Phase

Note: Development phase starts after technical feasibility has been established.

Amt capitalised in Development Stage cannot exceed (RA) Recoverable Amt. It is present value of Benefits expected after savings/Earnings from Use of IA, discounted using Cost of capital.

If Value of IA exceeds RA, then excess value is written off as Impairment Loss.

Note Packing Cost is not capitalised

⑦ Subsequent Expenditure on IA

If any IA has been fully developed and in use, but later entity incurs further expenditure, it will be

- capitalised, if such expenditure increases originally estimated future Economic Benefits.
- Expensed & written off in other cases.

Note: Expenditure incurred to defend in court any IA will always be written off.

⑧ Amortisation of IA (Amortisation means Depreciation)

(i) Intangible Asset should be amortised from date when it is Ready for use.

(ii) Ratio of Amortisation should be
- Ratio of Benefits i.e. Expected future Cash flows from IA
- SLM, if above ratio cannot be estimated

(iii) Ratio of Benefits may change in future. Then Amortisation ratio will change prospectively.

(iv) Life of IA should be taken based on future Economic Benefits. If it cannot be estimated, consider it as 10 years. Lower life can be taken, but do not take higher life, unless justified.

(v) Always assume scrap value / Residual value of IA as nil.

Note: If Entity has not correctly amortised IA, then
- Step 1 Calculate Correct value of IA as per AS-26
- Step 2 Identify Existing Book value of IA
- Step 3 Restate IA at correct value by adjusting it as prior period item.

Journal

Prior Period Item Dr (P/L) — Step 2 − Step 1
Amortisation (P/L) Dr — Current year Amortisation
To IA
(Being value of IA rectified)

9 Disclosure Requirements

- Always disclose IA with name, nature, cost, Amortisation, Book value etc
- If life is taken more than 10 years, give reason for higher life in notes to Accounts.

Accounting Standard - 27

Financial Reporting of Interest in Joint Ventures

① Order of application AS-21 1st order
AS 27 2nd "
AS 23 3rd "

② Meaning

Joint Venture is a Contractual arrangement, whereby two or more parties undertake an economic activity, which is subject to Joint Control.

Joint Control means contractually sharing of Control over Economic Entity

* Control means power to govern financial/operating policies of an economic activity so as to obtain benefits from it.

* Venturer is party to Joint Venture

③ Forms of Joint Ventures
(i) Jointly Controlled operations JCO
(ii) Jointly Controlled Assets JCA
(iii) Joint Controlled Entities JCE

④ Under J.C. operations, venturer do not create separate Entity but use own resources. Each party maintains own books and record its share of Expenses and Incomes. Generally all amts paid and received on behalf of Joint venture are recorded in Joint venture A/c

Later these Joint ventures A/c of each party are combined to prepare Draft Consolidated Profit & Loss A/c. Profits are shared in this case. It is similar to Memorandum Joint venture A/c.

⑤ Under Jointly Controlled Asset, each venturer record its own share of asset and liability. This is consolidated with other Assets and Liabilities of firm. Any Income and Expense are also recorded for each party on share basis.

* For sake of simplicity, it is better to prepare draft Combined Balance Sheet and P/L and then record share of Asset/Liabilities.

⑥ Jointly Controlled Entity

Here a new Entity is formed for the purpose of operation. This Entity prepare its own books of accounts and financial Statements. These financial Statements are prepared as usual applying various accounting standards.

Books of Venturer

Each venturer record its share of Investment in J.V as Investment. If Investments are temporary, then such Investments are shown as per AS-13 in separate financial Statements, as well as Consolidated financial Statements.
Meaning of temporary is same as in AS-23.

If Investments in Joint Venture are not temporary, then AS-27 requires application of Proportionate Consolidation method. Under this method, while Consolidating, all asset & liabilities including Income and Expenses are consolidated on line by line basis for proportionate amt.

* If any venturer receives any income from J.V, it is required using AS-9. Such party is called operator.

⑦ Transactions between venturers and Joint Venture

- Do not Record gain or loss on share of assets transferred to itself.
- Gain or loss can be recorded on share of assets sold to other venturers.
- If decline in market prices have been reported, then loss can be recorded on own share of asset also.

Transactions can be - purchase of asset for JCO & JCA
- Purchase from JCO/JCA
- Sold to JCO/JCA

Accounting Standard 28 : Impairment of Assets

① This is not applicable on level II, III and IV Entities. Also this AS does not applies to assets covered by

AS-2
AS-7
AS-13
and AS-22

Hence this AS applies to Property Plant + Equipment and Intangible Assets.

② Basic Terms

Impairment loss = Carrying Amount - Recoverable Amount

Carrying Amt means book value after depreciation and amortisation at year End. (This is after any revaluation)

Recoverable Amount = higher of value in use (VIU) or
= Net selling Price (NSP)

③ Accounting Treatment of Impairment loss

(a) Journal Entry

Revaluation Reserve Dr (1st Pref)
Impairment loss in P/L Dr
To Asset
(Being impairment loss recorded)

(b) Balance sheet Presentation

Asset cost	xxx
(-) Accumulated Dep	xxx
(-) Impairment loss	xxx
	xxx

(c) Depreciation of future periods will get reduced due to impairment loss

(d) Income Tax does not allow this, hence create Deferred Tax Assets on it

(4) Indicators of Impairment loss

External Indicators

(i) Market Price of Asset has declined Substantially
(ii) Unfavourable market Conditions against Entity in regard to demand, technology, Govt policies etc
(iii) Market Interest Rates have increased substantially
(iv) Low market Capitalisation

Internal Indicators

(i) Poor Economic performance by asset
(ii) Company has plans of Discontinuation or restructuring
(iii) Physical damage to asset

(5) Calculation of Recoverable Amount

(A) Calculation of value in use

- It means present value of net cash inflows from continuous use of asset and its residual value
- Such net cashflows should be reasonable and supportable to assumptions of management
- Generally most recent management forecasts and Budgets are used for calculation of net inflows
- Net Inflows means Gross Inflow − outflows to generate Inflows
- outflows include repairs for which management is committed
- Discount Rate should be pretax CAPM.
- Cashflows should be taken for maximum 5 years, unless Justified.
- Value in Use is calculated before Finance Cost and Taxes.

(B) Net Selling Price

= Expected Sale Price of Asset – Estimated Selling Expenses Excluding Tax & finance costs. (Example can be Commission)

Expected Selling Price is based on binding sale Price / Price in Active Market or Best Judgement of management

Note: Calculation of both V.Use and NSP is not required, if it can reliably calculate Impairment loss.

⑥ Cash Generating Unit (CGU)

CGU is the smallest identifiable group of assets working together to generate cashflows that are largely independent

Generally, if asset is capable of generating cash flows on independent basis, then such single asset is CGU. If such asset is damaged and will not be used in future consider it as separate asset, not part of CGU.

⑦ Treatment of Goodwill and Corporate Assets.

(i) Perform Bottom up test, if goodwill and Corporate Assets can be allocated on reliable basis.

(ii) Perform Bottom up test and Top down test if goodwill & Corporate assets cannot be allocated on reliable basis.

* Under Bottom up Test
  - Allocate Goodwill and Corporate assets to CGU's in consistent / Reliable Ratio
  - Compare CGU carrying Amt including Goodwill with Recoverable Amt of CGU.
  - Calculate Impairment loss in CGU
  - Allocate such Impairment loss 1st to Goodwill and Balance to other Assets in CGU in ratio of carrying Amts.

* Under Top down approach
  - Combine all CGU Carrying Amt after applying Bottom up approach.
  - Add Goodwill and Corporate Assets
  - Calculate Impairment loss
  - Allocate Impairment loss 1st to G/W (not impaired earlier)
    2nd to Corporate Assets.

Corporate Assets are Administrative assets like H.O Building and Research assets.

(8) Reversal of Impairment loss

(A) Indicators are

External (i) Market value of Assets increased substantially
(ii) favourable market condition
(iii) Market Int Rate has decline substantially

Internal (i) Company has incurred Capital Expenditure on asset
(ii) Increase in Economic performance of asset

(B) Impairment loss of Goodwill is not Reversed

(C) Reversal is lower of following
- RA - CA

  or
- Impairment loss recorded Earlier - Saving in Depreciation

(9) Disclosure Requirement.

(i) Impairment loss recorded in P&L

(ii) " " " " Revaluation Reserve

(iii) Impairment loss Reversed during the year

(iv) Segments affected by Impairment

(v) Indicator used for Calculation

(vi) Assumption applied in Calculation of RA.

(vii) CGU and its identification

Accounting standard-29 : Provisions, Contingent Liabilities & Contingent Assets

① This AS deals with
(i) Provision
(ii) Contingent Liabilities and losses
(iii) Contingent Assets or gains

② Provisions
It means liabilities measured using substantial degree of Estimation

Items	Occurrence	Amt	Remarks
creditors	sure	sure	Liab
Provision for warranty	Unsure	Unsure	Provision
Provision for Taxation	Sure	Unsure	Provision
Provision for Refund	unsure	Sure	Provision

③ Definition of Provision

Provision is a present obligation arising out of past Events, which will result in outflow of Resources and amount can be reliably measured.

④ Hence Provision has following Elements

(i) It is present obligation : means whose chance of occurrence are more than not

(ii) arising out of past Event : Some event has occurred in past which has eliminated any other alternatives

(iii) Which is expected to result in outflow of Resources

(iv) Which can be measured reliably using
(a) Expected value method i.e. Probability × Loss Amt
OR
(b) Possible outcome method or most likely outcome method where management calculate its amount

Note: While Calculating Amt of Provision, we should not deduct any expected gains of future

Note: Recovery assets or Idemnification assets will be recorded as separate assets if its realisation is virtually certain.

In P/L, Expense of Provision will get reduced with such recovery asset.

In Balancesheet Provision will be shown along with Recovery asset.

(5) Examples of Provisions

Generally in following situations, Provision is created

(a) Provision for warranty on Products : In such cases, companies create provision based on past Experience.

Provision Amt = Sale Amt × % of warranty exercised

(b) Financial guarantees. This is considered as provision, when chances of default by other party are high.

(c) legal Disputes like court cases, Tax disputes, Provision should be made, if possibility of loss is high.

(d) Provision for Restructuring Sometimes business needs to be restructured for which companies make plans in advance. Provision should be made for Expected cost of Restructuring. It should not be made for normal operating Expenses or Staff Training or shifting/Relocation Expenses.

(6) Contingent Liabilities/losses

It is possible obligation arising from past event which is expected

to arise on occurance or non occurance of uncertain future events
Also, it includes present obligation for which provision was not made due to
- non outflow of resource or
- it could not be measured reliably.

Possible obligation means whose chance of occurance is upto 50%.

Note: Treatment of Contingent Liabilities
It should be disclosed in Notes to financial statements.

⑦ Contingent Assets/Gains

These are unplanned and unexpected events, which will give rise to inflow of Resources in future and whose occurance is not yet certain.

Note: -: No Treatment for Contingent Gains/Assets. Not even disclosure.

Note: If such gain is virtually certain, then it is not contingent gain. It should be recorded as gain when it becomes virtually certain

(AMENDED AS PER GUIDANCE NOTE OF ICAI JAN 2022)

Preparation of financial statements

(A) Format of financial Statement - Schedule-3, Division-I

(B) Special Law Applications
- Calculation of managerial Remuneration
- Dividend Declaration Rules

(A) Format of financial Statements

Format of financial statements is given by Schedule-III of The Companies Act 2013. It has following Divisions

- **Division I** → To be applied by Companies applying AS → Applicable to Intermediate of CA Exams.
- **Division II** → To be applied by companies applying Ind AS → Not in course
- **Division III** → To be applied by NBFC. → Not in course

Division - I

- Format of P&L and Notes
- Format of Balance sheet and Notes
- General Points.

Format of "Statement of Profit and Loss"

Particulars	Note	Current yr	Previous Year
Revenue from operations		xxx	xxx
Other Income		xxx	xxx
Total Income	(A)	xxx	xxx
Cost of material consumed		xxx	xxx
Purchase of stock in Trade		xxx	xxx
Change in inventory of finished goods, WIP and stock in Trade		xxx	xxx
Employee Benefit Expense		xxx	xxx
Finance Cost		xxx	xxx
Depreciation and Amortisation		xxx	xxx
Other Expenses		xxx	xxx
Total Expense	(B)	xxx	xxx

Profit Before Exceptional and Extraordinary items	(A-B)	XXX	XXX
Less Exceptional items		XXX	XXX
Extraordinary items		XXX	XXX
Profit Before Tax		XXX	XXY
Less Tax Expense (Current Tax Deferred Tax)		XXX	XXY
Profit after Tax		XXX	XXX
E.P.S Basic and Diluted		XXX	XXX

NOTES on Statement of P/L

Meaning + Special Requirements	Examples
Revenue from operation - Principal or Ancillary Revenue generating Activities of Companies	• Sale of Product + Services • Grants and donations • Other operating Revenue Less Excise Duty if any.
Other Income - Other than Revenue from operations. - Do not include Negative Expense.	• Interest Income • Dividend " • Gain on sale of Asset • Other Non operating Income. • Transfer fees • Discount Income • Sale of Scrap
Cost of Material Consumed - It means only Raw material - Disclosure of opening and closing Raw material is not required.	Purchase of Raw Mat is adjusted with opening and closing stock of Raw Material. Food for Hotel Company Store and spare consumed
Purchase of stock in Trade - Include only goods Purchased for Resale	Purchases of Stock in Trade

Change in Inventory - Difference in opening and closing finished goods, stock in Trade & WIP - No need to Disclose opening & closing Just disclose change. - It will be zero, if opening, closing are same / Expected to be same	change in Inventory
finance Costs	- Interest Cost - Cost of arranging Borrowing funds.
Other Expenses	- Consumables in office - Preliminary Exp. writtenoff - Discount given - Director Fee - Director Remuneration. - P.D.D. created / cancelled
Employee Benefit Expense - Directors are not Employees.	- Salary & wages - Contribution to P.F - ESOP Expense - Staff welfare
Exceptional and Extraordinary items	- Abnormal losses or gain - Litigation settlement Exp - Retro law Expense.

Depreciation is for PPE (Tangible Assets)

Amortisation is for Intangible Assets.

Question

Prepare Profit + Loss

		DEBIT	CREDIT
Sale			10,00,000
Opening stock	Raw mat	5000	
	WIP	6000	
	finished goods	8000	
	Stock in Trade	2000	
Purchase	Raw material	300000	
	Stock in Trade	100000	
Salary + wages		200000	
Contribution to P.fund		80000	
Depreciation		30000	
Goodwill written off		20000	
Rent Income			40000
Profit on sale of machine			50000
Carriage outward		6000	
Carriage inward		8000	
Advertisement		9000	
Dividend Income			1000
Interest		15000	
Loss by fire		10000	
P.D.D Expense		5000	

Closing stocks are Raw Mat 20000, WIP 10000 and Stock in Trade 12000; finished goods 8000

Question

Prepare P&L A/C of X Ltd for 2022-23.

X Ltd has 10000 Equity Shares of ₹10 each.

Sale of goods		30,00,000
Sale of services		500,000
Purchase of Raw Material	700000	
op. stock of Finished goods	50000	
" " Raw material	40000	
Salary & wages	300000	
Director sitting fees	30000	
Gain on sale of Bitcoins		60,000
C.S.R Expense	25000	
Depreciation of PPE	30000	
Dividend Income		700000
Rental Expense	40000	
Interest Expense	90000	
Income in Survey		50000
Auditor Remuneration	8000	
Discount Income		6000
Discount Expense	18000	
Transfer fee		5000
Loss due to fire	50000	
P.D.D Expense	6000	
P.D.D Liability		6000

Adjustment Closing Stock Raw 35000

" " Finished 80000

Tax Rate 30%

Format of Balance sheet

Particulars	Note	C.Y	P.Y
Equity and Liabilities			
Shareholder funds			
Share Capital		xxx	xxx
Reserve + Surplus		xxx	xxx
Money against share warrants		xxx	xxx
Share Application Pending Allotment		xxx	xxx
Non current Liabilities			
L.T. Borrowing		xxx	xxx
Deferred Tax Liabilities		xxx	xxx
Other L.T. Liabilities		xxx	xxx
LT Provisions		xxx	xxx
Current Liabilities			
ST Borrowings		xxx	xxx
Trade Payable - MSME		xxx	xxx
- others		xxx	xxx
Other C. Liabilities		xxx	xxx
STerm Provisions		xxx	xxx
		xxx	xxx
Assets			
Non current Assets			
PPE and Intangible Asset			
PPE		xxx	xxx
Intangible Assets		xxx	xxx
Capital WIP		xxx	xxx
I. Asset under Development		xxx	xxx
Non current Investment		xxx	xxx
Deferred Tax Assets		xxx	xxx

L.T. Loan + Advance	xxx	xxx
Other Non Current Asset	xxx	xxx
Current Assets		
Current Investment	xxx	xxx
Inventory	xxx	xxx
Trade Receivable	xxx	xxx
Cash and Cash Equivalent	xxx	xxx
ST Loan + Advance	xxx	xxx
Other Current Asset	xxx	xxx
	xxx	xxx

NOTES

Items	Requirement	Presentation
Share capital	• Disclose for each class Number and Amt of Share • Disclosure Authorised Subscribed, Issued & Paid up Capital • Reconciliation Statement Beginning and End. • Rights, Preferences of each class. • Shareholders holding more than 5% shares • Bonus/Non Cash Consideration for 5 years (Nos and class) Source of Bonus not Required.	Authorised S/capital Nos X Amt XXX Issued, Subscribed + Called up Nos X Amt XXX (-) Calls in Arrears XXX Paid up S/cap XXX

Reserve & Surplus

Capital Reserve xxx
Cap. Redemption Reserve xxx
Security Premium xxx
Deb. Redemption Reserve xxx
Revaluation Reserve xxx
ESOP Reserve xxx
Retained Earnings xxx
(Can be Negative)

LT Borrowings

- It can be from Directors
- Current maturities are shown as ST Borrowings as deduction in LT Borrowings
- Show Secured, unsecured
- Show nature of security
- Show Term of Loan
- Show Source of loan (Director / Bank etc)

Bonds xxx
Debentures xxx
Deposit xxx
Fixed Deposit xxx
Deferred Payment Liabilities xxx
Finance lease Liabilities xxx

Deferred Tax Liab/Asset

- Tax Calculated as per AS-22
- It is not actually Paid.

Other LT Liabilities → Payable of Long term in nature like Creditors for Machinery.

LT Provisions → Provision for Retirement Benefits

ST Borrowings → Bank overdraft
Loan Repayable on demand
" " to Related Parties
Deposits
Other Loan

Current maturities of LT Borrowings. along with source of Borrowing

Trade Payable

- Give Ageing schedule
  0-12m
  12-24m
  24-36m
  others
- Give it for MSME and others
- Include Bills Payable

Other Current Liab

- Accrued Interest
- Income Received in Advance
- Unpaid/ Unclaimed Dividend
- Application money for Refund
- Unpaid matured Deposit

ST Provision

- Provision for Tax less Advance Tax

PPE

Always show Cost, Acc. Dep

" " Reco. Statement

(OBalance, Addition, Deletion, Closing Balance
Depreciation op, charged, closing)

If asset held for sale show it as current Asset

Classify them as Land, Building, Plant + Equipment
Furniture, fitting, vehicle, Office Equipment, leased Assets.

Intangible Assets

- G/W, Brand, Software, Title, mining Rights

- Give Reco. as above

Non current Investment

- Show Investment Property, Investment in Equity, Pref Shares, Govt Bonds, Debentures, Mutual Fund, Partnership firm

- Show value Basis (cost or fair value)

- " Quoted, unquoted, Provision for decline

Long term Loan & Advance

- Capital Advance
- Advance to Related Parties

- Show details of Secured, unsecured, etc

Other Non Current Assets

- LT Receivable (Sale of Plant)
- Security Deposit
- Give Ageing schedule
- Show Good, Doubtful
- " Unsecured, Secured

Current Investment

- Show Investment Property, Investment in Equity, Pref Shares, Govt Bonds, Debentures, Mutual Fund
- Show value Basis (cost or fair value)
- " Quoted, unquoted, Provision for decline

Inventory

- Disclose details of Raw mat, WIP, Stock in Trade and finished goods
- Stores
- Loose Tools (If meet definition of PPE, then it is shown as PPE)
- Show mode of valuation

Trade Receivable

- Give Ageing Schedule (Generally given 6m or more)
- Include B/Receivable
- Show unsecured, secured
- Reduce P.D.D

Cash and Cash Equivalent

- Show Non Scheduled Bank separately
- Include Cash, Bank, cheque in hand
- Margin money
- Bank Deposit (0-12 month)

STL & Advances

- Loan to Directors / Related Parties
- Small Advances
- Staff Advance
- Secured/Unsecured

Other CA

- Balance items like Accrued Int
- Advance Tax less P/Tax
- Prepaid Expenses

Contingent Liabilities

- Claims against companies, not acknowledged as debt
- Guarantee and Commitments
- Uncalled liability on Partly Paid shares
- Contracts Pending execution
- Bills discounted not matured
- Proposed Dividend
- Unused Borrowings from Banks

Meaning of Current and Non Current

Asset is current if any of condition satisfied

a) Expected to be realised in normal operating cycle or intended for Sale / consumption in operating cycle.

b) Held primarily for Trade

c) Expected to realise within 12 months after reporting date

d) Cash and Cash Equivalents.

* Normal operating cycle is time between Acquisition of asset for Processing and Realisation of Cash.

* If can't calculate operating cycle, assume 12 months

Liability is classified as current if

- Expected to be settled in operating cycle
- Held for Trade
- Due to be settled within 12 months after reporting date.
- Entity does not have unconditional right to defer settlement of liability for at least 12m after Reporting date

General Point

(1) Conflict of AS and S-III, then apply AS (not S-III)

(2) Round off Mandatory

Total Income (Revenue from operation and other Income)

- less than 100 cr → Round off in Hundred, lakh, millions.
- 100 cr or more → " " millions, crores.

(3) Format items are minimum line items. These can be increased if needed.

(4) Cash flow not Required by One person company and Startup Companies.

(5) Any Income + Expense exceeding (1% of Revenue or ₹ 100000 whichever is higher) should be disclosed.

6) Payment made to
- Auditors
- Directors
- CSR expense

Disclosure must

Auditors can be paid for Audit fee, Tax Matters, Law Matters Management Service, Other Service, out of Pocket Expenses.

7) from 1/4/21 Disclosure Required for
- Undisclosed Income in Tax survey
- Details of Crypto/Virtual Currency (Trade, Profit/Loss etc)

- Benami Properties
- Name of valuer
- Date of Becoming Wilful defaulter
- Relationship with struck off Companies

8) Ratios
   - Current
   - Debt Equity & Debt Service Coverage
   - ROE, ROCE, ROI
   - Turnover Ratio - Inventory, T. Receivable/Payable
   - N.P. Ratio

Adjustments

1) Revaluation of PPE

PPE
To Revaluation Reserve
(Being PPE Revalued)

2) Treatment of Proposed Dividend (upto year End) = Disclosure

3) Concept of Corporate Dividend Tax Deleted

4) for any Error, Journalise Rectification Entry like

- Sale of asset shown as suspense A/c

Suspense A/c Dr
Acc. Depreciation Dr
To PPE
To gain on sale
(Being PPE sold)

- Purchase include Advertisement Expense

Advt Expense Dr
To Purchase
(Being Purchase rectified)

- Salary include installation of Machine

Machine Dr
To Salary
(Being expence capitalised)

- B/R dishonoured and declared Bad

Bad debts Dr
To B/R
(Being B/R written off)

5) Charge Depreciation

Depreciation
To Acc. Depreciation
(Being dep charged)

P&L A/c Dr
To Dep.
(Being dep written off)

6) Issue of forfeited shares

Share capital Dr (Reiss. Price - Calls unpaid)

To capital Reserve

7) Outstanding Expense

Expense A/C Dr

To Expense Payable (Trade Payable) or OCL

(Being expense recorded)

8) Prepaid Expense

Prepaid Expense Dr (other C Asset)

To Expense

Being prepaid Expense Recorded)

9) Accrued Interest shown in Loan liability

Loan Liability Dr

To Accrued Interest (other Current Liab.)

(Being Interest Rectified)

10) Purchase A/C

To Op. Stock	xxx	By Adjusted Purchase or COGS	xxx
To Purchase	xxx		
		By Cl. Stock	xxx

11) Make Provision for Doubtful Debts

Provision for D.D Expense Dr
To P.D.D
(Being P.D.D Expense recorded)

P/L A/C Dr
To P.D.D. Expense
(Being P.D.D. Expense written off)

12) Calculate Tax on PBT

(B)

Managerial Remuneration

- For Private Ltd Companies
  - No Limit
- Public Limited
  - Maximum Remuneration can be higher of
    - As per Section 197
      - Overall Limit is 11% of Profit Calculated under Section 198.
      - (Powerful)
        - Managing Director/Manager or Whole time Director(s)
          - Only 1 MD or Manager
            - 5% of Profit
          - 2 WTD or more
            - 10% of Profit
        - Other Directors
          - Without MD Manager or WTD
            - 3% of Profit
          - With MD/Manager or WTD
            - 1% of Profit
    - or
    - Schedule V
      - Remuneration for Loss making companies or Inadequate Profit companies
        - See next Note

* These Limit can be increased by approving it in Special Resolution (Earlier Central Govt Approval was needed, now Removed)

* Approval of creditors to whom Defaulted is Required.

Note: Schedule V

Range of Effective Capital	Other than Independent Directors Maximum Remuneration Per Person Per Year	for Independent Directors. Maximum Remuneration Per Person Per Year
Negative to less than 5cr	60 lakh p.a	12 lakh p.a
from 5cr to less than 100cr	84 lakh p.a	17 lakh p.a
from 100cr to less than 250cr	120 lakh p.a	24 lakh p.a
from 250cr & Above	120 lakh p.a + 0.01% of Effective Capital exceeding 250cr	24 lakh + 0.01% of Effective Capital exceeding 250cr

* These limit can be increased by approving it in special Resolution (Earlier Central Govt Approval was needed, now Removed)
* Approval of creditors to whom Defaulted is Required.

Calculation of Effective Capital

EC = Eq. Share Cap + Pref Share Capital + Security Premium

+ other free Reserve / losses + LT Debt / Loan / Deposits
+ Capital Reserve if cash Realised

Less Investments in Case of Non Invt Companies.

Less Losses / Preliminary Expenses not written off

* Do not include Revaluation Reserve or Share Application money Pending allotment, Short term Liabilities or Advance for shares to be issued; Capital Reserve if not Realised in cash

NOTE Calculation of Profit as per section 198

PBT (Correct Profit) Before Director Remuneration	XXX
(+) Depreciation charged	XXX
- Depreciation as per section 123 or Schedule - II	XXX
- Unrealised Profit / Revaluation Profit (if included above)	XXX
Profit under section 198	XXX

* Director sitting fees is allowed and hence consider it as normal expense.

No limit on Director sitting fees.

Note: Managerial Remuneration is treated as expense and if not paid, then liability.

Excess Remuneration Paid is Staff Advance.

Question

Draft Statement of P/L of A ltd non Invt company

Sale	70,00,000
Other Income	10,00,000
	80,00,000
Cost of Material Consumed	300000
Purchase	20,00,000
Change in Stock	100000
Employee Benefit	300000
Finance Cost	400000
Depreciation	100000
Other EXP	10,00,000
	4200000
PBT	3800000
Tax Expense	10,00000
PAT	2800000

Balance sheet

S/Capital	5000,000
R/S	10,00,000
NCL – LT Borrowing	90,00,000
CL – Trade Payable	80,00,000
	230,00,000
PPE	50,00,000
NC Investment	10,00,000
CA	1,70,00,000
	2,30,00,000

Other Expense include Manager Remuneration of ₹600000 Dep schedule II 300000. Reserve + Surplus include Revaluation Reserve 300000.

Calculate M. Remuneration assuming 1 WTD, 1 PTD and 1 Independent Director.

Divisible Profit (Section 123 of The Companies Act 2013)

Company Can pay dividend out of

Current year Profits

↓

Allowed from Divisible Profits of Current year without limit.

↓

Calculation of Current Year Divisible Profit

Net Profit	xxx
+ Dep Charged	xxx
− Dep as per S-II / Section 123	xxx
Divisible Profit	xxx

Accumulated Past Profit

↓

Allowed with limit.

↓

Limit given by Companies Declaration of Dividend Rules 2014

↓

Lower of following

(i) Accumulated free Profits (P&L + General Reserve) less 15% of ESC + PSC

OR

(ii) 10% of Paid up S/Capital (ESC + PSC) + Acc. free Reserve (P&L + G/R)

Note: Rate of Dividend shall not exceed more than Avg Rate of Dividend in Past 3 years.

Question X Ltd has

ESC	5500,000
10% PSC	20,00,000
P&L Accumulated	10,00,000
G/R "	200000

In past X Ltd has distributed 6% Avg Dividend
Company wants to use past Profit to distribute 40% as Dividend.

Current year Divisible Profit is ₹ 300000

Calculate how much dividend can be distributed?

Question

9% PSC	20,00,000
ESC	50,00,000
GR (Past)	10,00,000
P&L (Past)	9,00,000
Current PAT	7,00,000

Avg Dividend past 3 year 10%
Company wants to declare @ 12%

Check can company distribute 12% as dividend?

Question

9% PSC	20,00,000
ESC	50,00,000
GR (Past)	10,00,000
P&L (Past)	9,00,000
Current PAT	7,00,000

Avg Dividend past 3 year 40%.
Company wants to declare @ 35%.

Check can company distribute 12% as dividend?

Cash Flow Statement (Accounting Standard-3)

[All Companies except one person company are required to prepare CFS]

① Cash Flow Statement is a statement specifying flow of cash and cash Equivalents during a period.

It should classify flows into

- Cash Flow from operating Activities
- Cash Flow from Investing Activities
- Cash flow from Financing Activities

② Cash Flow Statement is prepared to understand main sources of Inflows and outflows of Cash and Cash equivalents. It is useful to analyse Cash management policies of Entity and Business Valuation Information.

- This Statement is Useful in analysis of flow of Cash and Cash Equivalents.

- This Statement is also useful for identifying Over trading / Under trading in Entity.

- This helps in Better Comparison

- " " " improvement in budget.

(3) Cash and Cash Equivalents means - Cash in hand

- Cash at Bank

- Marketable Securities

where marketable securities means investments which are readily realisable within 3 months like Treasury Bonds etc.

(4) Cash Flow from Investing Activities means flow of Cash arising from fixed assets and Investments including Interest Income from Investments.

Note: For Financial Institutions like Banks, Investments are operating items and Interest on such Investments is also operating in nature.

Examples of Cash flow from Investing Activities

- Sale/Purchase of Property Plant & Equipment
- " " " Investments (other than Marketable)
- Interest on Investments
- Pre Acquisition dividend
- Post Acquisition dividend

(5) Cash Flow from financing Activities means flow of cash and cash equivalents arising from Share Capital and Borrowings including Service cost on them.

Service cost on Share Capital is Dividend Paid
" " " Borrowings is Interest Paid

Examples of Cash Flow from financing Activities

- Issue of Share Capital
- Receipt of Security Premium
- Issue of Debentures
- Payment of Interest
- Payment of Dividend

(6) Cash Flow from Operating Activities means flow of Cash and Cash equivalent from activities of operation and residual activities i.e. Flows which are neither financing nor investing in nature
Cash Flow from operating Activities can be derived by applying either
- Direct Method (Para 18a of AS-3)
- Indirect Method (Para 18b of AS-3)

Examples of operating Activities - Direct method

- Cash Sale
- collection from Debtors
- Payment to creditors
- Payment of operating Expenses
- Payment of Tax etc

(7) Preparation of Cash Flow Statement directly from Cash A/c, Bank A/c and Marketable Securities A/c. Here we need just 3 ledgers.

Step 1 Combine Cash and Cash Equivalents

- Cash A/c
- Bank A/c
- Marketable Securities A/c

Step 2 Eliminate Contra items in these ledgers

Step 3 Balance items are posted directly in Cash Flow Statement.

(8) Preparation of Cash Flow Statement from 2 Balancesheets and additional information.

Here we need various ledgers. Information extracted from these ledgers will be used to prepare Cash Flow Statement.

Cash Flow from operating Activities is calculated using Direct method i.e. selecting Cash/Bank in operating ledgers.

Cash Flow from operating activities is calculated using Indirect Method i.e. selecting non cash items in operating ledgers.

Note: Direct Method is applied by Insurance Companies whereas listed companies apply Indirect Method (SEBI Requirement)

Note: Indirect Method provides better information for valuation tools, hence it is preferred.

Note: following steps are applied in preparing various ledgers

Step1 : Prepare various ledgers from available information by applying Best Assumption.

Step 2 Select items of Cash/Bank or Non Cash Non operating items to calculate CFOA

Step3 Prepare Cash Flow Statement.

(9) How to prepare various ledgers?

(9A) P&L Appropriation Account

To General Reserve created	xxx	By Balance b/d	xxx
To other Reserve created	xxx	By Net Profit/PAT	xxx
To Dividend Paid	xxx	By General Reserve written back	xxx
To Corporate Dividend Tax (Now deleted but Question exist)	xxx	By other Reserve written Back	xxx
To Bonus Share	xxx		
To Premium on Redemption of Preference Share	xxx		
To Premium on Buy Back	xxx		
To Balance c/d	xxx		
	xxx		xxx

Note: All items relating to Shareholder (Equity or Preference) will be shown in Pr App A/c like Distribution to them.

Note: Any tax on such distributions is also Appropriation item.

Note: Transfer between Reserve is also appropriation

(9B) Fixed Assets / Property Plant and Equipment A/c

- If gross and Accumulated Dep is given
  or
  If net and Opening, closing Accumulated Depreciation is given
  ⇓
  Apply Gross Method ie.
  Prepare - Gross Fixed Asset at Cost A/c
  - Accumulated Depreciation A/c
  - Asset Disposal A/c.

- If Net values are given
  ⇓
  Prepare Fixed Assets (Net) A/c

* Accumulated Depreciation is also called Provision for Depreciation.

Gross method

Gross Assets A/c

To Balance b/d	xxx	By Asset Disposal A/c	xxx
To Bank - Purchase	xxx	By Revaluation of PPE	xxx
To Revaluation of PPE	xxx	By Balance c/d	xxx

Accumulated Depreciation / Provision for Dep A/c

To Asset Disposal A/c	xxx	By Balance b/d	xxx
To Balance c/d	xxx	By Depreciation charged	xxx

Asset Disposal A/c

To Gross Asset	xxx	By Acc. Depreciation	xxx
To gain on sale (P/L)	xxx	By Bank - sale	xxx
		By Asset written off	xxx
		By loss on sale (P/L)	xxx

Net method

To Balance b/d	xxx	By Bank - sale	xxx
To Bank - Purchase	xxx	By loss on sale	xxx
To Revaluation of PPE	xxx	By Asset written off	xxx
To gain on sale	xxx	By Revaluation of PPE	xxx
		By Depreciation (P/L)	xxx
		By Balance c/d	xxx

Note: If Question is silent about date of sale or Purchase of asset, assume 1st day of Year.

Note: If depreciation rate is given, with information about Sale/Purchase is missing then amount of depreciation is to be Calculated as follows

- All sale Purchase are on 1st day of Year
  ⇓
  $\frac{\text{Closing Balance of PPE}}{1-\text{Rate}} \times \text{Rate}$

- Sale Purchase have dates other than 1st day of year
  ⇓
  Calculate Dep on each transaction assuming x

(9C) Investment Account

To Balance b/d	xxx	By Bank - Sale	xxx
To Bank Purchase/Sale	xxx	By loss on Sale	xxx
To gain on sale	xxx	By Bank - Pre Aquisition Dividend	xxx
To Bonus	NiL	By Balance c/d	xxx

(9D) Dividend A/c / unclaimed Dividend A/c / Dividend Payable A/c

(Do not prepare Proposed Dividend)

To Bank - Dividend Paid	xxx	By Balance b/d	xxx
		By P&L App - Dividend Declared	xxx
To Balance c/d	xxx		

Note: If question does not have information about dividend declared & dividend Paid, then Best assumption is always assume opening Dividend Payable get paid during the year.

Note: Dividend Amt = Dividend Rate × PAID UP Share Capital

Note: Preference Dividend is also calculated and presented just like above equity dividend.

Note: If Question declares Equity dividend but is silent on Preference dividend, then best assumption is that Preference dividend has also been declared.

(9E) Taxation A/c or Provision for Tax A/c or Tax Payable A/c

To Balance b/d (Advance Tax)	xxx	By Balance b/d (Provision for Tax)	xxx
To Bank - Tax Paid	xxx	By P/L (Provision for Tax made)	xxx
To TDS deducted	xxx	By Bank - Income Tax Refund	xxx
To Balance c/d (Provision for Tax)	xxx	By Balance c/d Advance Tax	xxx

Note: If Q is silent on Tax Paid + Provision for Tax made during the year, Best assumption is that opening Tax liability (if any) was paid during the year.

Note: Tax is always assumed to be of business. Hence recorded in P/L A/c. (In non company case it is treated as drawings and shown in Capital A/c)

(9F) Interest Receivable A/C

To Balance b/d	xxx	By T.D.S	xxx
To Interest Income (PL)	xxx	By Bank - Int Received	xxx
		By Balance c/d	xxx
	___		___

Note: If Q provides rate of Interest on Investment then calculate Interest on Investments as Int Income based on rate.

Note: Always assume all transactions of Sale Purchase on 1st day.

(9G) Debentures/Bonds A/C

To Bank - Redemption	xxx	By Balance b/d	xxx
To Share Capital - Conversion	xxx	By Bank - Issue	xxx
To Balance c/d	xxx	By P/L B.F	xxx
	___		___

(9H) Share Capital A/c

To Bank Buy Back	xxx	By Balance b/d	xxx
To Bank - Premium on Buy Back	xxx	By Bank - Issue	xxx
		By Debenture - conversion	xxx
To Balance c/d	xxx	By Pr App (Bonus)	xxx
		By CRR Bonus	xxx

Note: If security Premium is also received, then it is financing activity.

Security Premium A/c

		By Balance b/d	xxx
		By Bank Premium Received	xxx
To Balance c/d	xxx		

Preference Share Capital A/c

To Bank Redemption	xxx	By Balance b/d	xxx
		By Bank - Issue	xxx
To Balance c/d	xxx	By P/L App (B.F)	xxx
	___		___

(9 I) Interest Payable A/c

To Bank - Int Paid	xxx	By Balance b/d	xxx
To Balance c/d	xxx	By P/L - Expense	xxx
	___		___

Note: If Int is to be calculated

= Liability x Rate of Interest

It is also called hidden Adjustment.

This ledger can be avoided.

(9J) Debtors

To Balance b/d	xxx	By Provision for D.D	xxx
To change in Debtors (B.F)	xxx	By Balance c/d	xxx

Provision for Doubtful debt A/c

To Debtors - Bad debt	xxx	By Balance b/d	xxx
To Balance c/d	xxx	By P/L - Provision made	xxx

(9K) Capital Reserve A/c / Revaluation Reserve

		By Balance b/d	xxx
		By Revaluation of Asset	xxx
To Balance c/d	xxx		

General Reserve A/c

To CRR - Transfer	xxx	By Balance b/d	xxx
To Balance c/d	xxx	By P/L App - created	xxx

Capital Redemption Reserve A/c

To Share Capital Bonus	xxx	By Balance b/d	xxx
		By General Reserve	xxx
To Balance c/d	xxx	By P/L App	xxx

(10) Preparation of Cashflow from operating Activities using direct method

Cash collection from Debtors	xxx
Cash Paid to creditors	(xxx)
" " " operating Expenses	(xxx)
CFOA Before Tax	xxx
(-) Tax Paid	xxx
CFOA Before EOI	xxx
(-) EOI	xxx
CFOA	xxx

(11) Calculation of CFOA under Indirect Method

Profit Before Taxation	XXX
Non operating items	
+ Depreciation PPE	XXX
+ Amortisation of Intangible Asset	XXX
+ Loss on Sale of PPE/Investment	XXX
− Gain " " " "	XXX
− Interest Income/Dividend Income	XXX
+ Interest Expense	XXX
+ Premium on Redemption of Debent	XXX
+ Provision created	XXX
Operating Profit Before Working Capital Change	XXX
± Change in operating Current Asset or	
± " " operating Current Liabilities	

10. − Increase in operating CA	xxx
+ Decrease in operating CA	xxx
+ Increase in " CL	xxx
− Decrease " " "	xxx
Cash Profit Before Tax & EOI	xxx
Less Tax Paid	xxx
Cash Profit Before EOI	xxx
Less EOI (operating)	xxx
CFOA	xxx

(12) Revaluation of Current Assets / Liab.

If Question provides information that few assets or liabilities have been revalued upward or downward then, in such cases

Step1 Calculate correct value of Asset/Liab ignoring Revaluation.

Step2 Find out Revaluation Amt and Eliminate its effect. (since it does not have any effect on cash flow)

- Reserve/Surplus will also get changed
- Asset/Liab. " " " ".

Step3 Start Cash Flow after eliminating effect of Revaluation.

(13) Special items

(13A) Meaning of Cash and Cash Equivalents

It includes,

	Cash in hand	xxx
+	Cash at Bank	xxx
+	Demand deposits with Bank (These are v. short term FD)	xxx
+	Any foreign exchange held (foreign currency x closing Rate)	xxx
		XXX

Hence Any liquid Investment which is

- very short term
- has no significant Risk
- is Readily Realisable (i.e. Market Exists)

Bank Overdraft is not Bank Balance, hence it is financing activity.

(13B) Cash at Bank means Bank Balance as per CashBook (Not PassBook)

(13C) Extraordinary items are Abnormal items like

- Abnormal loss by fire
- Settlement of law suit
- settlement gain by lottery
- Insurance claims

These are shown in CFS as separate item. as last item.

(13D) Treatment of Govt Grants

Govt Grants are treated as follows

Receipt of grant for land = Investing Activity

" " " as Promoter = financing Activity

" " for PPE/capital Grant = Investing Activity

" " " Expenses = operating Activity.

* Amortisation of Capital grant

since PBT includes amortisation of grant as income, it should be deducted from PBT in OA.

(13E) Proceeds of calls in Arrears

It is financing activity

(13f) Underwriting Commission Paid

It is also called financing activity.

(13g) For financial Institutions like Banks, Stock Brokers, non Banking finance Companies, following is relevant.

Loan & Advance Granted ⇒ OA

Int on Loan Earned ⇒ "

Purchase of Shares, Bonds, Options, Derivative ⇒ OA

Earnings from " " " " ⇒ OA

* Loan & Advance to Suppliers and Employees is Always considered operating activity. Similarly Int Earned from such Supplies is also OA.

(14) CFS should have following disclosures

(i) Reconciliation of Cash and Cash Equivalent opening and closing Balance.

(ii) Significant Non Cash Transaction should be disclosed.

(iii) Unused Borrowings should be disclosed

(iv) Cash & Cash Equivalent not available for use should be disclosed.

Buy Back of Securities (Section 68 to 70 of Companies Act 2013)

① BuyBack means cancellation by repayment of securities (generally Equity Shares). BuyBack is a way to repay capital. BuyBack is used by companies to
- Increase controlling share
- Avoid takeover by other person
- Improve capital based Ratios e.g. Debt Equity Ratio or Dividend per share Ratio
- Helps management by lower participation by shareholders.

② BuyBack is restricted by certain limits imposed by section 68. The reason for such restriction is to secure creditors of company.

Apart from restrictions, Section 68 and 69 require compliance, which again improve security of creditors of company.

Only fully Paid Equity shares can be bought back. This also improves security of creditors.

③ Following journal Entries are required for buyback

(i) Equity Share Buy Back A/c Dr
To Bank
Being amt paid on share BuyBack

(ii) Equity share capital A/c Dr — Paid up Capital
Premium on Buy Back Dr — Excess Amt paid up
To Equity share Buy Back A/c
(Being share Buy Back adjusted with capital)

(iii) Security Premium / General Reserve or P&L A/c Dr
(1st Pref) (2nd Pref)
To Premium on Buy Back
(Being Premium on Buy Back adjusted)

(iii) Revenue Reserve A/c Dr
To Capital Redemption Reserve
(Being CRR created)

* we can use security Premium also

Note: Amount of CRR should be

Paid up value of capital Bought Back	x
(-) fresh issue of any shares for the purpose of BuyBack	xxx
CRR Required	xxx

Note: If sufficient funds are not available for payment, assume Bank OD.

Note: Sometimes question requires sale of Investment or Raising loan then follow question requirements.

Note: After BuyBack, Balance Sheet should be prepared with note in capital about BuyBack. This is requirement of S-III

Note: Revenue Reserve means free Reserves ie.
- General Reserve
- P&L A/c
- Retained Earnings
- Surplus
- Dividend Equalisation Reserve

Note : CRR can be used only for Bonus Issue of Shares (Section 69)

(4) Additional Journal Entries

(i) Sale of Investment

Bank A/c Dr
To Investment
(Being Investment Sold)

* Diff in P&L as gain/loss on sale of Investment

(II) Raising Bank loan

Bank A/c Dr
To Bank loan
(Being loan raised)

(III) Buy Back Expense

B/back Expense A/c Dr
To Bank
(Being expense Paid)

* Buy Back Expense will be written off in P/L.

(IV) Issue of Pref shares (will affect CRR Amount)

Bank A/c Dr
To Pref-share Application & Allotment
(Being amt received on application)

Pref share Application & Allotment Dr
To Pref share capital
(Being amt transferred)

(V) Issue of Debentures (Does not affect CRR)

Bank A/c Dr
To Debenture Application & Allotment
(Being debenture Application received)

Debenture Application & Allotment Dr
To Debentures
(Being amount T/F)

(VI) Cancellation of own Debentures held as Investment

Debentures (Liab.) A/c Dr — Paid up Amt
To Investment in own Deb — Book value
To gain/loss on cancellation — B.F
(Being own Debentures cancelled)

* gain on cancellation will be T/F to P/L A/c.

(VII) Redemption of Pref. Shares (Section 55)

- Pref. share capital Dr Paid up Amt
  Premium on Redemption Dr Excess Amount
  To Pref share holder
  (Being amt transferred)

- Pref Shareholder A/c Dr
  To Bank
  (Being amount paid)

- Reserve and Surplus Dr
  To Premium on Redemption
  (Being Premium on Redemption W/off)

* Company is covered by Section 133 ⇒ P/L/GR (ICAI assumes)
" " Not " " " " ⇒ S/Premium, P/L, GR

* In Buy Back Security Premium is assumed to be free Reserve
Hence we always use security premium, then General Reserve, but
not is Section 55

Revenue Reserve Dr
To CRR
(Being CRR created under section 55)

* Rule for CRR calculation is same as in Buy Back i.e.
after Reducing fresh issue made for the purpose.

(VIII) Bonus Share Issue

CRR A/c Dr
Other Reserve Dr
To Bonus Issue
(Being Bonus announced)

Bonus Issue Dr
To Share Capital
(Being Bonus allotted)

Note: Transfer

Gain/loss on sale of Investment/Fixed Asset	= P/L
Gain/loss on cancellation of own Debentures	= P/L
ESOP cancellation	= G. Reserve
E Share BuyBack Premium Paid	= Security Premium, then Revenue Reserve
Pref Share Redemption (Section 133 Company)	= Revenue Reserve
Pref Share Redemption (Non Section 133 Company)	= Security Premium, then Revenue Reserve
CRR (S-55)	= only Revenue Reserve
CRR (S-69)	= Allowed from S/Premium but ICAI use only Revenue Reserve + give note
BuyBack Expenses	= P/L
Bonus Issue	= CRR, then S/Premium then Revenue Reserve.

5) Section 68 (Theory)

(i) Sources of Buy Back

- Fresh Issue of any Shares for Buy Back
  OR
- Free Reserve (including Security Premium)

* If source of Earlier issue of Shares, it should not be of same kind.

(ii) Conditions of Buy Back

- Allowed by Articles of Association
- Shares should be fully paid
- Special Resolution to be passed in General Meeting

Exception: If BuyBack is of less than 10% of Total Paid up capital + Free Reserve, Then Special Resolution is not Required, But Board Resolution is Required.

(iii) Limit on Buy Back

(A) If Buy Back is of Equity Shares, then take lower of

(a) 25% of [Total Paid up up value (Eq + Pref) + Free Reserve]

(b) Ratio of $\frac{\text{Secured + Unsecured Debt}}{\text{Post Buy Back Paid up S/capital + Free Reserve}} \leq \frac{2}{1}$

(c) 25% of No of E Shares (Paid up Equity Share Capital)

(B) Other Securities (Not in our course)

(iv) Other Compliance

(a) Follow regulation of SEBI and Company Rules in this regard or pay penalty.

(b) Post Buy Back, submit Solvency Certificate and Statement of Buy Back to authorities

(c) Do not make fresh issue for 6m of same kind of securities

(d) Do not further Buy Back for 1 year

(e) Buy Back can be from open Market or shares held by Employees under ESOP or proportionate Buy Back

* For Section 68, security Premium is free Reserve

6. Section 69

This Section requires creation of CRR, if Buy Back is from free Reserve or security Premium. CRR will be of nominal value of capital Bought Back. CRR can be used for Bonus issue

7. Section 70

Prohibits Indirect Buy Back through subsidiary company or Investment company

(8) Limit (in formulas)

BuyBack can be lowest of following

(a) 25% of Number of Equity shares = No of Shares to be Brought Back

or

(b) $\frac{25\% \text{ of [Total Paid up Capital Equity + Pref + Free Reserve including Security Premium]}}{\text{BuyBack Price}}$

= No of share That can be Brought Back

(c) $\frac{\left(\begin{array}{l}\text{Total Paid up Capital} \\ \text{(Equity + Pref)}\end{array} + \begin{array}{l}\text{Free Reserve including} \\ \text{S/Premium}\end{array}\right) - \frac{1}{2}\,\text{Debt}}{\text{BuyBack Price + Paid up Value per Equity Share}} =$

No of share That can be Brought Back

* Debt here means All Liabilities (LT, ST, Current) without Provision.

Example : Calculate how many shares can be Brought Back assuming BuyBack Price is ₹12 per share

E Share Capital (₹10 each)	₹10,00,000
S/Premium	₹300000
G/Reserve	₹200000
Debt	₹2700000

Amalgamation, Absorption and External Reconstruction
(Accounting Standard-14 : Accounting for Amalgamation)

Topics
a) Calculation of Purchase Consideration
b) Books of New Company, in case of purchase
c) Books of New Company, in case of merger/Pooling of Interest
d) Books of old Company

① Meaning

- Amalgamation means where two or more Companies are combined to form a new company. The general reason are economies of scale.

- Absorption means where existing company takes over another Existing company. The general reason is to reduce competition or growth.

- External Reconstruction means one existing company is restructured to form new company. The general reason is to restructure capital/business.

  * Internal Reconstruction means saving a bankrupt Company by changing its debt or altering its share capital. Its external structure remains same.

  * In our exams Absorption or take over means combination of Companies. This is generic word. AS-14 specifies Amalgamation/Absorption or external Reconstruction to be
    - In nature of Purchase
    - In nature of Merger/Pooling of Interest Method

* Demerger/Spinoff means splitting off company into two or more companies. This chapter is in CA final.

② Books of New Companies in case of Purchase
Following Journal Entries are required

(a) Business Purchase A/c Dr P.C
To Liquidation of old company P.C
(Being Business purchased)

(b) Sundry Assets A/c Dr Agreed value
To Debenture holder Agreed value
To Sundry Liabilities Agreed value
To Business Purchase P C
(Being Sundry Asset/Liab taken over)

* Any difference will be recorded as Goodwill/Capital Reserve

(c) Liquidation of old company Dr P C
To Eq. share Capital
To % Pref share Capital
To Cash
To Security Premium
To Any other Payment
(Being P.C Paid)

(d) For payment by new company other than P.C
Expense of old co paid
Good will Dr
To Bank
(Being amt paid)

(e) Payment to creditor/Debenture taken over
Creditor Dr
Debenture holder Dr
To Bank
To New debenture
To Security Premium
(Being payment made to liabilities)
* In case of discount on issue of Debenture, it will be written off against P&L of new Company.

(f) Payment of formation Expenses
Preliminary Expense
To Bank
(Being Preliminary Exp Paid)
* These will be written off in P&L A/c

(g) for creation of Statutory Reserve

Amalgamation Adjustment Dr *
To Export Profit Reserve
To Investment allowance Reserve
To Foreign project Reserve
To Shipping Reserve **

* Show in Balancesheet as negative item "Amalgamation Adjustment"

** These reserves are created under tax laws

Note: Above Entry is reversed, when period of such reserve, is expired

(h) Contra Elimination

Payable (Creditor/BP/Loan) Dr
To Receivable (Debtor/BR/Loan)
(Being contra cancelled)

(i) Elimination of unrealised Profit on stock

Upstream
Goodwill/Capital Reserve Dr
To Stock
(Being stock Reserve created)

Downstream
P/L A/c
To Stock
(Being Stock Reserve created)

Note: Finally in Balancesheet, Either Goodwill or Capital Reserve should appear

Note: format should be as per S-III.

③ Calculation of Purchase Consideration (P.C)

(i) P.C. will be either given in question or calculated.

(ii) Calculation of P.C can be by
- Net Payments method NPM (1st Pref)
- Net Assets method or Residual method NAM

* Apply NPM if complete payment details for Payment to Equity shareholder and pref shareholder is given in question. In other cases use Net Assets method

(iii) Calculation of PC under Net Payment method

Payment To	Payment In	Working	Amount
ESH	Eq share/Pshare/Cash etc	xxx	xxx
PSH	" " "	xxx	xxx
			xxx

As per AS-14, Payment made by New Company to Equity + Pref shareholder is called Consideration. Hence any other payment made by new company will Not be included in P.C

(iv) Calculation of PC under Net Assets method

	Sundry Assets takenover at agreed values	xxx
+	Goodwill " " " " "	xxx
-	Sundry Liabilities " " " " " (including debentures at agreed values)	xxx
	P.C	xxx

Payment In	Pref share	xxx
" "	Equity Share	xxx
" "	Cash	xxx
" "	other forms	xxx
	PC	xxx

Match

Note: for calculation of number of shares to be issued, question may provide Swap Ratio or Exchange Ratio. In such cases no of shares are calculated using Swap Ratio.

Alternatively, if Question provide Market Value or fair value of BOTH Companies Equity Shares, then

$$\text{No of Share to be issued} = \frac{\text{Value of old Co share} \times \text{No of old Co. share}}{\text{Value of new Company share}}$$

Also, if question requires Calculation of Intrinsic Value (kind of fair value) for companies, then

$$\text{Intrinsic value} = \frac{\text{Fair value of Assets} - \text{Fair value of Liab.} - \text{Fair value of PSH}}{\text{No of Eq. shares of Company}}$$

* Here fair values are Agreed values if given, else use Book values.

* Intrinsic Value also called Break up value or Net worth per share or Net Asset Value is not calculated for Pref shareholder.

Example: A Ltd taken over B Ltd (having 200000 ES share of ₹10 each)

Case A: A Ltd will issue 3 Equity shares of ₹10 each @ 12 each against 4 Equity Shares of B Ltd

Case B: A Ltd will issue necessary Equity Shares to Equity Shareholder of B Ltd based on Value of shares. Value A Ltd Share ₹12, B Ltd ₹20

Case C: A Ltd will issue necessary Equity Shares to ESHolders of B Ltd

Case D: A Ltd will issue 3 Equity Shares for 4 Equity Shares held. Value of Share of A Ltd is 12/=. Also A Ltd will pay Cash in accordance with Intrinsic Value of Shares

Case E: A Ltd will issue necessary shares to Shareholder of B Ltd based on Intrinsic value of Shares

Step1 : Check Swap Ratio is given → Use Payment Method

↓

No

Step2 Share value (not Par value / Paid value)
↳ Like market value / fair value
of Eshares of Both Companies
is given → Use Payment method

↓

No

Step3 Do Question requires Calculation of
Intrinsic Value of Both Company's → Use Payment method

↓

No

↓

Use NAM

(5) Treatment of Debentures

Debenture holders are recorded in P.C in N.A.M @ Agreed value. These are later recorded by new company in its Books @ agreed values but journalized using premium/Par/Discount values, as given in Question

Generally we tabulate it in Rough

Agreed value Method-I			Agreed value Method-II	
OLD Book value	× Redemption Terms	=	New Book value	× New Issue Terms
Always available in Q	will be given or assume Par value 1st Assumption		generally missing value	will be given or assume Par 2nd Assumption

Examples : Assume in all cases Book value of Debentures of old Co ₹5lakh

Case A : Debentures are takenover by new Company

Case B : Debentures are takenover by new Company at 10% Premium to be settled by issue of new Debentures at 5% premium.

Case C : new Company will issue debentures at 5% discount to pay old Company debentures at 20% Premium

Case D : new Company took over Debentures of old Company and agreed to pay by issue of 5100 debentures at 5% premium

⑥ Concept of Statutory Reserve

(i) Journal Entry for creation of Statutory Reserve

Amalgamation Adjustment A/c Dr
To Statutory Reserve
(Being Statutory Reserve created)

- Amalgamation Adjustment is shown as negative Reserve in Reserve + Surplus of new Company
- Statutory Reserve is shown in Balance sheet as positive Reserve + Surplus
- List of Statutory Reserve is given below
  - Investment Allowance Reserve
  - Export Profit Reserve
  - Foreign Project Reserve
  - Shipping Reserve
  - Mining Reserve etc

(ii) Journal Entry for cancellation of Statutory Reserve

Statutory Reserve A/c Dr
To Amalgamation Adjustment
(Being Statutory Reserve cancelled)

* If Question says time period for statutory Reserve is pending, Journalise for creation and upon time period Ending, Cancel statutory Reserve.

⑦ Concept of unrealised profit on stock

(i) Identify stock 'in hand' from sister Company Purchases (A) xx
Rate of profit on sale earned by seller company (B) xx

unrealised profit = A × B xxx
(-) change in value of stock due to different Agreed value xxx
unrealised profit to be Adjusted in Journal xxx

Entries already given earlier.

(8) Best Assumptions

To Pay Equity shareholders → Discharge in Equity shares of new Company
" " Pref " → " " Pref Shares " " "
" " Debenture holders → " " Debenture " " "
(same rate)

If Question does not provide
- Information about No of shares and value of share, assume shares are issued at Par
- Information about No of shares and value of share, but share are issued at premium, whose premium is also missing, assume same number of shares, that are in old Co, to be issued by new Company.

(9) Nature of Reserves

Reserve & surplus

Free Reserves
(means dividend can be Paid out of them)
↓
P/L, G/R, Retained Earnings
Surplus A/c, Balance in Appropriation A/c
Dividend Equalisation Reserve, Revenue Reserve

Non free Reserves
(Means not available for distribution and dividend)

Limits placed by Company law or AS or Guidance Note of ICAI or Company (self) or other laws (except Income Tax)
↓
Revaluation Reserve (AS-10)
Security Premium (Section 52)
Workmen Compensation fund (Factory act)
Investment Fluctuation fund (Banking)
Contingency Reserve (Electricity Comp. Act)
CRR (section 55 + 69)
DRR (Section 72)
Capital Reserve (S-III)
Profit Prior to Incorporation S-III
ESOP Reserve (Guidance Note)

Called Specific Reserve can have time limit.

Limits placed by Income Tax
↓
Invt Allowance Reserve
Export Profit Reserve
Foreign Project Reserve
Shipping Reserve
Mining Reserve
Tea & Coffee Reserve

Called specific Reserve. Have time limit

Note: Following are not Reserves, but Liabilities
- Employee Provident fund
- Provision
- Retirement Gratuity fund
- Workmen Profit Sharing fund
- Contingent Liability
- Workmen compensation fund to the extent mentioned as Liability.

⑩ Books of old Company

Step 1 Transfer all Items of Balance Sheet at Book value to various Accounts
- Equity Share Capital to Equity shareholders
- All Reserve / Surplus, Losses (Free, Non free) to Eq shareholders
- Pref share capital to Pref shareholder A/c
- Cash if not takenover by new Company to Cash A/c
- other items to Realisation A/c

Step 2 Sell Assets and Liabilities as specified in Question

(A) for assets and Liab not takenover → Cash A/c Dr
To Realisation
(Being asset sold)
or
Realisation Dr
To Cash
(Being Liab Paid)

* Liability settled against any asset No Entry
* If Q is silent on realisation of asset (which has not been takenover) assume No Realisation.
- If Q is silent on payment of Liability (which has not been takenover) assume Payment at Book value

(B) Takeover of Assets + Liab by new Company
New Company Dr P.C
To Realisation P.C
(Being Sundry Assets & Liab takenover by new co.)

Step 3 Payment of Realisation Expense (Old Company)
Realisation Dr
To Cash
(Being amt Paid)

Step4 check Book value of PSH + settlement value in PC for PSH
If both are not equal, record gain/loss on realisation

Excess Payment to PSH = Realisation
To PSH
(Being excess Amt Recorded)

Short Payment to PSH PSH
To Realisation
(Being short Amt recorded)

Step5 If new Company makes payment to old Company for Expenses or old Company which not takenover are being paid by new company in cash then record Receipt of cash

Cash A/c Dr
To Realisation
(Being amt Received)

* Payment Entries already made above.
* A shortcut Exist if neither Receiving nor payment made in above Case.

Step6 Close Accounts.
(i) Realise PC from New Company
(ii) Distribute it to ESH + PSH
(iii) Close Realisation & its Profit/loss is T/F to ESH
(iv) Any difference in Cash A/c is T/F to ESH A/c
(v) ESH/PSH will tally.

(11) updation of financial Statements-

If Balance Sheet given in question and date of Amalgamation/Absorption are not Same, then Balance Sheet Should be updated.

- If Question provides Net Profit for Gap Period, then missing fig is Cash
- " " does not provide Net Profit for Gap Period, then missing fig is net Profit

(12) Merger/pooling of Interest Method

Under Merger, Accounting is done as if Entities have combined (not purchased or sold). These merger schemes are approved in court and are subject to following conditions

(i) All Assets and All Liabilities of transferor (old) Company should be transferred to transferee (new) Company

(ii) Such transfer should be @ Book value only (No change allowed)

(iii) Same Business should be carried on by transferee Company which was being done by old company

(iv) Equity Shareholders holding at least 90% of Equity share capital should agree to become Equity shareholder of transferee company

(v) Such agreed shareholder should be paid in Equity Shares only.

Note: To check Merger in Question

- Question specifies Purchase or Merger. follow Question
- Question does not specifies anything. but
  - All Assets / Liab takenover ?
  - Takenover at Book Values ?
  - P.C Paid to Equity shareholders in Eshare only ?

  If all answers are Yes, it is merger.

(13) Journal Entries in Merger (New Company)

(i) Business Merger A/c Dr — Consideration
To Liquidator of Old Company — "
(Being Business merged)

(ii) Sundry Assets Dr — Book value
To Sundry Liab — Book value
To Reserve & Surplus of old co — @ Book value
To Business Merger
(Being S.Assets / Liab combined)

* Any difference is either General Reserve or P&L A/c.

* Do not take Debit Reserve/Surplus in above Entry.

(iii) Liquidator A/c Dr
To E Share Capital
To P Share Capital
To Security Premium
(Being P.C Paid)

(iv) P&L/G.R A/c Dr
To Cash
(Being expense Paid)

(v) P&L/G.R A/c Dr — (upstream or Downstream)
To Stock
(Being U.P Eliminated)

(vi) No Entry for Statutory Reserves

(vii) Entries for contra, Preliminary Expense Paid, underwriting Commission paid, New public Issue are all Same.

(14) Difference between Purchase and Merger

Purchase	Merger
• Selected Asset/Liab can be taken over	All assets and Liab are taken over
• Taken over at new values or Book value	Taken over at Book values only
• Difference b/w PC and Net Asset taken over is Goodwill/CR	Difference is called G/R or P/L
• Reserve and surplus not taken over by new Company	These are taken over by new Co.
• Expenses Paid by new Company for old Company are adjusted to Goodwill	Expense are adjusted in P/L or G/R

Internal Reconstruction

① Internal Reconstruction means altering rights of shareholders and/or creditors in such way that organisation increases its period of going concern. This reconstruction can be by following methods

a) Share Subdivision or Share Consolidation
b) Changes in Shareholders Rights
c) Capital Reduction Scheme
d) Share Surrender Scheme

② Companies are restructured internally under
a) Resolution Plan (RP) of IB Code or
b) Under Scheme made for Adjustment of Shareholders Rights

③ Steps involved in IBC

Application to NCLT for Insolvency

Appointment of Insolvency Resolution Professional (IRP)

IRP collects information about claims from creditors and Constitute Committee of Creditors COC

COC appoints Resolution Professional. He can be same as IRP

RP formulates Resolution plan based on admitted claims

Resolution plan is approved by COC

Resolution Plan is approved by NCLT, Govt. authorities + Shareholders

Execution of Resolution Plan ⇒ Do Accounting for it.

If at any stage Resolution plan cannot be approved, company goes into Liquidation

Journal Entries

(4) For subdivision and consolidation of shares

Pref /Equity share Capital (₹ old face value) Dr Paid up capital
To Pref /Equity Share Capital (₹ new face value) Paid up Share Cap
(Being share capital subdivided or consolidated from ...... shares of ₹ old F.V to ₹ Paid up value ...... shares of ₹ New F.V paid up)

(5) For converting share capital to stock capital

Equity share capital (₹ old face value) Dr Paid up Capital
To Equity STOCK Capital Paid up Capital
(Being share capital converted into stock capital)

* In Balance Sheet, don't write Authorised share capital or Issued & Paid up share capital. Instead write Authorised capital and Issued/Paid up capital

* If authorised capital is increased/Decreased, we do not journalise any entry. It is based on Board Resolution and hence just disclosed. It is not any transaction

Reconversion

Equity Stock Capital A/c Dr Paid up capital
To Equity SHARE Capital (₹ New FV) Paid up Capital
(Being stock capital converted to share capital)

(6) For Scheme of Reduction of capital

(i) Eq/Pref share capital (old F.V) Dr Paid up capital
To Eq/Pref share capital (New FV) New Paid up Capital
To Capital Reduction/Reconstruction A/c/Capital Reconstruction A/c/Internal Recons A/c (B.F)
(Being capital Reduced)

* Capital Reduction (by whatever name called) is a special Account and it must be closed at End. For this purpose, we generally prepare Capital Reduction A/c.

(ii) for change in value of assets and liabilities

Asset A/c Dr / Liability A/c Dr — change in value
To Capital Reduction
(Being asset/liab. changed)

* Above Entry may be reversed based on change in values

(iii) for Sale/settlement of Asset/Liability (recorded in books)

Bank A/c Dr	Liability A/c Dr
To Asset	To Bank/Share capital
To Capital Reduction b.f	To Capital Reduction
(Being asset sold)	(Being liabilities paid)

(iv) for settlement of Contingent liabilities

Contingent liability does not have any credit Balance. It just a footnote. Examples are
- Pref. Dividend in Arrears
- Bills discounted not yet matured
- Capital commitments
- legal disputes

If Contingent liabilities is waived/cancelled ⇒ No Entry

If Contingent liability is Paid or unrecorded liability is paid or Expenses of Reconstruction are paid or penalty calculated and paid on contract

Capital Reduction
To Bank
(Being amt paid)

(v) for fresh issue of shares/Debentures

Bank A/c Dr
To Share Capital
To Debentures
(Being share/Debentures issued)

* Entries can be formalised through Application A/c

(VI) for writing off losses

Capital Reduction A/c Dr
  To P/L
  To Sundry Assets
  To losses appearing in Balance Sheet like Preliminary Expenses
(Being Sundry Assets and losses written off)

* Sometimes opening Balance sheet is missing due to which P/L Balance is also missing, in such cases, prepare opening Balance sheet to calculate losses at start

(VII) Balance in Capital Reduction A/c

If credit Balance
↓
T/f it to Capital Reserve
↓
Capital Reduction Dr
  To Capital Reserve
(Being amt t/f)

If debit Balance
↓
use existing Reserves, G/R, P/L, security Premium to eliminate debit Balance
↓
G/R Dr
P/L Dr
Security Premium Dr
  To Capital Reduction
(Being amt t/f)

Note: Always make Balance sheet in S-III format after above entries. Also report issue of share Capital for non cash Consideration. Name of Company Should include "And Reduced" after its name

Note: If a creditor has multiple debts, then all debt should be transferred to personal Account before settlement

Note: Claim of creditor means Amt due to creditor including Interest

⑦ Journal Entries in case of Share Surrender Scheme

(i) For Share Surrender by shareholder

Eq share Capital/Pref Share Capital Dr — Paid up capital
To Eq Share Cap (₹FV)/PS Capital (₹FV) — New Paid up capital
To Share Surrender A/c
(Being share capital exchanged)

* Sometimes Shares are not exchanged but only surrendered, then journal would be

Share Capital Dr
To Share Surrender
(Being capital surrendered)

(II) When share surrendered are converted to any specific class, then

Share Surrender A/c Dr
To EShare/PShare Surrender A/c
(Being share surrender converted)

(III) When share surrender are settled with liability

Eq Share Surrender/PShare Surrender A/c Dr
To Eq/Pref Share Capital
(Being surrendered share transferred)

AND

Liability A/c Dr
To Capital Reduction
Being liability cancelled due to share surrender

* If liability is cancelled without share surrender, it will be journalised as usual

Liability A/c Dr
To Capital Reduction
(Being amount W/F)

(iv) Share Surrendered, not utilised will be now cancelled

Eq share Surrender / Pref Share Surrender Dr
To Capital Reduction
(Being Share Surrendered cancelled)

* Any Balance in Share Surrender must be cancelled by above Entry

* All other Entries remain same

(8) Amalgamation / Absorption with Internal Reconstruction

If question specifies that company is being restructured internally
and
also Amalgamation / Absorption occurs
then

Step 1 Apply Concept of Internal Reconstruction followed by

Step 2 Apply Amalgamation Accounting of AS-14

Branch Accounting

① Following Topics are covered

(i) Dependent Branch
(ii) Independent Branch - Domestic
(iii) " " - Foreign
(iv) Books of Head office

② Branches are extension of business. All Branches are controlled by Head office (H.O). Branches can be

(a) Dependent which are small Branches. These do not maintain own Books of Accounts. These prepare returns and tables, which are given to H.O for Accounting purposes.
All Accounting is done by Head office for Branch. Hence called Dependent Branch.

(b) Branch that maintains full books of Accounts are called Independent Branch. These can be Domestic or foreign

Example

Name of Branch	Maintains Books	Type
SBI Branch Delhi	Yes	
SBI " New York	Yes	
KFC " Amritsar	No	

③ Dependent Branches
In this case, H.O will maintain necessary entries, so as to calculate profit or loss of Branch. Such Entries can be journalized using any method

(I) Debtors method
(II) Stock and debtor method

Profit/loss can be calculated using final Accounts Method

(4) Debtors method

following Accounts are prepared

Branch Account

To opening Balance			By opening Balance		
Debtor	xxx		Creditors	xxx	
Stock @ S.P	xxx		Outstanding Balance	xxx	xxx
Cash/Petty Cash	xxx		By opening Stock Reserve		xxx
Fixed Assets	xxx		By Goods sent to Branch - Returns		xxx
Prepaid Expenses	xxx	xxx	By Remittances - Cash sent to H.O		xxx
To Goods sent to Branch at S.P		xxx	By Goods sent to Branch - Loading		xxx
To Bank - Cash sent to Branch		xxx	By Cl. Balances		
To Goods sent to Branch - load Returns		xxx	Debtors	xxx	
To closing Balance			Stock @ Selling Price	xxx	
Creditors	xxx		Cash/Petty Cash	xxx	
Outstanding Exp	xxx	xxx	Fixed Assets	xxx	
To Stock Reserve - closing		xxx	Prepaid Expenses	xxx	xxx
To Profit B.F		xxx	By Loss (B.F)		xxx
		xxx			xxx

Goods Sent to Branch A/c

To Branch - Goods Returns	xxx	By Branch - Goods sent	xxx
To Branch - load on goods sent	xxx	By Branch - load on Returns	xxx
To Purchases/Trading	xxx		

Stock Reserve A/c

To Branch – op stock Reserve	xxx	By Balance b/d	xxx
To Balance c/d	xxx	By Branch closing stock Reserve	xxx

Following memorandum Accounts can be prepared if needed. Branch Debtors Account is always prepared

Branch Debtor A/c

To Balance b/d	xxx	By Discount/Allowance	xxx
To credit sale (net of Return)	xxx	By Bad debts	xxx
		By collection from Debtors	xxx
		By Balance c/d	xxx

Branch Stock @ selling Price

To Balance b/d	xxx	By Goods sent to Branch - Return	xxx
To Goods sent to Branch	xxx	By Sale at S.P	xxx
To Surplus (B.F)	xxx	By Shortage	xxx
		By Abnormal + normal loss	xxx
		By Balance c/d	xxx
	xxx		xxx

Branch Cash A/c

To Balance b/d	xxx	By Petty Expenses	xxx
To Cash from H.O	xxx	By Balance c/d	xxx

Note: Always assume, if silent, that
- Sale is credit sale
- Return of sale is credit sale Return
- Branch Remits all collections immediately after paying Expense & liabilities
- Discount Allowed is cash discount
- All expenses of Branch are paid by H.O.

Note: Treatment of Abnormal & normal loss

In Branch A/c – No Treatment

In Stock A/c – Both will be credited to calculate correct closing stock.

Example : following are few transactions for April 20X1
- H.O sent goods to Branch ₹10 lakh
- " " cash " " ₹ 2 lakh
- Branch sold goods on cash ₹ 50000
- " " " " credit ₹ 60000
- collection from debtors by Branch ₹ 35000
- Branch paid Expenses ₹ 18000
- Baddebts of Branch ₹ 30000
- Discount allowed to debtors ₹ 20000

At month End, closing stock of Branch is ₹ 80000 . Journalise for H.O + Branch

Example : following are transactions of H.O and Branch
- HO sent goods ₹ 20,00,000 to Branch
- " " cash ₹ 1 lakh " "
- Branch sale (cash) ₹ 7 lakh
- " " credit ₹ 15 lakh
- Branch paid Expense ₹ 70000
- Branch Remittances to H.O ₹ 120000
- Branch Baddebts ₹ 50000
- Branch collection from debtors ₹ 60000

closing stock at Branch ₹ 30000.
Journalise for H.O and Branch.
Prepare final A/c of Branch
Consolidate Branch with H.O
Consolidate Branch with H.O assuming Branch does not maintain Books of A/c

Note: Trade Discount is not Journalised. It reduces Sale Price whereas Cash Discount is Journalised as Expense.

Note: Default Assumptions are that
Goods sent to Branch are @ IP
Sale is @ Selling Price
Purchase is @ Cost
Goods Returned by Debtors are @ ....
Stock at Branch @ ....
Stock at H.O @ ....

Note: Always remember that H.O and Branch are treated as separate persons for Accounting purposes. Later these are consolidated for presentation to Shareholders.

Note: $\frac{1}{3}$ of Cost = $\frac{1}{4}$ Sale

$\frac{1}{5}$ Sale = $\frac{1}{4}$ of Cost

(5) Final Accounts method

Under this method, following Accounts are prepared

Trading A/c

Profit & loss Account

Trading A/c

To opening stock @ cost	xxx	By sale	xxx
To goods sent to branch at cost price	xxx	By Abnormal loss (cost price)	xxx
To G.P	xxx	By cl. stock @ cost	xxx

Profit & loss A/c

To Expenses	xxx	By G.P	
To Abnormal loss	xxx		
To Net profit	xxx		
	xxx		xxx

Note: Treatment of Normal loss - No Treatment

" " " Abnormal loss → Shown above

But if we prepare stock A/c then both normal & Abnormal loss are credited to it.

Note: Sometimes Branch sells goods to other Branches at Invoice Price then, final A/c are prepared at branch level will be at I.P. Any closing stock of goods at IP will be made at C.P. For this purpose stock Reserve should be adjusted in Branch P&L.

Branch P&L A/c

To closing stock Reserve (on stock held by other Branches which was invoiced by this Branch)	xxx	By G.P	xxx
To Expenses	xxx	By op. stock Reserve (on stock held by other Branches which was invoiced by this Branch)	xxx
To N.P			

⑥ Stock and Debtor method

Under this method, following accounts are prepared

Branch Stock at I.P A/c

To op. stock	xxx	By goods returned to H.O	xxx
To goods sent to Branch	xxx	By Sale net of Return	xxx
To Surplus on sale B.F	xxx	By Abnormal loss	xxx
		By normal loss	xxx
		By closing stock	xxx
	___		___

Branch Debtor A/c

To Balance b/d	xxx	By Discount/Allowance	xxx
To credit sale (net of Return)	xxx	By Bad debts	xxx
		By collection from debtor	xxx
		By Balance c/d	xxx
	___		___

Branch Adjustment A/c

To goods Returned to H.O - load	xxx	By op. stock Reserve	xxx
To Abnormal loss - load	xxx	By goods sent to Branch - load	xxx
To Normal loss - full	xxx	By surplus from Branch stock	xxx
To closing stock - load	xxx		
To G.P	xxx		
	___		xxx

Branch Profit & loss A/c

To Abnormal loss - cost	xxx	By G.P	xxx
To Expenses	xxx		
To net Profit	xxx		
	___		___

Example: H.O sent goods to Branch at Cost + 25%.

Opening Stock at I.P	50000
goods sent to Branch	150000
Sale net of Return	140000
Abnormal Loss	70000
Normal loss	5000
Expenses	20000

All sales were in Cash and Branch does not have other asset/liab

Prepare Trading/P&L A/c. Assume Branch Remits cash after paying its expenses.

Note: If Q is silent about method, use either Debtor method or Stock and debtor method. Do not apply final A/c method.

If Stock and Debtor method is applied, it gives all missing fig. for other methods.

Note. If Question does not having loading, i.e. goods are invoiced at Cost only then Branch Adjustment A/c will have only following items

Branch Adj A/c

To G.P	xxx	By Surplus (from Branch Stock A/c)	xxx
	—		—

⑦ Dual Profit Situations

Sometimes Branch is neither fully dependent, nor fully Independent. Generally this happens when H.O provides more independence in terms of day to day actions and H.O controls limited items.

Example can be Wholesale Trade by H.O and Branch are Retail outlets. Here H.O invoices goods at Wholesale Price and Branch sells them at Above wholesale Price. Hence dual profit/Pricing Situation arises.

Another example can be Branches allowed to purchase and sell goods without involving H.O

Accounting Treatment

In such cases, Branch will prepare its own draft/Memorandum Accounts to calculate profit/loss. Such Accounts can be prepared by using either Stock and Debtor method or final A/c method. These are prepared from Branch point of view.

H.O will Consolidate profit specified by Branch. It will have to adjust

Stock Reserve in its P/L A/c as follows.

H.O P/L A/c

To closing stock Reserve (Stock held by Branch on which H.O has invoiced)	xxx	By G.P of H.O	xxx
To Expenses	xxx	By Profit of Branch	xxx
To Profit	xxx	By op. stock Reserve (Stock held by Branch on which H.O had invoiced)	xxx

Similarly if Branch A sells goods to Branch B on independent Basis Branch A P/L will be as follows.

Branch P/L A/c

To closing stock Reserve (on stock held by other Branches which was invoiced by this Branch)	xxx	By G.P	xxx
To Expenses	xxx	By op. stock Reserve (on stock held by other Branches which was invoiced by this Branch)	xxx
To N.P			

(8) Journal Entries - Basic Entries for Independent Branch

	Books of H'O	Books of Branch
(i) Goods sent by H'O to Branch		
	Branch Dr	Goods sent by H'O Dr
	To goods sent	To H'O
	(Being goods sent)	(Being goods sent)
(ii) Goods Returned by Branch to H'O		
	Goods sent Dr	H'O Dr
	To Branch	To Goods sent
	(Being goods Returned)	(Being goods returned)
(iii) Cash sent to Branch		
	Branch Dr	Cash Dr
	To Cash	To H'O
	(Being amt sent)	(Being amt Received)
(iv) Debtor of Branch paid to H'O directly		
	Cash A/c Dr	H'O
	To Branch	To Debtors
	(Being amt Received)	(Being amt Received by H'O)
(v) Asset of H'O, used by Branch to be depreciated		
	Branch	Depreciation
	To Asset	To H'O
	(Being asset depreciated)	(Being depreciated)
(vi) H'O Rent Paid by Branch		
	Rent	H'O
	To Branch	To Cash
	(Being Rent Paid)	(Being Rent Paid)

Hence

In the Books of H'O

Branch A/c Balance will Always be equal and opposite to Balance in H'O A/c in Books of Branch.

(9) Domestic/Local Independent Branches - Reconciliation

Reconciliation Entries

	Books of H.O	Books of Branch
(a) Goods sent to Branch but not received by it	No Entry	Goods in Transit Dr To H.O (Being goods in transit recorded) * Correct Entry should be Goods sent by H.O Dr To H.O (Being goods sent) * GIT should be included in Cl. stock of Branch.
(b) Cash sent by Branch, not received by H.O	Cash in transit Dr To Branch (Being cash in transit recorded)	- No Entry -
(c) Abnormal loss in transit to be recorded by H.O	Loss in transit Dr To Branch (Being loss recorded)	- No Entry -
(d) Abnormal loss in transit to be recorded by Branch	- No Entry -	Loss in transit Dr To H.O (Being loss recorded)
(e) Expense allocated by H.O to Branch, not recorded by Branch	No Entry	Expenses Dr To H.O (Being expense recorded)
(f) Income allocated by H.O to Branch, not recorded by Branch	No Entry	H.O Dr To Income (Being Income Recorded)

(g) Branch purchased Assets whose Account is to be maintained by H.O

Branch	H.O
Fixed Asset Dr	H.O
To Branch	To Branch
(Being asset recorded)	(Being Asset Recorded)

* If payment is made by H.O Entry would be

Asset Dr	- No Entry -
To Bank	
(Being asset purchased)	

* Depreciation on such asset

Branch Dr	Depreciation
To Asset	To H.O
(Being Dep charged)	(Being Dep charged)

Note: Apart from above, Entries may be required for normal Accounting at H.O or Branch.

Note: If Branch deals with other Branches, it is assumed that transactions are with H.O instead of other Branches. H.O will journalise following

Receiving Branch Dr
To giving Branch
(Being Inter Branch transaction recorded)

For above Entry, H.O will Combine all Inter Branch Transactions and then pass single Jornal Entry.

Example Following information is available. H.O invoices goods to Branch at selling price less 20%. Branch sells goods at Cost to H.O + 80%.

	H.O	Branch
Opening Stock	10,00,000	200000
Purchase	500000	-
Goods sent to Branch	120000	
Sale	40,00,000	10,00,000
Abnormal loss	5000	30000
Normal loss	10000	6000
Sundry Expense	30000	10000

H.O sale to customers at selling Price which is equal to Branch Sale Price

Prepare H.O Trading Ac and Branch final Ac

(10) Consolidation of Branch and H.O

Step1 : Apply Reconciliation Entries

Step2 : Prepare H.O and Branch final Accounts based on Trial Balance provided
* such Trial Balance should be after all Reconciliation Entries passed in Step1 above
* If closing stock is missing, it should be calculated by preparing Branch Stock A/c @ I.P or H.O Stock @ Cost
* If Question provides any adjustment, it should be adjusted in final A/c.

Step3 Incorporation Entries/Consolidation Entries

Books of H.O	Books of Branch
(i) For incorporation of Profit/loss	
Branch A/c Dr	P/L A/c Dr
To P/L	To H.O
(Being profit incorporated)	(Being profit T/F)

* Instead of above Entry, following Entries can be made by H.O

Branch Dr
To Branch Trading A/c
(Being credit items incorporated)

Branch Trading A/c Dr
To Branch
(Being debit items incorporated)

Branch A/c Dr
To Branch P/L
(Being other Income of Branch incorporated)

Branch P/L A/c Dr
To Branch
(Being Expenses incorporated)

(ii) for incorporation of Asset/Liab.

Assets Dr
To Liab
To Branch
(Being asset/liab incorporated)

H.O Dr
Liab Dr
To Assets
(Being asset/liab T/F)

(iii) for Stock Reserve

P&L A/c Dr
To Stock Reserve) Provision for Unrealised profit
Being Stock Reserve created on closing Stock

* opening Stock Reserve will be cancelled by T/F to P&L by H.O

Example : following are transaction of Branch

(i) Goods sent to Branch ₹ 100000 IP ₹ 120000
(ii) Branch sold goods for ₹ 85000. Sale was at 20% above I.P
(iii) Debtor Paid ₹ 70000, Discount ₹ 1000
(iv) Expences of Branch paid by H.O ₹ 12000
(v) Branch remitted to H.O ₹ 60000

- Calculate profit of Branch by Debtor Method, Stock & Debtor Method and final A/c
- Prepare in books of H.O Branch A/c assuming Branch calculate it profit (own level) Also prepare final A/c of Branch
- Prepare final A/c of Branch assuming Branch is independent. For this purpose make Trial Balance of Branch and Branch A/c. Also incorporate Balance sheet of Branch.

(11) foreign Independent Branch

Step1: Convert Trial Balance of Branch to local currency.

* Apply Rules of AS-11 (IFO or NIFO)

* If Question requires adjustment to be made in Trial Balance itself then make adjustments in Trial Balance before conversion

* If Stock is missing, then prepare Branch Stock @ I.P in foreign currency and later convert it

* Trial Balance Should be after rectification and reconciliation if any.

Step2: Prepare H.O and Branch final Acc.

If Stock of H.O is missing, calculate it at Cost to H.O

Step3 Prepare Consolidated final & Formalize Incorporation Entries.

Note: Manager Commission will be paid in foreign currency, since he is Branch manager, managing in foreign currency. for this purpose, we may need to prepare Branch trading P/L in foreign currency.

(12) Foreign Branch or foreign H.O

Whenever H.O and Branch are in different Countries, i.e they have different currencies, then following points are relevant.

Step 1 Convert Branch currency to H.O currency.
If H.O is in India (₹), Branch is in USA ($), then Branch Trial Balance in ($) will be converted to (₹).
For this purpose conversion Rules given in AS-11 will be applied.

Note: Conversion Rules of AS-11

Generally Branch is considered as Integral foreign operation (IFO), but if question specifies, Branch can be Non Integral foreign operation (NIFO). [Best Assumption is IFO]

Items	Conversion Rule IFO	Conversion Rule NIFO
(i) Fixed Assets, Investments Depreciation	Rate on Date of Transaction	closing Rate
(ii) Current Assets, Current liab and other Long term Liab.	closing Rate	Closing Rate
(iii) Inter related Accounts like H.O A/c, Goods sent to Branch A/c, Remittance Account etc	Actual Balance in H.O Books	Actual Balance in H.O Books
(iv) opening stock	opening Rate	op. Rate
(v) All other Incomes and Expenses [Depreciation covered in (i) Point]	Average Rate	Average Rate

Note: Any difference in Trial Balance is considered as

IFO ⇒ Exchange Difference, Treated as Income/Expense in P/L A/c

NIFO ⇒ Translation Reserve, Treated as Reserve/Surplus in Balance sheet.

Note: Before Converting Trial Balance, Adjustments will be incorporated in Trial Balance. if Question has mentioned. Otherwise Adjustments will be done later in final A/c.

Note: If closing stock is missing, calculate stock of Branch in its OWN currency. Such stock will be converted using Closing Rate.

Step 2 Reconciliations are not required here. since currency is different.

Step 3 Prepare final A/c of H.O and Branch.

Step 4 Incorporate Branch in H.O