CA INTER

ADVANCED ACCOUNTING

MOST DO QUESTIONS

(For Practice Before Exams)

FOR SEP'24 AND JAN' 25 ATTEMPT

Total No. of Questions - 183

Compiled by CA. Jai Chawla

Scanned with OKEN Scanner

INDEX

Sr. No.	Chapter Name	Page No.	Question of No.
1.	AS 19 – LEASES	1	5
2.	AS 20 – “EARNINGS PER SHARE”	5	6
3.	AS 11 - “EFFECTS OF CHANGES IN FOREIGN EXCHANGE RATES”	9	7
4.	BRANCH	16	12
5.	FINANCIAL STATEMENTS	33	5
6.	BUYBACK OF SECURITIES	50	4
7.	CASH FLOW STATEMENT	60	6
8.	ACCOUNTING FOR RECONSTRUCTION OF COMPANIES	72	6
9.	AMALGAMATION OF COMPANIES	87	10
10.	AS 15 – EMPLOYEE BENEFITS	115	5
11.	AS 16 - BORROWING COSTS	119	7
12.	AS 10 - PPE	125	6
13.	CONSOLIDATION	130	10
14.	AS 23 – INVESTMENT IN ASSOCIATES	147	8
15.	AS – 27 JOINT VENTURES	152	5
16.	AS 2 - INVENTORIES	158	5
17.	AS 13 - INVESTMENTS	162	4
18.	AS 26 - “INTANGIBLE ASSETS”	170	4
19.	AS 28 – IMPAIRMENT OF ASSETS	173	5
20.	AS - 22 “ACCOUNTING FOR TAXES ON INCOME”	177	4
21.	FRAMEWORK	181	4
22.	AS 1 – DISCLOURE OF ACCOUNTING POLICIES	184	3
23.	AS – 7 “CONSTRUCTION CONTRACTS”	187	5
24.	AS – 9 “REVENUE RECOGNITION”	191	4
25.	AS 12 - ACCOUNTING FOR GOVERNMENT GRANTS	194	6
26.	AS 17 – “SEGMENT REPORTING”	198	3
27.	AS 25 - INTERIM FINANCIAL REPORTING	201	3

Scanned with OKEN Scanner

28.	AS 4 - CONTINGENCIES & EVENTS OCCURRING AFTER THE BALANCE SHEET DATE	204	7
29.	AS 5 - "NET PROFIT OR LOSS FOR THE PERIOD, PRIOR PERIOD ITEMS & CHANGE IN ACCOUNTING POLICIES"	208	7
30.	AS 18 - RELATED PARTY DISCLOSURES	212	9
31.	AS 24 - DISCONTINUING OPERATION	218	2
32.	AS 29 - "PROVISIONS, CONTINGENT LIABILITIES AND CONTINGENT ASSETS"	220	7

Scanned with OKEN Scanner

Scanned with OKEN Scanner

1. AS – 19 LEASES

QUESTION 01

ABC Ltd. took a machine on lease from XYZ Ltd., the fair value being Rs. 10,00,000. The economic life of the machine as well as the lease term is 4 years. At the end of each year, ABC Ltd. pays Rs. 3,50,000. The lessee has guaranteed a residual value of Rs. 40,000 on expiry of the lease to the lessor. However, XYZ Ltd. estimates that the residual value of the machinery will be Rs. 35,000 only. The implicit rate of return is 16% and PV factors at 16% for year 1, year 2, year 3 and year 4 are 0.8621, 0.7432, 0.6407 and 0.5523 respectively. You are required to calculate the value of machinery to be considered by ABC Ltd. and the finance charges for each year.

SOLUTION

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

Value of machinery

In the given case, fair value of the machinery is Rs. 10, 00,000 and the net present value of minimum lease payments is Rs. 10,01,497 (Refer working Note). As the present value of the machine is more than the fair value of the machine, the machine and the corresponding liability will be recorded at fair value of Rs. 10,00,000.

Calculation of finance charges for each year

Year	Finance charge (Rs)	Payment (Rs)	Reduction in outstanding liability (Rs)	Outstanding liability (Rs)
1st year beginning	-	-	-	10,00,000
End of 1st year	1,60,000	3,50,000	1,90,000	8,10,000
End of 2nd year	1,29,600	3,50,000	2,20,400	5,89,600
End of 3rd year	94,336	3,50,000	2,55,664	3,33,936
End of 4th year	56,064	3,90,000*	2,96,570	0

*Assuming Lessee is paying GRV also

Working Note:

Present value of minimum lease payments

Annual lease rental x PV factor Rs. 3,50,000 x (0.8621 + 0.7432 + 0.6407+ 0.5523)	Rs 9,79 ,405
Present value of guaranteed residual value Rs 40,000 x (0.5523)	Rs 22,092
	Rs 10,01,497

Alternate 2: -

If Lessee has not Paid GRV of 40,000. Then Assets need to be returned to Lessor. In such case, Asset to Derecognised at BV & Lease Liability having BV of 40,000 shall be derecognised. Difference shall be transferred to P&L.

QUESTION 02

Aksat International Limited has given a machinery on lease for 36 months, and its useful life is 60 months. Cost & fair market value of the machinery is Rs. 5,00,000. The amount will be paid in 3 equal annual installments and the lessee will return the machinery to lessor at termination of lease. The unguaranteed residual value at the end of 3 years is Rs. 50,000. IRR of investment is 10% and present value of annuity factor of Rs 1 due at the end of 3 years at 10% IRR is 2.4868 and present value of Rs. 1 due at the end of 3rd year at 10% IRR is 0.7513.

Scanned with OKEN Scanner

You are required to comment with reason whether the lease constitute finance lease or operating lease. If it is finance lease, calculate unearned finance income.

SOLUTION

Determination of Nature of Lease

Present value of unguaranteed residual value at the end of 3rd year

= Rs. 50,000 x 0.7513

= Rs. 37,565

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

= Rs 4,62,435

The percentage of present value of lease payments to fair value of the equipment is

(Rs. 4,62,435/ Rs 5,00,000) x 100 = 92.487%.

Since, lease payments substantially covers the major portion of the fair value; the lease constitutes a finance lease.

Calculation of Unearned Finance Income

Annual lease payment = Rs. 4,62,435/ 2.4868 =Rs. 1,85,956 (approx.)

Gross investment in the lease = Total minimum lease payments + unguaranteed residual value

= (Rs. 1,85,956 × 3) + Rs. 50,000

= Rs. 5,57,868 + Rs. 50,000 = Rs. 6,07,868

Unearned finance income = Gross investment - Present value of minimum lease payments and unguaranteed residual value

= Rs. 6,07,868 – Rs. 5,00,000 = Rs. 1,07,868

QUESTION 03

Sun Limited leased a machine to Moon Limited on the following terms:

	(Amount in Rs.)
Fair value at inception of lease	50,00,000
Lease Term	4 Years
Lease Rental per annum	16,00,000
Guaranteed residual value	3,00,000
Expected residual value	4,50,000
Implicit Interest rate	15%

Discounted rates for 1st year, 2nd year, 3rd year and 4th year are 0.8696, 0.7561, 0.6575 and 0.5718 respectively. Calculate the value of Lease Liability and ascertain Unearned Finance Income as per AS-19.

SOLUTION

According to AS 19 "Leases", the lessee should recognise the lease as an asset and a liability at an amount equal to the fair value of the leased asset at the inception of the finance lease. However, if the fair value of the leased asset exceeds the present value of the minimum lease payments from the standpoint of the lessee, the amount recorded as an asset and a liability should be the present value of the minimum lease payments from the standpoint of the lessee. In calculating the present value of the minimum lease payments, the discount rate is the interest rate implicit in the lease. Present value of minimum lease payments will be calculated as follows:

Year	Minimum Lease Payment Rs.	Internal rate of return (Discount rate @15%)	Present value Rs.
1	16,00,000	0.8696	13,91,360
2	16,00,000	0.7561	12,09,760
3	16,00,000	0.6575	10,52,000
4	19,00,000*	0.5718	10,86,420
Total	67,00,000		47,39,540

Scanned with OKEN Scanner

Present value of minimum lease payments i.e., Rs. 47,39,540 is less than fair value at the inception of lease i.e., Rs. 50,00,000, therefore, the value of lease is Rs. 47,39,540 and lease liability should be recognized in the books at Rs. 47,39,540 as per AS 19.

Calculation of Unearned Finance Income

As per AS 19 on Leases, unearned finance income is the difference between (a) the gross investment in the lease and (b) the present value of minimum lease payments under a finance lease from the standpoint of the lessor; and any unguaranteed residual value accruing to the lessor, at the interest rate implicit in the lease.

Where:

i. Gross investment in the lease is the aggregate of (i) minimum lease payments from the stand point of the lessor and (ii) any unguaranteed residual value accruing to the lessor.

Gross investment = Minimum lease payments + Unguaranteed residual value

= [Total lease rent + Guaranteed residual value (GRV)] + Unguaranteed residual value (URV)

= [(Rs. 16,00,000 x 4 years) + Rs. 3,00,000] + Rs. 1,50,000 = Rs. 68,50,000

ii. Present value of minimum lease payment from Lessor's view point

Lease liability Rs. 47,39,540 + present value of (URV) unguaranteed residual value (Rs. 1,50,000 x 0.5718) = Rs. 48,25,310

Unearned Finance Income = (a) – (b) = Rs. 68,50,000 – Rs. 48,25,310= Rs. 20,24,690

*Minimum Lease Payment of 4th year includes guaranteed residual value amounting i.e 16,00,000 + 3,00,000 =19,00,000.

QUESTION 04

A machine was given on 3 years operating lease by a dealer of the machine for equal annual lease rentals to yield 30% profit margin on cost Rs. 1,50,000. Economic life of the machine is 5 years and output from the machine are estimated as 40,000 units, 50,000 units, 60,000 units, 80,000 units and 70,000 units consecutively for 5 years. Straight line depreciation in proportion of output is considered appropriate. Compute the following:

i. Annual Lease Rent
ii. Lease Rent income to be recognized in each operating year and
iii. Depreciation for 3 years of lease.

SOLUTION:

i. Annual lease rent

Total lease rent

=130% of Rs. 1,50,000 output during lease periodtotal output

=130% of Rs. 1,50,000 x (40,000+50,000+60,000) / (40,000+50,000+ 60,000+80,000+70,000)

=1,95,000 x 1,50,000 units / 3,00,000 units=Rs. 97,500

Annual lease rent = Rs. 97,500 / 3 = Rs. 32,500

ii. Lease rent Income to be recognized in each operating year

Total lease rent should be recognised as income in proportion of output during lease period, i.e. in the proportion of 40:50:60.

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

Year 1 Rs. 26,000,
Year 2 Rs. 32,500 and
Year 3 Rs. 39,000.

Scanned with OKEN Scanner

iii. *Depreciation for three years of lease*

Since depreciation in proportion of output is considered appropriate, the depreciable amount Rs. 1,50,000 should be allocated over useful life 5 years in proportion of output, i.e. in proportion of 40:50:60:80:70

Depreciation for year 1 is Rs. 20,000, year 2 = 25,000 and year 3 = 30,000.

QUESTION 05

Journalise in each of the following cases assuming transaction is of sale and operating lease back:

Cases	Fair Value	Book Value	Sale Price
1	100000	100000	100000
2	100000	80000	100000
3	100000	120000	100000
4	100000	100000	120000
5	100000	80000	120000
6	100000	120000	120000
7	100000	100000	90000
8	100000	90000	80000
9	100000	70000	80000
10	100000	110000	80000

Answer:

1) No Profit/Loss

2) Gain 20000 => P & L immediately

3) Loss 20000

General Rule – Immediately transfer to P&L

Exception – If loss is compensated with future lease payments then Deferred &Amortised.

4) Gain = 20000 D&A

5) Gain = 40000 — 20K P & L
20K D&A

6) Rule-3 => Imp. Loss = 20000 P & L

Rule-2 => Profit = 20000 D&A

7) Loss = 10000 — Generally P & L
If compensated with rent then D&A

8) Loss = 10000 (same as 7)

9) Gain = 10000 P & l (Rule 2)

10) Rule – 3 => Imp. Loss 10000 P & L

Rule – 1 => Loss = 20000

Scanned with OKEN Scanner

2. AS – 20 "EARNINGS PER SHARE"

QUESTION 06

On 1st April, 20X1 a company had 6,00,000 equity shares of Rs. 10 each (Rs. 5 paid up by all shareholders). On 1st September, 20X1 the remaining Rs. 5 was called up and paid by all shareholders except one shareholder having 60,000 equity shares. The net profit for the year ended 31st March, 20X2 was Rs. 21,96,000 after considering dividend on preference shares of Rs. 3,40,000.

You are required to compute Basic EPS for the year ended 31st March, 20X2 as per Accounting Standard 20 "Earnings Per Share".

SOLUTION:

Basic earnings per share (EPS) =

net profit attributable to equity shareholders weighted average number of equity shares outstanding during the year

= 21,96,0004,57,500 shares = Rs. 4.80 per share

Working note:

Calculation of weighted average number of equity shares

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

Date	No. of equity shares	Amount paid per share	Weighted average no. of equity shares
	Rs.	Rs.	Rs.
1.4.20X1	6,00,000	5	6,00,000 x 5/10 x 5/12 = 1,25,000
1.9.20X1	5,40,000	10	5,40,000 x 7/12 = 3,15,000
1.9.20X1	60,000	5	60,000 x 5/10 x 7/12 = 17,500
Total weighted average equity shares			4,57,500

000 / (10,00,000+ 5,00,000)

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

= Rs. 41.53 per share

Basic EPS for the year 2021-2022

Basic EPS = Total Earnings – Preference Shares Dividend) / (Total shares outstanding at the beginning + Bonus issue + weighted average of the shares issued in January, 2022)

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

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

= Rs. 5.29 per share

QUESTION 07

NAT, a listed entity, as on 1st April,2021 had the following capital structure:

	Rs.
10,00,000 Equity Shares having face value of Rs. 1 each	10,00,000
10,00,000 8% Preference Shares having face value of Rs. 10 each	1,00,00,000

During the year 2021-2022, the company had profit after tax of Rs. 90,00,000

On 1st January,2022, NAT made a bonus issue of one equity share for every 2 equity shares outstanding as at 31st December,2021.

On 1st January,2022, NAT issued 2,00,000 equity shares of Rs. 1 each at their full market price of Rs. 7.60 per share. NAT's shares were trading at Rs. 8.05 per share on 31st March,2022.

Scanned with OKEN Scanner

Further it has been provided that the basic earnings per share for the year ended 31st March,2021 was previously reported at Rs. 62.30.

You are required to:

I. Calculate the basic earnings per share to be reported in the financial statements of NAT for the year ended 31st March,2022 including the comparative figure, in accordance with AS-20 Earnings Per Share.

II. Explain why the bonus issue of shares and the shares issue at full market price are treated differently in the calculation of the basic earnings per share?

SOLUTION

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

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

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

= Rs. 6,23,00,000

b. Adjusted Earnings per share after taking into consideration bonus issue

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

= Rs. 6,23,00

ii. In case of a bonus issue, equity shares are issued to existing shareholders for no additional consideration. Therefore, the number of equity shares outstanding is increased without an increase in resources. Since the bonus issue is an issue without consideration, the issue is treated as if it had occurred prior to the beginning of the year 2021, the earliest period reported.

However, the share issued at full market price does not carry any bonus element and usually results in a proportionate change in the resources available to the enterprise. Therefore, it is taken into consideration from the time it has been issued i.e., the time- weighting factor is considered based on the specific shares outstanding as a proportion of the total number of days in the period

QUESTION 08

From the following information, you are required to compute the basic and adjusted Earnings per share:

Net profit for 2015-16	11 lakh
Net profit for 2016-17	15 lakh
No. of shares issued before rights issue	5 lakhs
Right issue	One for every 5 held
Right issue price	15 per share
Last date of exercising right option	1-06-2016
Fair value of shares before right issue	21 per share

ANSWER:

Computation of theoretical ex-rights fair value per share

Fair value of all outstanding shares immediately prior to exercise of rights

+ Total amount received from exercise of rights

Number of shares outstanding prior to exercise +

number of shares issued in the exercise

(Rs. 21.00 x 5,00,000 shares) + (Rs.15.00 x 1,00,000 shares)

5,00,000 shares + 1,00,000 shares

Theoretical ex-rights fair value per share = Rs. 20.00

(a) Computation of adjustment factor

(b) $\frac{\text{Fair value per share prior to exercise of rights}}{\text{Theoretica I ex-right value per share}} = \frac{\text{Rs.}(21.00)}{\text{Rs.}(20.00)}$ = 1.05

Scanned with OKEN Scanner

Computation of earnings per share

	Year 2015-16	Year 2016-17
EPS for the year 2015-16 as originally reported: (Rs. 11,00,000/5,00,000 shares)	Rs. 2.20	
EPS for the year 2015-16 restated for rights issue: [Rs. 11,00,000/ (5,00,000 shares x 1.05)]	Rs. 2.10	
EPS for the year 2016-17 including effects of rights issue $\frac{\text{Rs. } 15,00,000}{\left(5,00,000 \times \frac{1.05}{12}\right) + \left(6,00,000 \times \frac{10}{12}\right)}$		Rs. 2.55

QUESTION 09

EAESH = 18,00,000

No. of Equity Shares = 1,00,000

During the year, 10,000 no. of Debenture @ 11% Interest issued at face value 100/-

Conversion into equity is 40,000 no. after 3 years

Interest paid on such Debenture = 27,500/-

SOLUTION

Debenture must have been issued on 1/Jan/24

Since Interest of 27,500 belongs to 3 months

Interest	Months
1,10,000	12
27,500	?

DEPS = 18,00,000 + (27,500 x 70%)/1,00,000 + (40,000 x 3/12)

= 16.53/-

QUESTION 10

Net Profit for the year 2020	Rs. 12,00,000
Weighted Avg. number of equity shares outstanding during the year 2020	5,00,000 shares
Avg. Fair Value of one equity share during the year 2020	Rs. 20.00
Weighted Avg. number of equity shares under option during the year 2020	1,00,000 shares
Exercise price for shares under option during the year 2020	Rs. 15

Compute Basic and Diluted Earnings Per Share.

SOLUTION

Particulars	Earnings	Shares	EPS
Net Profit for the Year 2020	12,00,000	-	
Weighted avg. no. of shares 2020	-	5,00,000	
Basic EPS			2.40/-
No. of Shares under options	-	1,00,000	
Number of Shares that would have been issued at Fair Value (100000 x 15) / 20	-	(75,000)	
Diluted EPS	**12,00,000**	**5,25,000**	**2.29/-**

Note: The earnings have not been increased as the total number of shares has been increased only by the number of shares (25,000) deemed for the purpose of the computation to have been issued for no consideration.

EPS in case of Discontinued Operations:

If there is a loss in continuing operation then while calculating DEPS, do not consider potential equity share. Consider Ordinary equity shares only for DEPS also.

Scanned with OKEN Scanner

QUESTION 11:

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

Solution

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

Scanned with OKEN Scanner

3. AS - 11

QUESTION 12:

Vsmart Ltd. took a Foreign Currency Loan of $1,00,000 to purchase machine of the same amount. On 1st April, 2022 Loan is of 5Years. To be repaid in lumpsum after 5 Years.

Depreciation Rate is 10%

Exchange rates are as follows:

On 1/4/22 - $1 = ₹ 78

On 31/3/23 - $1 = ₹ 82

On 31/3/24 - $1 = ₹ 80.5

Show A/c as per AS 11 in following cases:

a. Without PARA 46

b. With PARA 46

Solution:

1. Initial Recognition:

Foreign Currency should recognise at the rate prevailing on transaction Date (i.e. SPOT Rate) i.e. $1 = ₹ 78

Transaction Value = $1,00,000 x 78 = 78,00,000

1/4/22

Particulars		Dr.	Cr.
Machine A/c To Foreign Currency Loan A/c	Dr.	78,00,000	78,00,000

(Note: assuming machine is measured at cost always)

(Note: Foreign Currency Loan is a LTFCMI)

2. Subsequent measurement:

Case 1: without PARA 46

Exchange Difference due to Subsequent measurement shall be transfer to Profit & Loss A/c

1st Year end: 31/3/23

Foreign Currency Loan Should be = $1,00,000 x 82 = 82,00,000

Exchange Difference (Loss) = 4,00,000

31/3/23

Particulars		Dr.	Cr.
Exchange Difference (P&L) A/c To Foreign Currency Loan A/c	Dr.	4,00,000	4,00,000
Profit & Loss A/c To Exchange Difference A/c	Dr.	4,00,000	4,00,000

2nd Year end: 31/3/24

Foreign Currency Loan Should be = $1,00,000 x 80.5 = 80,50,000

Exchange Difference (Gain) = 82 – 80.5 = 1,50,000

Particulars		Dr.	Cr.
Foreign Currency Loan A/c To Exchange Difference (P&L) A/c	Dr.	1,50,000	1,50,000
Exchange Difference (Gain) A/c To Profit & Loss A/c	Dr.	1,50,000	1,50,000

Case 2: with PARA 46

Exchange Difference should be adjusted to the cost of machine

31/3/23

Exchange Difference (Loss) = 4,00,000

Scanned with OKEN Scanner

Machine A/c Dr.	4,00,000	
To Foreign Currency Loan A/c		4,00,000

Depreciation @10& = 82,00,000 x 10% = 8,20,000
Remaining Balance of Machine = 73,80,000
31/3/24
Exchange Difference (Gain) = 1,50,000
Deduct From Machines Book Value

Foreign Currency Loan A/c Dr.	1,50,000	
To Machine A/c		1,50,000

Depreciation @10% on (73,80,000 – 1,50,000) = 72,30,000 x 10% = 7,23,000

QUESTION 13:

Vsmart Ltd. took a loan of $75,000 on 1/4/22 when $1 = ₹ 78. Loan is utilized for working capital requirement loan is of 6 Years. Principal repayment equally every year.
1st year end - $1 = ₹ 81.30
2nd year end - $1 = ₹ 82.15
3rd year end - $1 = ₹ 82
4th year end - $1 = ₹ 81.50
5th year end - $1 = ₹ 81.90
6th year end - $1 = ₹ 82
Apply PARA 46 of AS 11:

Solution:

1. **Initial Recognition:**

Bank A/c Dr.	58,50,000	
To Foreign Currency Loan A/c		58,50,000

2. **Subsequent Measurement:**

31/3/23 (Fist remeasure then pay installment)

FCMIT Difference A/c Dr.	2,47,500	
To FC Loan A/c ($75,000 x 3.30)		2,47,500
FC Loan A/c Dr.	10,16,250	
To Bank A/c ($12,500 x 81.30)		10,16,250

Foreign Currency Book Value = 50,81,250
Amortize FCMIT Difference in 6 Years = 2,47,500 / 6 = 41,250

Profit & Loss A/c Dr.	41,250	
To FCMIT Difference A/c		41,250

Balance unamortised FCMIT = 2,06,250 (Dr. Balance)

31/3/24	31/3/25	31/3/26	31/3/27	31/3/28
$1 = ₹ 82.15	$1 = ₹ 82	$1 = ₹ 81.50	$1 = ₹ 81.90	$1 = ₹ 82
Prev. rate = 81.30	Prev. rate = 81.25	Prev. rate = 82	Prev. rate = 81.50	Prev. rate = 81.90
Loss = 0.85 x $62,500	Gain = 0.15 x $50,000	Gain = 0.5 x $37,500	Loss = 0.4 x $12,500	Loss = 0.10 x $12,500
Total Loss = 53,125	Total Gain = 7,500	Total Gain = 18,750	Total Loss = 10,000	Total Loss = 1,250
Loss added to FCMIT Difference	Deduct from FCMIT Difference	Deduct from FCMIT Difference	Added to FCMIT Difference	Added to FCMIT Difference

Scanned with OKEN Scanner

Revised FCMIT Difference = 2,59,375	Revised FCMIT Difference = 2,00,000	Revised FCMIT Difference = 1,31,250	Revised FCMIT Difference = 97,500	Revised FCMIT Difference = 50,000
Year = 5	Year = 4	Year = 3	Year = 2	Year = 1
P&L A/c = 51,875	P&L A/c amortised = 50,000	P&L A/c amortised = 43,750	P&L A/c amortised = 48,750	Fully amortised to P&L A/c = 50,000
Closing Balance of FCMIT = 2,07,500	Closing Balance of FCMIT = 1,50,000	Closing Balance of FCMIT = 87,500	Closing Balance of FCMIT = 48,750	

QUESTION 14

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

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

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

SOLUTION

Amount of Exchange difference and its Accounting Treatment

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

Thus, Exchange Difference on Long term loan amounting Rs. 1,00,000 may either be charged to Profit and Loss A/c or to Foreign Currency Monetary Item Translation Difference Account but exchange difference on trade receivables amounting Rs. 50,847.456 is required to be transferred to Profit and Loss A/c.

QUESTION 15

Om Ltd. purchased an item of property, plant and equipment for US $ 50 lakh on 01.04.2019 and the same was fully financed by the foreign currency loan [US $] repayable in five equal installments annually. (Exchange rate at the time of purchase was 1 US $ = Rs. 60]. As on 31.03.2020 the first installment was paid when 1 US $ fetched ₹ 62.00. The entire loss on exchange was included in cost of goods sold. Om Ltd. normally provides depreciation on an item of property, plant and equipment at 20% on WDV basis and exercised the option to adjust the cost of asset for exchange difference arising out of loan restatement and payment. Calculate the amount of exchange loss, its treatment and depreciation on this item of property, plant and equipment.

SOLUTION

Exchange differences arising on restatement or repayment of liabilities incurred for the purpose of acquiring an item of property, plant and equipment should be adjusted in the carrying amount of the respective item of property, plant and equipment as Om Ltd. has exercised the option and it is long term foreign currency monetary item. Thus, the entire exchange loss due to variation of Rs. 20 lakhs on 31.03.2020 on payment of US $ 10 lakh, should be added to the

Scanned with OKEN Scanner

carrying amount of an item of property, plant and equipment and not to the cost of goods sold. Further, depreciation on the unamortized depreciable amount should also be provided.

Calculation of Exchange loss:

Foreign currency loan (in Rs.) = (50 lakh $ x Rs. 60) = Rs. 3,000 lakhs

Exchange loss on outstanding loan on 31.03.2020 = Rs. 40 lakh US $ x (62.00-60.00) = Rs. 80 lakhs.

So, Rs. 80 lakhs should also be added to cost of an item of property, plant and equipment with corresponding credit to outstanding loan in addition to Rs. 20 lakhs on account of exchange loss on payment of installment. The total cost of an item of property, plant and equipment to be increased by Rs. 100 lakh. Total depreciation to be provided for the year 2019-2020 = 20% of (Rs. 3,000 lakh + 100 lakh) = Rs. 620 lakhs.

QUESTION 16

Trower Limited is an Indian importer. It imports goods from True View Limited situated at London. Trower Limited has a payable of £ 50,000 to True view Limited as on 31st March, 2023. True View Limited has given Trower Limited has given Trower Limited the following two option:

i. Pay immediately with a cash discount of 1% on the payable.

ii. Pay after 6 months with interest @ 5% p.a. on the Payable.

The borrowing rate for Trower Limited in rupees is 15% p.a.

The following are the exchange rates:

Date	₹/£
31st March,2023	97
30th September, 2023	99

You are required to given your opinion to Trower Limited on which of the above two options to be chosen.

Solution

Option (i) Pay immediately with Cash discount of 1% on the payable

	₹
Total amount payable as on 31.3.2023 (50,000 x ₹ 97)	48,50,000
Less: Cash discount	(48,500)
	48,01,500
Add: Borrowing cost @ 15% p.a. for 6 months	3,60,112.50
If payment made immediate	51,61,612.50

Option (ii) Pay after 6 months with interest @ 5% p.a. on the payable

	₹
Total amount payable as on 31.3.2023 (50,000 x ₹ 99)	49,50,000
Interest for 6 months @ 5%	1,23,750
If payment made after 6 months	50,73,750

Thus, Option (ii) is beneficial to Trower Limited as the Rupee outflow will be lower by ₹ (51,61,612 – 50,73,750) = ₹ 87,862 in option (ii).

Note: The above answer be presented in the **alternative manner** given as below:

Option (i) Pay immediately with Cash discount of 1% on the payable

Total amount payable on 31.3.2023	50,000
Less: Cash discount (50,000 x 1 / 100)	(500)

Scanned with OKEN Scanner

49,500 x ₹ 97	49,500 48,01,500
Add: Borrowing cost @ 15% p.a. for 6 months	3,60,112.50
If payment made immediate	₹ 51,61,612.50

Option (ii) Pay after 6 months with interest @ 5% p.a. on the payable

	₹
Total amount payable on 31.3.2023	50,000
Interest for 6 months @ 5% (50,000 x 5 / 100 x 6 / 12)	1,250
If payment made after 6 months (51,250 x 99)	51,250 50,73,750

Thus, Option (ii) is beneficial to Trower Limited as the Rupee outflow will be lower by ₹ (51,61,612 – 50,73,750) = ₹ 87,862 in option (ii).

QUESTION 17

(i) Jared Limited purchased a Machine for US $ 20,000 on 31st December, 2021 payable after four months. It entered into a forward contract for four months @ ₹ 78.85 per US $. On 31st December,2021 the exchange rate was ₹ 77.50 per US $.

How will you recognize the Profit or Loss on Forward Contract for the year ended 31st March,2022 in the books of Jared Limited?

(ii) Trade Payables of Jared Limited includes amount due to Sterling Limited ₹ 9,75,000 recorded at the prevailing exchange rate on the date of purchase; transaction recorded at US $ 1 = ₹ 75.00. The exchange rate on Balance Sheet date (31st March,2022) was US $ 1 = 79.00 The payment was made on 1st May,2022 when the exchange rate was US $ 1 = ₹ 78.30.

You are required to calculate the amount of exchange difference on 31st March, 2022 and 1st May, 2022 and also explain the accounting treatment needed in the above case as per AS 11 in the books of Jared Limited.

Solution

(i)

	₹
Forward Rate	78.85
Less: Spot Rate	(77.50)
Premium on Contract	1.35
Contract Amount	US$ 20,000
Total Loss (20,000 x 1.35)	**₹ 27,000**

Contract period 4 months (3 months falling in the year ended 31st March, 2022)

Loss to be recognized (₹27,000x 3/4) = ₹ 20,250 in the year ended 31st March, 2022.

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

Trade payables	**Foreign Currency Rate**	**Amount ₹**
Initial recognition US $13,000 (9,75,000/75)	1 US $ = ₹ 75	
Exchange Rate on Balance sheet date	1 US $ = ₹ 79	
Exchange Difference Loss US $ 13,000 X (79-75)		52,000
Exchange Rate on Settlement date	1 US $ = ₹ 78.30	
Exchange Difference Profit US $ 13,000x(79-78.30)		9,100

Scanned with OKEN Scanner

For the year ended 31st March, 2022 exchange difference loss amounting ₹ 52,000 will be charged to statement of Profit & Loss A/c.

However, there is exchange difference gain of ₹ 13,000 x (79-78.30) = 9,100 on 1st May, 2022. Thus, gain of ₹ 9,100 will be credited to statement of Profit & Loss A/c for the year ended 31st March, 2023.

QUESTION 18

Mr. A bought a forward contract for three months of US$ 1,00,000 on 1st December at 1 US$ = Rs 47.10 when exchange rate was US$ 1 = Rs 47.02. On 31st December when he closed his books exchange rate was US$ 1 = Rs 47.15. On 31st January, he decided to sell the contract at Rs 47.18 per dollar. Show how the profits from contract will be recognised in the books.

SOLUTION

Since the forward contract was for speculation purpose the premium on contract i.e. the difference between the spot rate and contract rate will not be recorded in the books. Only when the contract is sold the difference between the contract rate and sale rate will be recorded in the Profit & Loss Account.

Sale Rate	Rs 47.18
Less: Contract Rate	(Rs 47.10)
Premium on Contract	Rs 0.08
Contract Amount	US$ 1,00,000
Total Profit (1,00,000 x 0.08)	**Rs 8,000**

Scanned with OKEN Scanner

4. BRANCH

QUESTION 19

Delhi HO sends goods to its Pune branch at 20% above cost. Branch has been instructed by HO to sell goods as under: -

Cash sales at IP

Credit sales at SP (Which is 50% above cost)

1) Opening stock = Rs. 75,000 (IP)
2) Goods sent to branch = Rs. 5,40,000 (IP)
3) Cash sales = Rs. 1,08,000 (IP)
4) Credit sales = Rs. 4,65,000 (SP)
5) Sales return by credit customer = Rs. 22,500 (SP)
6) Sales return by cash customer =Rs. 12,000 (IP)
7) Goods return by branch to HO = Rs. 48,000 (IP)
8) Goods received by branch till year end = Rs. 5,10,000 (IP)
9) Closing stock at the end = Rs. 72,000 (IP)

SOLUTION

Opening Stock (Cost) – 62,500 + Net Goods Sent to Branch – 4,10,000 ((5,40,000 – 48,000) / 120 x 100)				
Total (IP) – 4,72,500				
COGS (IP)	**Closing Stock**	**Goods in Transit**	**Shortage (b/f)**	**Gross Profit**
1) Cash Sales: Net Sales = 96,000 / 120 x 100 COGS (Cash) = 80,000 2) Net Credit Sales = 4,42,500 (SP) COGS = 4,42,500 / 150 x 100 = 2,95,000 Total COGS = 3,75,000	60,000	25,000	12,500	1,63,500

Memorandum Branch Trading and P&L A/c

To Opening Stock	62,500	By Sales Net Cash Net Credit	 96,000 4,42,500
To Net Goods sent to Branch	4,10,000	By Shortage	12,500
To Gross Profit	1,63,500	By Closing Stock In Hand In Transit	 60,000 25,000
	6,36,000		**6,36,000**
To Abnormal Loss	12,500	By Gross Profit	1,63,500
To Net Profit	1,51,000		
	1,63,500		**1,63,500**

QUESTION 20

Following is the information of the Jammu branch of Best New Delhi for the year ending 31st March, 20X2 from the following:

(1) Goods are invoiced to the branch at cost plus20%.

(2) The sale price is cost plus50%.

(3) Other information:

	Rs.
Stock as on 01.04.20X1(invoice price)	2,20,000
Goods sent during the year (invoice price)	11,00,000

Scanned with OKEN Scanner

Sales during the year	12,00,000
Expenses incurred at the branch	45,000

Ascertain

(i) the profit earned by the branch during the year.

(ii) branch stock reserve in respect of unrealized profit.

SOLUTION

(i) Calculation of profit earned by the branch

In the books of Jammu Branch

Trading Account and Profit and Loss Account

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

(ii) Stock reserve in respect of unrealized profit

= Rs. 3,60,000 x (20/120) = Rs. 60,000

(iii) Opening Stock = 36,667/-

Working Note:

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

QUESTION 21

Harrison of Chennai has a branch at New Delhi to which goods are sent @ 20% above cost. The branch makes both cash and credit sales. Branch expenses are met partly from H.O. and partly by the branch. The statement of expenses incurred by the branch every month is sent to head office for recording.

Following further details are given for the year ended 31st December, 20X1:

		Rs.
Cost of goods sent to Branch at cost		2,00,000
Goods received by Branch till 31-12-20X1 at invoice price		2,20,000
Credit Sales for the year @ invoice price		1,65,000
Cash Sales for the year @invoice price		59,000
Cash Remitted to head office		2,22,500
Expenses paid by H.O.		12,000
Bad Debts written off		750
Balances as on	**1-1-20X1**	**31-12-20X1**
Stock	25,000 (Cost)	28,000 (invoice price)
Debtors	32,750	26,000
Cash in Hand	5,000	2,500

Scanned with OKEN Scanner

Show necessary ledger accounts in the books of the head office and determine the Profit and Loss of the Branch for the year ended 31st December, 20X1.

SOLUTION

Books of Harrison

Branch Stock Account

	Rs.		Rs.
To Balance b/d	30,000	By Branch Debtors	1,65,000
To Goods Sent to Branch A/c	2,40,000	By Branch Bank	59,000
To Branch Adjustment A/c (Excess of sale over invoice price)	2,000	By Balance c/d	
		Goods in Transit (Rs. 2,40,000 –Rs. 2,20,000)	20,000
		By Stock at Branch	28,000
	2,72,000		**2,72,000**

Branch Debtors Account

	Rs.		Rs.
To Balance b/d	32,750	By Bad debts written off	750
To Branch Stock	1,65,000	By Branch Cash- collection (bal. fig.)	1,71,000
		By Balance c/d	26,000
	1,97,750		**1,97,750**

Branch Cash Account

	Rs.		Rs.
To Balance b/d	5,000	By Bank Remit to H.O.	2,22,500
To Branch Stock	59,000	By Branch profit & loss A/c [Bal. fig. (exp. Paid by Branch)]	10,000
To Branch Debtors	1,71,000	By Balance c/d	2,500
	2,35,000		**2,35,000**

Branch Adjustment Account

	Rs.		Rs.
To Stock Reserve (on closing stock (48,000 × 1/6)	8,000	By Stock Reserve opening (25000 ×20%)	5,000
To Gross Profit c/d	39,000	By Goods sent to Branch A/c	40,000
		By Branch Stock A/c	2,000
	47,000		**47,000**

Branch Adjustment Account

	Rs.		Rs.
To Cash (H.O)	12,000		
To Branch Cash	10,000	By Branch P&L a/c	22,000
	22,000		**22,000**

Branch Profit and Loss Account

	Rs.		Rs.
To Branch Expenses (paid by HO: Rs. 12,000 and paid by Branch Rs. 10,000)	22,000	By Gross Profit b/d	39,000
To Branch Debtors-Bad debts	750		
To Net Profit	16,250		

Scanned with OKEN Scanner

	39,000		39,000

Goods Sent to Branch Account

	Rs.		Rs.
To Branch Adjustment A/c To Purchase A/c –Transfer	40,000 2,00,000	By Branch to Stock A/c	2,40,000
	2,40,000		**2,40,000**

QUESTION 22

Ayan Ltd. Invoices goods to its branch at cost plus $33\frac{1}{3}$%From the following Particulars prepare Branch Stock Account, Branch Stock Adjustment Account and Branch Profit and Loss Account as they would appear in the books of head office.

	Rs
Stock at commencement at Branch at invoice Price	3,60,000
Stock at close at Branch at Invoice Price	2,88,000
Goods sent to Branch during the year at invoice price (including goods invoiced at Rs. 48,000 to Branch on 31.03.2018 but not received by Branch before close of the year).	24,00,000
Return of goods to head office (invoice Price)	1,20,000
Credit Sales at Branch	1,20,000
Invoice value of goods pilfered	24,000
Normal loss at Branch due to wastage and deterioration of stock (at invoice price)	36,000
Cash Sales at Branch	21,60,000

Ayan closes its books on 31st March, 2018.

SOLUTION

In the books of Head Office Branch Stock Account

Particulars	Rs	Particulars	Rs
To Balance b/d	3,60,000	By Bank A/c (cash Sales)	21,60,000
To Goods sent to Branch A/c	24,00,000	By Branch Debtors A/c (Credit Sales)	1,20,000
To Branch Adjustment A/c – balancing fig. (Surplus)***	36,000	By Goods sent to Branch A/c (Returns to H.O.)	1,20,000
		By Branch Adjustment A/c* (Rs. 24,000 x25/100)	6,000
		By Branch P&L A/c * (Cost of Abnormal Loss)	18,000
		By Branch Adjustment A/c** (Invoice price of normal loss)	36,000
		By Balance c/d: In hand in transit	 2,88,000 48,000
	27,96,000		**27,96,000**

- Alternatively, combined posting for the amount of Rs. 24,000 may be passed through Goods pilfered account.
- Alternatively, it may first be transferred to normal Loss account which may ultimately be closed by transfer to Branch Adjustment account. The final amount of net profit will however remain same.
- It has been considered that the surplus may be due to sale of goods by branch at price higher than invoice price.

Branch Stock Adjustment Account

Particulars	(Rs)	Particulars	(Rs)
To Branch Stock A/c (Loading on	6,000	By Stock Reserve A/c	90,000

Scanned with OKEN Scanner

Abnormal Loss)		(Rs. 3,60,000 x 25/100)	
To Branch Stock A/c (Normal Loss)	36,000	By Goods Sent to Branch A/c (Rs. 24,00,000 – Rs. 1,20,000) x 25/100	5,70,000
To Stock Reserve A/c (Rs. 3,36,000x25/100)	84,000	By Branch Stock A/c (Surplus)	36,000
To Gross Profit t/f to P & L A/c	5,70,000		
	6,96,000		**6,96,000**

Branch Profit and Loss Account

Particulars	Rs	Particulars	Rs
To Branch Stock A/c (Cost of Abnormal Loss)	18,000	By Branch Adjustment A/c (Gross Profit)	5,70,000
To Net Profit t/f to General P & LA/c	5,52,000		
	5,70,000		**5,70,000**

QUESTION 23

Buckingham Bros, Bombay have a branch at Nagpur. They send goods at cost to their branch at Nagpur. However, direct purchases are also made by the branch for which payments are made at head office. All the daily collections are transferred from the branch to the head office.

From the following, prepare Nagpur branch account in the books of head office by Debtors method.

	Rs.		Rs.
Opening balance (1-1-20X1) Impress Cash	2,000	Bad Debts	1,000
Sundry Debtors	25,000	Discount to Customers	2,000
Stock: Transferred from H.O.	24,000	Remittances to H.O.	
Direct Purchases	16,000	(recd. by H.O.)	1,65,000
Cash Sales	45,000	remittances to H.O.	
Credit Sales	1,30,000	(Not recd. by H.O. so far)	5,000
Direct Purchases	45,000	Branch Exp. directly paid by H.O.	30,000
Returns from Customers	3,000	Closing Balance (31-12- 20X1)	
Goods sent to branch from H.O.	60,000	Stock: Direct Purchase	10,000
Transfer from H.O. for Petty	4,000	Transfer from H.O.	15,000
Cash expenses		Debtors	?
		Imprest Cash	?
		Petty Cash expenses	4,000

SOLUTION

In the Books of Buckingham Bros,
Bombay Nagpur Branch Account

Particular	Amount	Particular	Amount	Amount
To Opening Branch Assets Stock (24,000+16,000) Debtors Imprest Cash	 40,000 25,000 2,000	By Bank – Remittances received from branch Cash Sales Cash from Debtors Cash from Debtors in transit	 45,000 1,20,000 5,000	 1,70,000
To Goods sent to Branch A/c	60,000	By Stock: Transfer from H.O. Direct Purchase		 15,000 10,000

Scanned with OKEN Scanner

To Creditors (Direct Purchases)	45,000	By Sundry Debtors (W.N. 2)		24,000
To Bank (Sundry exp.)	30,000	By Imprest Cash (W.N. 3)		2,000
To Bank (Petty cash exp.)	4,000			
To Net Profit transferred to General Profit & Loss A/c	15,000			
	2,21,000			2,21,000

Working Notes:

(1) Memorandum Debtors A/c

Particulars	Amount Rs.	Particulars	Amount Rs.
To Balance b/d	25,000	By Sales Return	3,000
To sales	1,30,000	By Bad Debts	1,000
		By Discount	2,000
		By Cash	1,25,000
		By Balance c/d	24,000
	1,55,000		**1,55,000**

(2)Memorandum Petty Cash

Particulars	Amount Rs.	Particulars	Amount Rs.
To Balance b/d	2,000	By Expenses (met by Br.)	4,000
To transfer from H.O	4,000	By Balance c/d	2,000
	6,000		**6,000**

QUESTION 24

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

Following are the other details:

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

	(Delhi)	
Balance as on:	1-1-20X1	31-12-20X1
Stock: Ghee	1,50,000	3,12,500
Oil	3,50,000	4,17,250
Debtors	7,32,750	-
Cash on Hand	70,520	55,250
Furniture & Fittings	21,500	19,350
Plant/Machinery	3,07,250	7,73,500

Scanned with OKEN Scanner

	(Lucknow)	
Balance as on:	1-1-20X1	31-12-20X1
Stock: Ghee	17,000	13,250
Oil	27,000	44,750
Debtors	75,750	?
Cash on Hand	7,540	12,350
Furniture & Fittings	6,250	5,625
Plant/Machinery	-	

- Addition to Plant/Machinery on 1-1-20X1 Rs. 6,02,750.
- Rate of Depreciation: Furniture / Fittings @ 10% and Plant / Machinery @ 15% (already adjusted in the above figures).
- The Branch Manager is entitled to 10% commission after charging such commission whereas, the General Manager is entitled to 10% commission on overall company profits after charging such commission. General Manager is also entitled to a salary of Rs. 2,000 p.m. General expenses incurred by H.O. Rs. 24,000.

Prepare Branch Account in the head office books and also prepare the Arnold's Trading and Profit and Loss A/c (excluding branch transactions).

SOLUTION

In the books of Arnold

Lucknow Branch Account

To Balance b/d		By Bank (Remittance to H.O.)	6,13,250
To Opening stock:		By Balance c/d	
Ghee	17,000	Closing stock:	
Oil	27,000	Ghee	13,250
Debtors	75,750	Oil	44,750
Cash on hand	7,540	Debtors (W.N. 1)	86,900
Furniture & fittings	6,250	Cash on hand (W.N. 2)	12,350
To Goods sent to Branch A/c		Furniture & fittings	5,625
Ghee (15 x 1500 x 12)	2,70,000		
Oil (25 x 1000 x 12)	3,00,000		
To Bank (Expenses paid by H.O.)	14,250		
To Branch Manager commission (Rs. 58,335 × 1/11)	5,303		
To Net Profit transferred			
to General P & L A/c	53,032		
	7,76,125		**7,76,125**

Arnold Trading and Profit and Loss account for the year ended 31st December, 20X1 (Excluding branch transactions)

		Rs.		Rs.
To Opening Stock:			By Sales:	
Ghee		1,50,000	Ghee	18,46,350
Oil		3,50,000	Oil	27,41,250
To Purchases:			By Closing Stock:	
Ghee	14,75,000	12,05,000	Ghee	3,12,500
Less: Goods sent to Branch	(2,70,000)		Oil	4,17,250
Oil	29,32,000			
Less: Goods sent to Branch	(3,00,000)	26,32,000		

Scanned with OKEN Scanner

To Direct Expenses	3,83,275		
To Gross Profit	5,97,075		
	53,17,350		**53,17,350**
To Manager's Salary	24,000	By Gross Profit	5,97,075
To General Expenses	24,000	By Branch Profit transferred	53,032
To Depreciation			
Furniture @10% 2,150			
Plant & Machinery @ 15% (W.N.3) 1,36,500	1,38,650		
To General Manager's Commission @ 10% (i.e., 4,63,457 × 1/11)	42,132		
To Net profit	4,21,325		
	6,50,107		**6,50,107**

Working Notes:

1. Debtors Account

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

2. Branch Cash Account

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

3.Depreciation on Plant & Machinery 3,07,250 x 15% + 6,02,750 x 15% = Rs. 1,36,500

QUESTION 25

Alpha Ltd. has a retail shop under the supervision of a manager. The ratio of gross profit at selling price is constant at 25 per cent throughout the year to 31st March, 2017.

Branch manager is entitled to a commission of 10 percent of the profit earned by his branch, calculated before charging his commission but subject to a deduction from such commission equal in 25 percent of any ascertained deficiency of branch stock. All goods were supplied to the branch in head office.

The following details for the year ended 31st March, 2017 are given as follows:

	Rs		**Rs**
Opening Stock (at cost)	74,736	Chargeable expenses	49,120
Goods sent to branch (at cost)	2,89,680	Closing Stock (Selling Price)	1,23,328
Sales	3,61,280		
Manager's commission paid on account	2,400		

From the above details, you are required to calculate the commission due to manager for the year ended 31st March, 2017.

Scanned with OKEN Scanner

SOLUTION

Step 1: Calculation of Deficiency

Branch stock account (at invoice price)

Particulars	Rs	Particulars	Rs
To Opening Stock (Rs. 74,736 + 1/3 of Rs. 74,736)	99,648	By Sales	3,61,280
To Goods sent to Branch A/c (Rs. 2,89,680 + 1/3 of Rs. 2,89,680)	3,86,240	By Closing Stock	1,23,328
		By Deficiency at sale price [Balancing figure]	1,280
	4,85,888		**4,85,888**

Step 2: Calculation of Net Profit before Commission

Branch account

Particulars	Rs	Particulars	Rs
To Opening [Rs. 74,736 + 1/3 of Rs. 74,736]	99,648	By Sales	3,61,280
To Gross sent to Branch A/c (Rs. 2,89,680 + 1/3 of Rs. 2,89,680)	3,86,240	By Closing Stock	1,23,328
To Expenses	49,120	By Stock Reserve A/c	24,912
To Stock Reserve A/c (Rs. 1,23,328 x 25/100]	30,832	By goods sent to Branch A/c	96,560
To Net Profit – subject to manager's commission	40,240		
	6,06,080		**6,06,080**

Step 3: Calculation of Commission still due to manager

		Rs
A	Calculation at 10% profit before charging his commission [Rs. 40,240 x 10/100]	4,024
B	Less: 25% of cost of deficiency in stock (25% of (75% of Rs. 1,280)	(240)
C	Commission for the year [A-B]	3,784
D	Less: Paid on account	(2,400)
E	**Balance due (C-D)**	**1,384**

QUESTION 26

Pass necessary Journal entries in the books of an independent Branch of M/s TPL Sons, wherever required, to rectify or adjust the following transactions:

(i) Branch paid Rs. 5,000 as salary to a Head Office Manager, but the amount paid has been debited by the Branch to Salaries Account.

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

(iii) Branch assets accounts retained at head office; depreciation charged for the year Rs. 15,000 not recorded by Branch.

(iv) Head Office expenses Rs. 75,000 allocated to the Branch, but not yet been recorded by the Branch.

(v) Head Office collected Rs. 60,000 directly from a Branch Customer. The intimation of the fact has not been received by the Branch.

(vi) Goods dispatched by the Head office amounting to Rs. 50,000, but not received by the Branch till date of reconciliation.

(vii) Branch incurred advertisement expenses of Rs. 10,000 on behalf of other Branches, but not recorded in the books of Branch.

(viii) Head office made payment of Rs. 16,000 for purchase of goods by branch, but not recorded in branch books.

Scanned with OKEN Scanner

SOLUTION

Books of Branch

Journal Entries

			Amounts Rs	
			Dr.	**Cr.**
(i)	Head Office Account To Salaries Account (Being rectification of salary paid on behalf of Head Office)	Dr.	5,000	5,000
(ii)	No entry in Branch Books is required.			
(iii)	Depreciation A/c To Head Office Account (Being depreciation of assets accounted for)	Dr.	15,000	15,000
(iv)	Expenses Account To Head Office Account (Being allocated expenses of Head Office recorded)	Dr.	75,000	75,000
(v)	Head Office Account To Debtors Account (Being adjustment entry for collection from Branch Debtors directly by Head Office)	Dr.	60,000	60,000
(vi)	Goods in-transit Account To Head Office Account (Being goods sent by Head Office still in-transit)	Dr.	50,000	50,000
(vii)	Head Office Account To expenses Account / To Cash (Being expenditure incurred, wrongly recorded in books)	Dr.	10,000	10,000
(vii)	Purchases account A/c / Creditors To Head Office Account (Being purchases booked)	Dr.	16,000	16,000

QUESTION 27

Show adjustment journal entry in the books of head office at the end of April, 20X1 for incorporation of inter – branch transactions assuming that only head office maintains different branch accounts in its books.

A. Delhi branch:

(1) Received goods from Mumbai – Rs. 35,000 and Rs. 15,000 from Kolkata.

(2) Sent goods to Chennai – Rs. 25,000, Kolkata – Rs. 20,000.

(3) Bill Receivable received – Rs. 20,000 from Chennai.

(4) Bill Acceptances sent to Mumbai – Rs. 25,000, Kolkata – Rs. 10,000.

B. Mumbai Branch (apart from the above):

(1) Received goods from Kolkata – Rs. 15,000, Delhi – Rs. 20,000.

(2) Cash sent to Delhi – Rs. 15,000, Kolkata – Rs. 7,000.

C. Chennai Branch (apart from the above):

(3) Received goods from Kolkata – Rs. 30,000.

(4) Acceptances and Cash sent to Kolkata – Rs. 20,000 and Rs.10,000 respectively.

D. Kolkata Branch (apart from the above):

(5) Sent goods to Chennai – Rs. 35,000.

(6) Paid cash to Chennai – Rs.15,000.

(7) Acceptances sent to Chennai – Rs.15,000.

Scanned with OKEN Scanner

SOLUTION

(a) Journal entry in the books of Head Office

Date	Particulars		Dr.	Cr.
			Rs.	Rs.
30th April, 20X1	Mumbai Branch Account	Dr.	3,000	
	Chennai Branch Account	Dr.	70,000	
	To Delhi Branch Account			15,000
	To Kolkata Branch Account			58,000
	(Being adjustment entry passed by head office in respect of inter-branch transactions for the month of April, 20X1)			

Working Note:

		Delhi	Mumbai	Chennai	Kolkata
		Rs.	Rs.	Rs.	Rs.
A.	Delhi Branch				
1	Received goods	50,000(Dr.)	35,000(Cr.)		15,000(Cr.)
2	Sent goods	45,000(Cr.)		25,000(Dr.)	20,000(Dr.)
3	Received Bills receivable	20,000(Dr.)		20,000(Cr.)	
4	Sent Acceptance	35,000(Cr.)	25,000 (Dr.)		10,000(Dr.)
B.	Mumbai Branch				
5	Received goods	20,000(Cr.)	35,000 (Dr.)		15,000(Cr.)
6	Sent cash		22,000 (Cr.)		
C.	Chennai Branch				
7	Received goods			30,000 (Dr.)	30,000(Cr.)
8	Sent cash and acceptances			30,000(Cr.)	30,000 (Dr.)
D.	Kolkata Branch				
9	Sent goods			35,000(Dr.)	35,000(Cr.)
10	Sent cash			15,000(Dr.)	15,000(Cr.)
11	Sent acceptances			15,000(Dr.)	15,000(Cr.)
		15,000 (Cr.)	**3,000(Dr.)**	**70,000(Dr.)**	**58,000(Cr.)**

QUESTION 28

Ring Bell Ltd. Delhi has a branch at Bombay where a separate set of books is used. The following is the Trail balance extracted on 31st Dec.,2010:

Particulars	HO		Branch	
	Dr.	Cr.	Dr.	Cr.
Equity Share capital	-	8,00,000	-	-
Profit & Loss a/c (01/01/2010)	-	25,310	-	-
Profit for 2010	-	82,200	-	31,700
Interim dividend paid	30,000	-	-	-
General Reserve	-	1,00,000	-	-
Fixed Assets	5,30,000	-	95,000	-
Stock	2,22,470	-	50,460	-
Debtors and Creditors	50,500	21,900	19,100	10,400
Cash Balance	62,730	-	6,550	-
HO a/c in branch books	-	-	-	1,29,010
Branch a/c in HO books	1,33,710	-	-	-

The difference between the balance of HO a/c and Branch a/c in both set of books is accounted for as follows:

(1) Cash remitted by the branch on 31st Dec 2010 but received by the HO on 1st Jan. 2011- 3,000/-

Scanned with OKEN Scanner

(2) Stock Stolen in transit from HO and charged to branch by the HO, but not credited to HO a/c in the branch books as the branch manager declined to admit any liability (not covered by insurance)- 1,700/-.

Give the Branch a/c in the HO books after incorporating the branch Trail balance through journal entries. Also prepare company's Balance Sheet as on 31st Dec., 2010.

(Answer: 10,39,810/-)

SOLUTION

The Branch Current Account in the Head Office Books and Head Office Current Account in the Branch Books do not show the same balances. Therefore, in order to reconcile them, the following journal entries will be passed in the Head Office books:

Journal Entries

		Dr.	Cr.
20X1		Rs.	Rs.
Dec., 31	Cash in Transit A/c Dr. To Branch Current A/c (Cash sent by the Branch on 31st Dec., 20X1 but received at H.O. on 1st Jan.,20X2)	3,000	3,000
	Loss by theft A/c Dr. To Branch Current A/c (Stock lost in transit from H.O. to Branch)	1,700	1,700

In order to incorporate, in the H.O. books, the given Branch trial balance which has been drawn up after preparing the Branch Profit &Loss Account, the following journal entries will be necessary:

Journal Entries

20X1			Rs.	Rs.
Dec. 31	Branch Current Account To Profit & Loss Account (Branch Profit for the year)	Dr.	31,700	31,700
	Branch Fixed Assets	Dr.	95,000	
	Branch Stock	Dr.	50,460	
	Branch Debtors	Dr.	19,100	
	Branch Cash	Dr.	6,550	
	To Branch Current Account (Branch assets brought into H.O. Books)			1,71,110
	Branch Current A/c To Branch Creditors (Branch creditors brought into H.O. Books)	Dr.	10,400	10,400

Branch Current Account

	Rs.		Rs.
To Balance b/d	1,33,710	By Cash in transit	3,000
To Profit & Loss A/c	31,700	By Loss of theft	1,700
To Branch Creditors	10,400	By Sundry Branch Assets	1,71,110
	1,75,810		**1,75,810**

Profit and Loss Account for 20X1

	Rs.		Rs.
To Loss by Theft	1,700	By Balance b/d	25,310
To Balance c/d	1,07,510	By Year's Profit: H.O.	52,200
		Branch	31,700
	1,09,210		**1,09,210**

Scanned with OKEN Scanner

QUESTION 29

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

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

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

From the information given below, you are required to prepare for the year ended 31st Dec.,20X1 in columnar form.

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

(b) Balance Sheet as on 31st Dec., 20X1 for the entire business.

	H.O.		Branch	
	Rs.	Rs.	Rs.	Rs.
Raw materials purchased	35,000			
Direct wages	1,08,500			
Factory overheads	39,000			
Stock on 1-1-20X1				
Raw materials	1,800			
Finished goods	13,000		9,200	
Debtors	37,000			
Cash	22,000		1,000	
Administrative Salaries	13,900		4,000	
Salesmen Salaries	22,500		6,200	
Other administrative &				
selling overheads	12,500		2,300	
Inter-unit accounts	5,000			2,000
Capital		50,000		
Sundry Creditors		13,000		
Provision for unrealized profit in stock		1,200		
Sales		2,00,000		65,200
Goods sent to Branch		46,000		
Goods received from H.O.			44,500	
	3,10,200	**3,10,200**	**67,200**	**67,200**

Notes:

(8) On 28th Dec., 20X1 the branch remitted Rs. 1,500 to the H.O. and this has not yet been recorded in the H.O. books. Also, on the same date, the H.O. dispatched goods to the branch invoiced at Rs. 1,500 and these too have not yet been entered into the branch books. It is the company's policy to adjust items in transit in the books of the recipient.

(9) The stock of raw materials held at the H.O. on 31st Dec.,20X1 was valued at Rs. 2,300.

(10) You are advised that:

- There were no stock losses incurred at the H.O. or at the branch.
- It is KP's practice to value finished goods stock at the H.O. at factory cost.
- There were no opening or closing stock of work-in-progress.

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

SOLUTION

In the books of KP

Scanned with OKEN Scanner

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

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

Balance Sheet as on 31st Dec., 20X1

	H.O.	Branch	Total		H.O.	Branch	Total
	Rs.	Rs.	Rs.		Rs.	Rs.	Rs.
Capital	50,000	-	50,000	Fixed Assets	-	-	-
Profit: H.O. 17,053 Branch 6,904	17053		23,957	Current Assets:			
				Raw material	2,300		2,300
Trade Creditors	13,000		13,000	Finished Goods (Less Stock Res.)	15,000	9,560	23,313 *
Bonus Payable		156	156	Debtors	37,000	-	37,000
H.O. Account*		3500		Cash (including transit item)	23,500	1,000	24,500
Stock Reserve (W.N.4)	1,247			Branch A/c	3500		
	88,204	**10,560**	**87,113**		**88,204**	**10,560**	**87,113**

*9,560 × 100/115 i.e., (8,313 + 15,000) = Rs.23,313

** (5,000 + 6,904) – 1500 = Rs. 10,404.

Working Notes:

(1) Material Consumed

Opening raw material + Raw Material Purchased – Closing raw material

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

(2) Closing stock at head office

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

= 34,500 + 1,08,500 + 39,000 = 1,95,000

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

= 2,00,000 – 2,00,000 x 70% = 1,40,000

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

Scanned with OKEN Scanner

(d) Closing stock=1,95,000–1,40,000–40,000=15,000

(3) **Gross profit of Branch** = Sales x Gross profit ratio
= 65,200 x 30% =19,560

(4) **Closing stock reserve** = 9,560 x 15/115 = 1,246
Charge to profit and loss=1,247–1,200=47

QUESTION 30

M & S Co. of Lucknow has a Branch in Canberra, Australia (as an integral foreign operation of M & S Co.). At the end of 31st March 2019, the following ledger balances have been extracted from the books of the Lucknow office and the Canberra.

	Lucknow office (Rs. In thousands)		Canberra Branch (Aust. Dollars in thousands)	
	Dr.	Cr.	Dr.	Cr
Capital		2,000		
Reserves & Surplus		1,000		
Land	500			
Buildings (Cost)	1,000			
Buildings Dep. Reserves		200		
Plant and Machinery (Cost)	2,500		200	
Plant and Machinery Dep. Reserves		600		130
Debtors/Creditors	280	200	60	30
Stock as on 1- 4-2018	100		20	
Branch Stock Reserve		4		
Cash & Bank Balances	10		10	
Purchases/Sales	240	520	20	123
Goods sent to Branch		100	5	
Managing Partner's Salary	30			
Wages and Salary	75		45	
Rent			12	
Office Expenses	25		18	
Commission Receipts		256		100
Branch/HO Current Account	120			7
	4,880	**4,880**	**390**	**390**

The following information is also available:

(i) Stock as at 31st March, 2019
Lucknow Rs. 1,50,000
Canberra A$ 3125 (all stock are out of purchases made at Abroad)

(ii) Head Office always sent goods to the Branch at cost plus 25%

(iii) Provision is to be made for doubtful debts at5%

(iv) Depreciation is to be provided on Buildings at 10% and on Plant and Machinery at 20% on written down value.

You are required to:

(1) Convert the Branch Trial Balance into rupees by using the following exchange rates:

Opening rate	1 A $ = Rs. 50
Closing rate	1 A $ = Rs. 53
Average rate	1 A $ = Rs. 51.00
For Fixed Assets	1 A $ = Rs. 46.00

Prepare Trading and Profit and Loss Account for the year ended 31st March 2019 showing to the extent possible H.O. results and Branch results separately.

Scanned with OKEN Scanner

SOLUTION

M & S Co. Ltd.

Canberra, Australia Branch Trial Balance As on 31st March 2019

	($ 'thousands)			(Rs.' thousands)	
	Dr.	**Cr.**	**Conversion rate per $**	**Dr.**	**Cr.**
Plant & Machinery (cost)	200		Rs. 46	9,200	
Plant & Machinery Dep. Reserve		130	Rs. 46		5,980
Trade receivable/payable	60	30	Rs. 53	3,180	1,590
Stock (1.4.2018)	20		Rs. 50	1,000	
Cash & Bank Balances	10		Rs. 53	530	
Purchase / Sales	20	123	Rs. 51	1,020	6,273
Goods received from H.O.	5		Actual	100	
Wages & Salaries	45		Rs. 51	2,295	
Rent	12		Rs. 51	612	
Office expenses	18		Rs. 51	918	
Commission Receipts		100	Rs. 51		5,100
H.O. Current A/c		7	Actual		120
				18,855	**19,063**
Foreign Exchange Loss (bal. fig.)				208	
	390	**390**		**19,063**	**19,063**
Closing stock	**3.125**		**53**	**165.625**	

Trading and Profit & Loss Account for the year ended 31st March, 2019

				(Rs.'000)					
		H.O.	**Branch**	**Total**			**H.O.**	**Branch**	**Total**
To	Opening Stock	100	1,000.000	1,100.000	By	Sales	520	6,273.000	6,793.000
To	Purchases	240	1,020.000	1,260.000	By	Goods sent to Branch	100	–	100.000
To	Goods received from Head Office	–	100.000	100.000	By	Closing Stock	150	165.625	315.625
To	Wages & Salaries	75	2,295.000	2,370.000					
To	Gross profit c/d	355	2,023.625	2,378.625					
		770	**6,438.625**	**7,208.625**			**770**	**6,438.625**	**7,208.625**
To	Rent	–	612.000	612.000	By	Gross profit b/d	355	2,023.625	2,378.625
To	Office expenses	25	918.000	943.000	By	Commission receipts	256	5,100.000	5,356.000
To	Provision for doubtful debts @ 5%	14	159.000	173.000					
To	Depreciation (W. N.)	460	644.000	1,104.000					
To	Balance c/d	112	4,790.625	4,902.625					
		611	**7,123.625**	**7,734.625**			**611**	**7,123.625**	**7,734.625**
To	Managing Partner's Salary			30.000	By	Balance b/d			4,902.625
To	Exchange Loss			208.000	By	Branch stock reserve			4.000
To	Balance c/d			4,668.625					
				4,906.625					**4,906.625**

Scanned with OKEN Scanner

Working Note:

Calculation of Depreciation

	H.O Rs. '000	Branch Rs. '000
Building – Cost	1,000	
Less: Dep. Reserve	(200)	
	800	
Depreciation @ 10% (A)	80	
Plant & Machinery Cost	2,500	9,200
Less: Dep. Reserve	(600)	(5,980)
	1,900	3,220
Depreciation @ 20% (B)	380	644
Total Depreciation (A+B)	**460**	**644**

Note: As the closing stock of Branch does not consist any stock transferred from M&S Co., there is no need to create closing stock reserve. But the opening branch stock reserve has to be reversed in the P&LA/c.

Scanned with OKEN Scanner

5. FINANCIAL STATEMENTS

QUESTION 31

The Balance Sheet of Appropriate Ltd. as at 31st March, 2016 is as follows:

	Note No.	31st March, 2020	31st March, 2019
EQUITY & LIABILITIES			
Share Capital	1		
Reserves and Surplus	2		
Employee Stock Option Outstanding	3		
Share Application Money Refundable	4		
Non-Current Liabilities			
Deferred Tax Liabilities (Arising from Indian Income Tax)	5		
Current Liabilities			
Trade Payable			
Total	6		
ASSETS			
Non-Current Assets			
PPE – Tangible	7		
Capital Work in Progress – (Including Capital Advance)	8		
Current Assets			
Trade Receivables			
Deferred Tax Assets (Arising from Income Tax)	9		
Profit and Loss (Debit Balance)	10		
Total			

Comment on the presentation in terms of Schedule III to the Companies Act, 2013 notified by the Central Government.

SOLUTION

Following Observations are considered from the given Balance Sheet Presentation: -

1) Under Equity & Liabilities side, First head is "Shareholders Fund" which is not mentioned on the face of Balance Sheet.
2) "Employee Stock Option Outstanding" is being wrongly shown on the face of Balance Sheet. It should be shown under the head "Reserves & Surplus" as a separate line item in Notes.
3) Share Application money refundable should be shown under Other Current Liabilities in the Notes.
4) Share Application money Pending Allotment head is missing on the Face of Balance Sheet
5) Capital Advance should be shown under "Long term Loans & Advances" in Non-Current Assets & Not as Capital Work in progress.
6) DTA shall be shown under Non-Current Assets Instead on Current Assets.
7) Dr. Balance of P&L A/c shall be shown separately as Negative figure under Reserves and not Asset side.

Correct Presentation in Balance Sheet (as per Schedule III)

Particulars	Note. No.	CY (Rs.)	PY (Rs.)
Equity &b Lability			
1) Shareholder's Fund			
a) Share capital			
b) Reserves & Surplus	1		
2) Share application money pending allotment			
3) Non-Current Liabilities			

Scanned with OKEN Scanner

Deferred Tax Liability			
4) Current Liabilities			
Trades Payables			
Other Current Liabilities	2		
Assets			
1) Non-Current Assets			
a) PPE			
(i) Tangible Assets			
(ii) Capital Work in Progress			
b) Deferred Tax Assets			
c) Long term Loans & Advances	3		
2) Current Assets			
Trade Receivables			

Notes to Accounts: -

1) Reserves & Surplus	
a) ESOP Outstanding	
b) Dr. Balance of P&L A/c	
2) Other Current Liabilities	
a) Share application money refundable	
3) Long term loans & advances	
a) Capital Advances	

QUESTION 32

You are required to prepare a Statement of Profit and Loss and Balance Sheet from the following Trial Balance extracted from the books of the International Hotels Ltd., on 31st March, 20X2:

	Dr.	Cr.
	Rs	Rs
Authorised Capital-divided into 5,000 6% Preference Shares of Rs 100 each and 10,000 equity Shares of Rs 100 each		15,00,000
Subscribed Capital -		
5,000 6% Preference Shares of Rs 100 each		5,00,000
Equity Capital		8,05,000
Purchases - Wines, Cigarettes, Cigars, etc.	45,800	
- Foodstuffs	36,200	
Wages and Salaries	28,300	
Rent, Rates and Taxes	8,900	
Laundry	750	
Sales - Wines, Cigarettes, Cigars, etc.		68,400
- Food		57,600
Coal and Firewood	3,290	
Carriage and Cooliage	810	
Sundry Expenses	5,840	
Advertising	8,360	
Repairs	4,250	
Rent of Rooms		48,000
Billiard		5,700
Miscellaneous Receipts		2,800
Discount received		3,300
Transfer fees		700
Freehold Land and Building	8,50,000	

Scanned with OKEN Scanner

Furniture and Fittings	86,300	
Inventory on hand, 1st April, 20X1		
Wines, Cigarettes. Cigars, etc.	12,800	
Foodstuffs	5,260	
Cash in hand	2,200	
Cash with Bankers	76,380	
Preliminary and formation expenses	8,000	
2,000 Debentures of Rs 100 each (6%)		2,00,000
Profit and Loss Account		41,500
Trade payables		42,000
Trade receivables	19,260	
Investments	2,72,300	
Goodwill at cost	5,00,000	
General Reserve		2,00,000
	19,75,000	**19,75,000**
Wages and Salaries Outstanding	1,280	
Inventory on 31st March, 20X2		
Wines, Cigarettes and Cigars, etc.	22,500	
Foodstuffs	16,400	

Depreciation: Furniture and Fittings @ 5% p.a.: Land and Building @ 2% p.a.

The Equity capital on 1st April, 20X1 stood at Rs 7,20,000, that is 6,000 shares fully paid and 2,000 shares Rs 60 paid. The directors made a call of Rs 40 per share on 1st October 20X1. A shareholder could not pay the call on 100 shares and his shares were then forfeited and reissued @ Rs 90 per share as fully paid. The Directors declare a dividend of 8% on equity shares, transferring any amount that may be required from General Reserve. Ignore Taxation.

SOLUTION

Statement of Profit and Loss of International Hotels Ltd.
for the year ended 31st March, 20X2

	Particulars	Notes	Amount
I.	Revenue from operations	9	1,79,700
II.	Other income	10	6,800
III.	**Total Revenue (I + II)**		**1,86,500**
IV.	Expenses:		
	Cost of materials consumed	11	25,060
	Purchases of Inventory-in-Trade	12	45,800
	Changes in inventories of finished goods work-in-progress and Inventory-in-Trade	13	(9,700)
	Employee benefits expense	14	29,580
	Other operating expenses	15	18,000
	Selling and administrative expenses	16	14,200
	Finance costs	17	12,000
	Depreciation and amortisation expense	18	21,315
	Other expense (preliminary expenses written off)		8,000
	Total expenses		**1,64,255**
V.	**Profit (Loss) for the period (III - IV)**		**22,245**

Balance Sheet of International Hotels Ltd. as on 31st March, 20X2

Particulars			Note No	Rs
EQUITY AND LIABILITIES				
1	**Shareholders' funds**			
	a	Share capital	1	13,00,000

Scanned with OKEN Scanner

	b	Reserves and Surplus		2	2,68,745
2	Non-current liabilities				
	a	Long-term borrowings		3	2,00,000
3	Current liabilities				
	a	Trade Receivables		4	42,000
	b	Other current liabilities		5	13,280
			Total		**18,24,025**
ASSETS					
1	Non-current assets				
	a	PPE			
		I	Tangible assets	6	9,14,985
		II	Intangible assets (Goodwill)		5,00,000
	B	Non-current investments			2,72,300
2	Current assets				
	A	Inventories		7	38,900
	B	Trade receivables			19,260
	C	Cash and bank balances		8	78,580
			Total		**18,24,025**

Notes to accounts

			Rs
1	**Share Capital**		
	Equity share capital		
	Authorised		
	10,000 Equity shares of Rs 100 each		10,00,000
	Issued & subscribed		
	8,000 Equity Shares of Rs 100 each		8,00,000
	Preference share capital		
	Authorised		
	5,000 6% Preference shares of Rs 100 each		5,00,000
	Issued & subscribed		
	5,000 6% Preference shares of Rs 100 each		5,00,000
	Total		**13,00,000**
2	**Reserves and Surplus**		
	Capital reserve [100 x (90 – 40)]		5,000
	General reserve	2,00,000	
	Less: Amount used to pay dividend	(30,255)	1,69,745
	Surplus (Profit & Loss A/c)	22,245	
	Add: Balance from previous year	41,500	
			63,745
	Total		**2,68,745**
3	**Long-term borrowings**		
	Secured		
	6% Debentures		2,00,000
	Total		**2,00,000**
4	**Trade Receivables**		42,000
5	**Other current liabilities**		
	Wages and Salaries Outstanding	1,280	
	Interest on debentures dividend Receivable	12,000	13,280
	Total		**13,280**
6	**Tangible assets**		
	Freehold land & Buildings	8,50,000	

Scanned with OKEN Scanner

	Less: Depreciation	(17,000)	8,33,000
	Furniture and Fittings	86,300	
	Less: Depreciation	(4,315)	81,985
	Total		**9,14,985**
7	**Inventories**		
	Wines, Cigarettes & Cigars, etc.		22,500
	Foodstuffs		16,400
	Total		**38,900**
8	**Cash and cash equivalents**		
	Cash at bank		76,380
	Cash in hand Other bank balances		2,200 Nil
	Total		**78,580**
9	**Revenue from operations**		
	Sale of products		
	Wines, Cigarettes, Cigars etc.	68,400	
	Food	57,600	1,26,000
	Sale of services		
	Room Rent	48,000	
	Billiards	5,700	53,700
	Total		**1,79,700**
10	**Other income**		
	Transfer fees	700	
	Miscellaneous Receipts	2,800	
	Discount received	3,300	
	Total		**6,800**
11	**Cost of materials consumed**		
	Opening Inventory	5,260	
	Add: Purchases during the year	36,200	
	Less: Closing Inventory	(16,400)	25,060
	Total		**25,060**
12	**Purchases of Inventory-in-Trade**		
	Wines, Cigarettes etc.		45,800
	Total		**45,800**
13	**Changes in inventories of finished goods work-in-progress and Inventory-in-Trade**		
	Wines, Cigarettes etc.		
	Opening Inventory	12,800	
	Less: Closing Inventory	(22,500)	(9,700)
	Total		**(9,700)**
14	**Employee benefits expense**		
	Wages and Salaries	28,300	
	Add: Wages and Salaries Outstanding	1,280	29,580
	Total		**29,580**
15	**Other operating expenses**		
	Rent, Rates and Taxes		8,900
	Coal and Firewood		3,290
	Laundry		750
	Carriage and Cooliage		810
	Repairs		4,250
	Total		**18,000**
16	**Selling and administrative expenses**		

Scanned with OKEN Scanner

	Advertising		8,360
	Sundry Expenses		5,840
	Total		**14,200**
17	**Finance costs**		
	Interest on Debentures (2,00,000 x 6%)	12,000	
	Total		**12,000**
18	**Depreciation and amortisation expense**		
	Land and Buildings (8,50,000 x 2%)	17,000	
	Furniture & Fittings (86,300 x 5%)	4,315	
	Total		**21,315**

QUESTION 33

On 31st March, 20X1, SR Ltd. provides the following ledger balances after preparing its Profit & Loss Account for the year ended 31st March, 20X1.

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

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

1) 50,000 fully paid equity shares were allotted as consideration for land.
2) The cost of assets were:

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

3) Trade Receivables for Rs. 4,86,000 due for more than 6 months.
4) Balances with banks include Rs. 56,000, the Naya bank, which is not a scheduled bank.
5) Loan from Public Finance Corporation repayable after 3 years.
6) The balance of Rs. 26,30,000 in the loan account with Public Finance Corporation is inclusive of Rs.1,34,000 for interest accrued but not due. The loan is secured by hypothecation of land.

Scanned with OKEN Scanner

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

Loan taken from Nixes Bank	Rs. 13,80,000
(Amount repayable within one year)	(Rs. 4,80,000)
Loan taken from Directors	Rs. 8,50,000

8) Bills Receivable for Rs. 1,60,000 maturing on 15th June, 20X1 has been discounted.

9) Short term borrowings includes:

Loan from Naya bank	Rs. 1,16,000 (Secured)
Loan from directors	Rs. 48,000

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

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

You are required to prepare the Balance Sheet of the Company as on March 31st 20X1 as required under Part - I of Schedule III of the Companies Act, 2013.

You are not required to give previous year figures

SOLUTION

SR Ltd.

Balance Sheet as at 31st March, 20X1

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

Notes to accounts

1.	**Share Capital**		
	Equity share capital		
	Issued, subscribed and called up		
	1,60,000 Equity Shares of Rs. 50 each (Out of the above 50,000 shares have been issued for consideration other than cash)	80,00,000	
	Less: Calls in arrears	(15,000)	79,85,000
2.	**Reserves and Surplus**		
	General Reserve	9,41,000	

Scanned with OKEN Scanner

	Add: Transferred from Profit and loss account	35,000	9,76,000
	Securities premium		15,00,000
	Surplus (Profit & Loss A/c)	5,80,000	
	Less: Appropriation to General Reserve (proposed)	(35,000)	5,45,000
			30,21,000
3.	**Long-term borrowings**		
	Secured: Term Loans		
	Loan from Public Finance Corporation [Receivable after 3 years (Rs. 26,30,000 - Rs. 1,34,000 for interest accrued but not due)] (secured by hypothecation of land)		24,96,000
	Unsecured		
	Bank Loan (Nixes bank)	9,00,000	
	(Rs. 13,80,000 - Rs. 4,80,000 Receivable within 1 year)		
	Loan from Directors	8,50,000	
	Others	20,000	17,70,000
	Total		**42,66,000**
4.	**Short-term borrowings**		
	Loan from Naya bank (Secured)	1,16,000	
	Loan from Directors	48,000	
	Loan from Nixes bank Receivable within one year	4,80,000	
	Others	2,96,000	
			9,40,000
5.	**Other current liabilities**		
	Unpaid dividend	70,000	
	Interest accrued but not due on borrowings	1,34,000	
			6,84,000
6.	**Short-term provisions**		
	Provision for taxation		3,80,000
7.	**PPE**		
	Land		25,00,000
	Buildings	32,00,000	
	Less: Depreciation	(2,00,000)	30,00,000
	Plant & Machinery	30,00,000	
	Less: Depreciation	(6,00,000)	24,00,000
	Furniture & Fittings	16,50,000	
	Less: Depreciation	(3,50,000)	13,00,000
	Total		**92,00,000**
8.	**Inventories**		
	Raw Material	13,00,000	
	Finished goods	40,00,000	
	Loose tools	5,00,000	58,00,000
9.	**Trade receivables**		
	Outstanding for a period exceeding six months		4,86,000
	Others		12,64,000
	Total		**17,50,000**
10.	**Cash and cash equivalents**		
	Balances with banks		
	with Scheduled Banks	3,58,000	
	with others banks	56,000	4,14,000
	Cash in hand		70,000
	Total		**4,84,000**

Scanned with OKEN Scanner

Note: There is a contingent liability amounting to Rs. 1,60,000

QUESTION 34

The following is the Trial Balance of H Ltd., as on 31st March, 2021:

	Dr.	Cr.
Equity Capital (Shares of Rs. 100 each)		8,05,000
5,000, 6% preference shares of Rs. 100 each		5,00,000
9% Debentures		4,00,000
General Reserve		40,00,000
Profit & Loss A/c (of previous year)		72,000
Sales		60,00,000
Trade Payables		10,40,000
Provision for Depreciation on Plant & Machinery		1,72,000
Suspense Account		40,000
Land at cost	24,00,000	
Plant & Machinery at cost	7,70,000	
Trade Receivables	19,60,000	
Inventories (31-03-2021)	9,50,000	
Bank	2,30,900	
Adjusted Purchases	22,32,100	
Factory Expenses	15,00,000	
Administration Expenses	3,00,000	
Selling Expenses	14,00,000	
Debenture Interest	36,000	
Goodwill	12,50,000	
	1,30,29,000	**1,30,29,000**

Additional Information:

(i) The authorised share capital of the company is:

	Rs.
5,000, 6% preference shares of Rs. 100 each	5,00,000
10,000, equity shares of Rs. 100 each	10,00,000

Issued equity capital as on 1st April 2020 stood at Rs. 7,20,000, that is 6,000 shares fully paid and 2,000 shares of Rs. 60 paid. The directors made a call of Rs. 40 per share on 1st October 2020. A shareholder could not pay the call on 100 shares and his shares were then forfeited and reissued @ Rs. 90 per share as fully paid.

(ii) On 31st March 2021, the Directors declared a dividend of 5% on equity shares, transferring any amount that may be required from General Reserve. Ignore Taxation.

(iii) The company on the advice of independent valuer wishes to revalue the land at Rs. 36,00,000.

*This should have been given as 31.3.2021.

(iv) Suspense account of Rs. 40,000 represents amount received for the sale of some of the machinery on 1-4-2020. The cost of the machinery was Rs. 1,00,000 and the accumulated depreciation thereon being Rs. 30,000.

(v) Depreciation is to be provided on plant and machinery at 10% on cost.

(vi) Amortize 1/5th of Goodwill.

You are required to prepare H Limited's Balance Sheet as on 31-3-2021 and Statement of Profit and Loss with notes to accounts for the year ended 31-3-2021 as per Schedule III of the Companies Act, 2013. Ignore previous years' figures & taxation.

SOLUTION

Balance Sheet as at 31st March 2021

Particulars	Note No	Amount in Rs.
Equity and Liabilities		
I. Shareholders' Funds		

Scanned with OKEN Scanner

	a. Share Capital	1	13,00,000
	b. Reserves and Surplus	2	53,91,900
II.	**Non-Current Liabilities**		
	a. Long Term Borrowings	3	4,00,000
III.	**Current Liabilities**		
	a. Trade Payables	4	10,40,000
	b. Other Current Liabilities	5	70,000
	Total		**82,01,900**
Assets			
I.	**Non-Current Assets**		
	a. Property, Plant and Equipment	6	40,61,000
	b. Intangible Assets	7	10,00,000
II.	**Current Assets**		
	a. Inventories		9,50,000
	b. Trade Receivables		19,60,000
	c. Cash and Cash equivalents		2,30,900
	Total		**82,01,900**

Statement of Profit and Loss for the year ended 31st March 2021

	Particulars	Note No	Amount in Rs.
I.	Revenue from operations		60,00,000
	Total Revenue		60,00,000
II.	**Expenses**		
	Purchases (adjusted)		22,32,100
	Finance Costs	8	36,000
	Depreciation and Amortization	9	3,17,000
	Other Expenses	10	32,30,000
	Total Expenses		58,15,100
III.	**Profit/(Loss) for the period**		**1,84,900**

Notes to Accounts **(Amount in Rs.)**

1	**Share Capital**		
	a. Authorized Capital		
	5,000, 6% Preference shares of Rs. 100/- each		5,00,000
	10,000 Equity Shares of Rs. 100/- each		10,00,000
			15,00,000
	b. Issued & Subscribed Capital		
	5,000, 6% Preference shares of Rs. 100/- each		5,00,000
	8,000, Equity shares of Rs. 100/- each		8,00,000
	Total		**13,00,000**
2	**Reserves & Surplus**		
	Capital Reserve (100 X (90-40))		5,000
	Revaluation Reserve (36,00,000-24,00,000)		12,00,000
	General Reserve		40,00,000
	Surplus	1,84,900	
	Add: Balance from previous year	72,000	
	Less: Dividends declared	(70,000)	
	Profit/(Loss) carried forward to Balance Sheet		1,86,900

Scanned with OKEN Scanner

	Total		**53,91,900**
3	**Long-Term Borrowings**		
	Secured		
	9% Debentures		4,00,000
4	**Trade Payables**		**10,40,000**
5	**Other Current Liabilities**		
	Dividend Payable		
	Preference Dividend		30,000
	Equity Dividend		40,000
	Total		**70,000**
6	**Property, Plant and Equipment**		
	Land		
	Opening balance		24,00,000
	Add: Revaluation Adjustment		12,00,000
	Closing Balance		36,00,000
	Plant and Machinery		
	Opening Balance		7,70,000
	Less: Disposed off		(1,00,000)
	Depreciation		(2,09,000)
	Closing Balance		4,61,000
	Total		**40,61,000**
7	**Intangible Assets**		
	Goodwill		12,50,000
	Less: Amortized (1/5th)		(2,50,000)
	Total		10,00,000
8	**Finance Costs**		
	Debenture Interest		36,000
9	**Depreciation and Amortization**		
	Plant and Machinery		67,000
	Goodwill		2,50,000
	Total		**3,17,000**
10	**Other Expenses**		
	Factory Expenses		15,00,000
	Selling Expenses		14,00,000
	Administrative Expenses		3,00,000
	Loss on sale of Plant and Machinery		
	Book Value (1,00,000-30,000)	70,000	
	Less: Sale Value	(40,000)	30,000
	Total		**32,30,000**

Note:

1. The inventories (31.3.20) amounting Rs. 9,50,000 (given in the trial balance of the question) should have been as closing inventory i.e., as on 31.3.21. In the above solution, this inventory has been considered as closing inventory i.e., for 31.3.21. If this is considered as inventory of 31.3.20, the closing inventory (as on 31.3.21) will not be available for the balance sheet as on 31.3.21 and in that case, the balance sheet will not tally without using suspense account amounting Rs. 9,50,000.

Scanned with OKEN Scanner

2. The financial statements given in the above answer include adjustment for dividend declared on 31st March, 2021, strictly, as per the information given in the question. However, practically dividends are declared in the annual general meetings which take place after the reporting date.

UYBACK

QUESTION 35

The following is the Trial Balance of Holding Ltd., as on 31st March, 20X2:

PARTICULARS	DR.	CR.
Equity Share Capital	-	16,25,000
3000, 9% Cumulative Pref. Share Capital	-	3,00,000
10% Debentures	-	4,80,000
Security Premium	-	1,55,000
General Reserves	-	15,00,000
Profit and Loss A/c (PY)	-	1,50,000
Sales	-	90,00,000
Trade Payables	-	11,50,000
Provision for Depreciation on P&M	-	3,50,000
Suspense A/c	-	1,40,000
Land at Cost	40,00,000	-
Plant and Machine at Cost	12,50,000	-
Sundry Debtors	15,00,000	-
Bills Receivables	4,00,000	-
Inventories Closing (Stock in Trade)	7,50,000	-
Bank Balance	4,30,000	-
Adjusted Purchase of Stock in Trade	21,30,000	-
Factory Expenses	12,00,000	-
Administration Exp	4,00,000	-
Selling Exp	9,00,000	-
Debenture Interest Paid till 30th Sep	35,000	-
Goodwill	10,00,000	-
Interim Dividend Paid	90,000	-
Bad Debts	45,000	-
Provision for Doubtful Debts	-	67,000
Directors Fees	51,000	
Loose Tools	25,000	
Consumables	18,000	
Unclaimed Dividend of Last Year	-	12,000
Long Term Investments (7.5%)	16,00,000	-
Interest received on above Investments	-	90,000
Preliminary Expenses	40,000	-
Opening Raw Material	2,10,000	-
Purchase of Raw Material	8,10,000	-
Long Term Loan from Bank	-	13,20,000
Long Term Laon from Other Parties	-	3,00,000
Short Term Loan from Bank	-	5,00,000
Govt. Grant Received (Revenue Nature)	-	1,75,000
Managerial Remuneration Paid	1,00,000	-
Income Tax Paid	9,50,000	-
Provision for Income Tax (as on 1/04/20X1)	-	5,20,000
Deferred Tax Liability	-	1,00,000

Scanned with OKEN Scanner

	1,79,34,000	1,79,34,000

Additional Information:

1. The authorised share capital of the company is:
   3,000, 9% preference shares of Rs. 100 each 3,00,000
   20,000, Equity shares of Rs. 100 each 20,00,000
2. Issued equity capital as on 1st April 20X1 stood at Rs. 14,40,000, that is 12,000 shares fully paid and 4,000 shares of Rs. 60 paid. The directors made a call of Rs. 40 per share on 1st October. A shareholder could not pay the call on 500 shares and his shares were then forfeited and reissued @ Rs. 90 per share as fully paid.
3. On 31st March 20X2, the Directors declared a dividend of 12% on equity shares, transferring any amount that may be required from General Reserve.
4. The company on the advice of independent valuer wishes to revalue the land by 10%
5. Suspense account of Rs. 1,40,000 represents amount received for the sale of some of the machinery on 1-4-20X1. The cost of the machinery was Rs. 3,00,000 and the accumulated depreciation thereon being Rs. 1,80,000.
6. Depreciation is to be provided on plant and machinery at 10% on diminishing balance.
7. Amortize 1/5th of Goodwill.
8. Rs. 2,00,000 of Debentures were redeemed on 1st Oct at 10% Premium but premium amount not yet debited to Security Premium A/c. Full Amount wrongly debited to Debentures A/c.
9. Maintain a Provision of 7% on Debtors as on 31st March 20X2.
10. Provision for Income Tax as on 31st March should be Rs. 8,00,000
11. Closing Raw Material is Rs. 2,45,000
12. Adjusted Purchase of Stock in Trade includes 16,000 distributed among valued customers
13. Long Term loan from Bank includes Interest Accrued but not due Rs. 50,000 and Rs. 1,20,000 To be payable within 1 Year.
14. Bills receivables discounted not yet matured Rs. 15,000
15. Outstanding expenses Rs. 21,000
16. Transfer 20% of NPAT to General Reserve.

You are required to prepare Holding Limited's Balance Sheet as on 31-3-20X2 and Statement of Profit and Loss with notes to accounts for the year ended 31-3-20X2 as per Schedule III of the Companies Act, 2013.

Solution:

Holding Ltd

Balance Sheet as on 31/03/X2

Particulars	Note no	Amount
Equity & Liabilities		
1) Shareholder's Fund		
(i)Share capital	1	19,00,000
(ii) Reserve & Surplus	2	39,30,000
2) Non-current liabilities		
(i)Long term Borrowings	3	19,50,000
(ii) DTL	-	1,00,000
3)Current liabilities		
i)Short term borrowings	4	6,20,000
ii)Trade payables	-	11,50,000
iii)Other current liabilities	5	3,27,000
iv)Short term provisions	6	8,00,000
Total		**1,07,77,000**
ASSETS		
Non-current assets		
(i)PPE	7	51,02,000
(ii)Intangible asset	8	8,00,000
(iii)Non-current investment	9	16,00,000

Scanned with OKEN Scanner

Currents Assets		
(i)Inventories	10	10,20,000
(ii)Trade Receivable	11	17,95,000
(iii)Cash & Cash eq.	12	4,30,000
(iv) Other current asset	13	30,000
Total		**1,07,77,000**

Statement of profit & loss A/C for the year ended 31/03/×2

Particular	Note no.	Amount
Incomes		
1)Revenue From operation	14	90,00,000
2)Other Incomes	15	3,15,000
Total Incomes (a)		**93,15,000**
Expenditures		
1)Cost of Material consumed	16	7,75,000
2)Purchase of SIT	17	21,14,000
3)Finance cost	18	60,000
4)Depreciation & Amortization	19	2,78,000
5)Other expenses	20	28,29,000
Total Expenditure (b)		**60,56,000**
Net-profit before tax (a-B)		32,59,000
(-)Tax expense (WN-1) (Current tax liabilities)		(12,30,000)
Net profit after tax (Transfer to R&S)		20,29,000

Note to accounts:

1) Share Capital	
(a)Authorised Capital	
9% PSC of 100/-(3,000 no)	3,00,000
Equity share of 100/-(20,000 no)	20,00,000
	23,00,000
(b)Issued/Subscribed/paid-up	
9% Cumulative PSC of 100/-	3,00,000
Equity share capital of 100/- (16000 no)	16,00,000
	19,00,000

2) Reserves & surplus		
a) Capital Reserve		25,000
b) Revaluation reserve		4,00,000
c) Security premium (-) Premium On redeem	1,55,000 (20,000)	1,35,000
d) Gen Reserves opening (+) Transfer From P&L	15,00,000 4,05,800	19,05,800
e) Profit & loss a/c Opening balance (+) NPAT (-) Transfer to GR 20% (-) Interim Dividend (-) Preference Dividend (-) Equity Dividend	 1,50,000 20,29,000 (4,05,800) (90,000) (27,000) (1,92,000)	14,64,200
Total		**39,30,000**

Scanned with OKEN Scanner

3) Long Term Borrowings	
(i) 10% Debentures (4,80,000 + 20,000)	5,00,000
ii) Loan from bank (13,20,000 – 50,000 – 1,20,000)	11,50,000
iii) Loan frame other	3,00,000
Total	**19,50,000**

4) Short term Borrowing	
Loans frame bank: -	
a) Short-term loan	5,00,000
b) Current maturity of LT	1,20,000
Total	**6,20,000**

5) Other current liabilities		
i) Unclaimed Div. of LY		12,000
ii) Dividend payable		2,19,000
Preference	27,000	
Equity	1,92,000	
iii) Interest payable		75,000
Debentures interest	25,000	
Interest on Bank loan	50,000	
iv) O/S expenses		21,000
Total		**3,27,000**

6) Short term provision	
Current tax liabilities (provision)	8,00,000

7) Property Plant and Equity			
Particulars	**Gross value**	**Prov. for Dep**	**Net value**
a) Land	40,00,000	-	40,00,000
(+) Revaluation	4,00,000	-	4,00,000
	44,00,000	-	44,00,000
b) P&M	12,50,000	3,50,000	9,00,000
(-) Sale	(300000)	(1,80,000)	(1,20,000)
(+/-) Depreciation	-	78,000	(78,000)
	95,000	**2,48,000**	**51,02,000**

8) INTANGIBLE ASSETS			
	Gross	Amortisation	Net
Goodwill	10,00,000	2,00,000	8,00,000

9) Non Current Investments	
7.5% investment	16,00,000

10) Inventories	
a) Raw material	24,500
B) Stock in trade	7,50,000
c) Loose Tools	25,000
Total	10,20,000

Scanned with OKEN Scanner

11) Trade Receivables		
a) Debtors Bal Grass	15,00,000	
(-) Prov for DD @7% (Increase in provision by (10,5000 – 6,7000) = 38,000	(1,05,000)	13,95,000
b) Bills receivable		4,00,000
		17,95,000

12) Cash & Cash equivalents	
Bank Balance	4,30,000

13) Other Current Assets	
a) Interest accrued as investment 16,00,000× 7.5% = 1,20,000 (-) Int. receive = (90,000)	30,000

14) Revenue from operation	
Sales	90,00,000

15) Other Interest	
Gain of sale of machine	20,000
Govt. Grant	1,75,000
Int. on Investment (90,000 + 30,000)	1,20,000
Total	**3,15,000**

16) Cost of material consumed	
Opening RM	2,10,000
(+) Purchase of RM	8,10,000
(-) Closing RM	(2,45,000)
Total	**7,75,000**

17) Purchase of Stock in Trade	
Total adjusted purchase	21,30,000
(-) goods given for sample	(16,000)
Total	**21,14,000**

18) Finance cost	
Debentures Interest (35+25)	**60,000**

19) Depreciation & Amortisation	
a) Depreciation as PPE	78,000
b) Amortisation on goodwill	2,00,000
Total	**2,78,000**

20) Other Expense	
Factory Expense	12,00,000
Administration Expense	4,00,000
Selling Expense	9,00,000
Bad debts	45,000
Consumables	18,000
Preliminary Expense	40,000

Scanned with OKEN Scanner

Managerial remuneration	1,00,000
Director fees	51,000
Other Misc. Expense	21,000
Provision for DD	38,000
Advertisement Expense	16,000
Total	**28,29,000**

21) Contingent liabilities

Bills discounted for Rs 15,000 but still not yet matured.

Working Note 1

Prov for tax a/c			
To IT paid	9,50,000	By balance b/d	5,20,000
To Bal c/d	8,00,000	By P&L a/c	12,30,000

Scanned with OKEN Scanner

6. BUYBACK OF SECURITIES

QUESTION 36

Mukti Ltd. (a non-listed company) provide the following information as on 31.3.2020:

	(Rs.)
Land and Building	21,50,000
Plant & Machinery	15,00,000
Non- current Investment	2,00,000
Trade Receivables	5,50,000
Inventories	1,80,000
Cash and Cash Equivalents	40,000
Share capital:1,00,000 Equity Shares of Rs. 10 each fully paid up	10,00,000
Securities Premium	3,00,000
General Reserve	2,50,000
Profit & Loss Account (Surplus)	1,50,000
10% Debentures (Secured by floating charge on all assets)	20,00,000
Unsecured Loans	8,00,000
Tarde Payables	1,20,000

On 21st April, 2020 the Company announced the buyback of 15,000 of its equity shares @ Rs. 15 per share. For this purpose, it sold all its investment for Rs. 2.50 lakhs. On 25th April, 2020, the company achieved the target of buy back. On 1st May, 2020 the company issued one fully paid-up share of Rs. 10 each by way of bonus for every eight equity shares held by the equity shareholders.

You are required to pass necessary Journal Entries for the above transactions.

SOLUTION:

In the books of Vriddhi Infra Ltd.

Journal Entries

Date	Particulars		Dr.	Cr.
April 21	Bank Account	Dr.	2,50,000	
	To Investment Account			2,00,000
	To Profit and Loss Account			50,000
	(Being investment sold on profit)			
April 25	Equity Share capital account	Dr.	1,50,000	
	Securities premium A/c	Dr.	75,000	
	To Equity shares buy back Account			2,25,000
	(Being the amount due to equity shareholders on buy back)			
	Equity shares buy back A/c	Dr.	2,25,000	
	To bank A/c			2,25,000
	(Being the payment made on account of buyback of 15,000 Equity Shares)			
	General reserve A/c	Dr.	1,50,000	
	To Capital redemption reserve A/c			1,50,000
	(Being amount equal to nominal value of bought back shares from free reserves transferred to capital redemption reserve account as per the law)			
May 1	Capital redemption reserve A/c	Dr.	1,06,250	
	To Bonus shares A/c (W.N.1)			1,06,250
	(Being the utilization of capital redemption reserve to issue bonus shares)			
	Bonus shares A/c	Dr.	1,06,250	
	To Equity share capital A/c			1,06,250
	(Being issue of one bonus equity share for every ten equity shares held)			

Scanned with OKEN Scanner

Working Note:

Amount of bonus shares = {(1,00,000 – 15,000) X 1/8} X 10
= Rs. 1,06,250

QUESTION 37

VIJ Ltd. has the following Capital Structure as on 31st March, 2022:

Particulars		(₹ in Lakhs)
Equity Share Capital (Shares of ₹ 10 each, fully Paid)		990
Reserves & Surplus:		
General Reserve	720	
Securities Premium Account	270	
Profit & Loss Account	270	
Infrastructure development Reserve	540	1,800
Loan Funds		5,400

On the recommendation of the Board of Directors, the shareholders of the company have approved on 2nd September, 2022 a proposal to buy-back the maximum permissible number of equity shares, considering the sufficient funds available at the disposal of the company.

The current market value of the company's shares is ₹ 25 per share and in order to induce the existing shareholders to offer their shares for buy-back, it was decided to offer a price of 20% over market rate.

You are also informed that the Infrastructure Development Reserve is created to satisfy income tax requirements.

You are required to compute the maximum permissible number of equity shares that can be brought back in the light of the above information and also under a situation where the loan funds of the company were either ₹ 3,600 lakh or ₹ 4,500 lakh.

The entire buy-back is completed by 09/12/2022, show the accounting entries with full narration in the company's books in each situation.

SOLUTION:

Statement determining the maximum number of shares to be bought back

(Number of shares)

Particulars	When loan fund is		
	₹ 5,400 lakhs	**₹3,600 lakhs**	**₹4,500 lakhs**
Shares Outstanding Test (W.N.1)	24.75	24.75	24.75
Resources Test (W.N.2)	18.75	18.75	18.75
Debt Equity Ratio Test (W.N.3)	Nil	11.25	Nil
Maximum number of shares that can be bought back [least of the above]	**Nil**	**11.25**	**Nil**

Journal Entries for the Buy-Back
(applicable only when loan fund is ₹ 3,600 lakhs)

₹ in lakhs

	Particulars		Debit	Credit
(a)	Equity share capital account	Dr.	112.50	
	To Equity share buy- back account	Dr.	225.00	
	(Being cancellation of shares bought back)			337.5
(b)	Equity share buy-back account	Dr.	337.50	
	To Bank account			337.5
	(Being buy-back of 11.25 lakhs equity shares of ₹10 each @ ₹30 per share)			
(c)	General reserve account	Dr.	112.50	
	To Capital redemption reserve account			112.50

Scanned with OKEN Scanner

	(Being transfer of free reserves to capital redemption reserve to the extent of nominal value of share capital bought back out through free reserves)			

Notes:

1. In place of entry (a), Alternative set of entries can be given as follows:

₹ in lakhs

Particulars		Dr. (₹)	Cr. (₹)
Equity share capital A/c	Dr.	112.50	
Premium payable on buy-back	Dr.	225.00	
To Equity shares buy-back A/c			337.50
(Being the amount due on buy-back of equity shares)			
Securities Premium A/c	Dr	225.00	
To Premium payable on buy-back			225.00
(Being premium payable on buy-back charged from Securities premium)			

2. In place of entry (c), Alternative set of entries can be given as follows:

₹ in lakhs

Particulars		Dr. (₹)	Cr. (₹)
Securities Premium A/c	Dr.	45.00	
General Reserve A/c	Dr.	67.50	
To Capital redemption reserve A/c			112.50
(Being transfer of free reserves to capital redemption reserve to the extent of nominal value of share capital bought back out through free reserves)			

Working Notes:

1. **Shares Outstanding Test**

Particulars	(Shares in lakhs)
Number of shares outstanding	99
25% of the shares outstanding	24.75

2. **Resource Test**

Particulars	
Paid up capital (₹ in lakhs)	990
Free reserves (₹ in lakhs) (720+270+270)	1260
Shareholders' funds (₹ in lakhs)	
25% of Shareholders fund (₹ in lakhs)	2250
Buy-back price per share	₹562.5 lakhs
Number of shares that can be bought back (shares	₹ 30
in lakhs)	18.75 akhs shares

3. **Debt Equity Ratio Test**

	Particulars	When loan fund is		
		₹ 5,400 lakhs	**₹ 3,600 lakhs**	**₹ 4,500 lakhs**
(a)	Loan funds (₹ in lakhs)	5,400	3,600	4,500
(b)	Minimum equity to be maintained after buyback in the ratio of 2:1 (₹ in lakhs)	2,700	1,800	2,250
(c)	Present equity shareholders fund (₹ in lakhs)	2,250	2,250	2,250
(d)	Future equity shareholder fund (₹ in lakhs)	N.A	2137.5 (2,250-112.5)	N.A.

Scanned with OKEN Scanner

(e)	Maximum permitted buy-back of Equity (₹in lakhs) [(d) – (b)]1	Nil	337.5 (by simultaneous equation)	Nil
(f)	Maximum number of shares that can be bought back @ ₹30 per share (shares in lakhs) (See Working Note)	Nil	11.25(by simultaneous equation)	Nil

Under Situations 1 & 3 the company does not qualify for buy-back of shares as per the provisions of the Companies Act, 2013.

Working Note:

Amount transferred to CRR and maximum equity to be bought back will be calculated by simultaneous equation method. As per section 68 of the Companies Act, 2013, the ratio of debt owed by the company should not be more than twice the capital and its free reserve after such buy-back. In the question, it is stated that the company has surplus funds to dispose of therefore; it is presumed that buy- back is out of free reserves or securities premium and hence a sum equal to the nominal value of the share bought back shall be transferred to Capital Redemption Reserve (CRR). Utilization of CRR is restricted to issuance of fully paid-up bonus shares only. It means CRR is not available for distribution as dividend. Hence, CRR is not a free reserve. Therefore, for calculation of future equity i.e. share capital and free reserves, amount transferred to CRR on buy-back has to be excluded from present equity.

Suppose amount equivalent to nominal value of bought back shares transferred to CRR account is 'x' and maximum permitted buy-back of equity is 'y'.

Then

Equation 1 : (Present equity – Nominal value of buy-back transfer to CRR) – Minimum equity to be maintained= Maximum permissible buy-back of equity

$(2250 - x) - 1800 = y$ (1)

Since $450 - x = y$

Equation 2: $\left[\frac{\text{maximum by – back}}{\text{Offer price for buy – back}}\right] \times$ Nominal Value

= Nominal value of the shares bought –back to be transferred to CRR

$= (Y/30) \times 10 = x$

Or $3x = y$ (2)

by solving the above two equations we get

x = ₹112.5 lakhs

y = ₹ 337.5 lakhs

QUESTION 38

Extra Ltd. (a non-listed company) furnishes you with the following Balance Sheet as at 31st March, 20X1:

(in lakhs ₹)

		Particulars	Notes	₹
		Equity and Liabilities		
1		**Shareholders' funds**		
	A	Share capital	1	120
	B	Reserves and Surplus	2	118
2		**Non-current liabilities**		
		Long term borrowings	3	4
3		**Current liabilities**		
	A	Trade Payables		70
		Total		**312**
		Assets		

Scanned with OKEN Scanner

1		**Non-current assets**		
	A	Property, plant and Equipment		50
	B	Non-current Investments		120
2		**Current assets**		
	A	Cash and Cash equivalents		142
		Total		**312**

Notes to accounts

No.	Particulars	₹
1	**Share Capital**	
	Authorized, issued and subscribed capital:	
	Equity shares of ₹ 10 each fully paid	100
	9% Redeemable preference shares of ₹ 100 each fully paid	20
	Total	120
2	**Reserves and Surplus**	
	Capital reserves	8
	Revenue reserves	50
	Securities premium	60
	Total	118
3	**Long term borrowings**	
	10% Debentures	4

(i) The company redeemed the preference shares at a premium of 10% on 1st April, 20X1.

(ii) It also bought back 3 lakhs equity shares of ₹ 10 each at ₹ 30 per share. The payment for the above was made out of huge bank balances.

(iii) Included in its investment were "investments in own debentures" costing ₹ 2 lakhs (face value ₹ 2.20 lakhs). These debentures were cancelled on 1st April, 20X1.

(iv) The company had 1,00,000 equity stock options outstanding on the above- mentioned date, to the employees at ₹ 20 when the market price was ₹30 (This was included under current liabilities). On 1.04.20X1 employees exercised their options for 50,000 shares.

(i) Pass the journal entries to record the above.

(ii) Prepare Balance Sheet as at 01.04.20X1.

SOLUTION

(₹ in lakhs)

Date	Particulars		Debit	Credit
20X1	9% Redeemable preference share capital A/c	Dr.	20.00	
1st April	Premium on redemption of preference shares A/c	Dr.	2.00	
	To Preference shareholders A/c			22.00
	(Being preference share capital transferred to shareholders account)			
	Preference shareholders A/c	Dr.	22.00	
	To Bank A/c			22.00
	(Being payment made to shareholders)			
	Equity shares buy-back A/c	Dr.	90.00	
	To Bank A/c			90.00
	(Being 3 lakhs equity shares of ₹ 10 each bought back @ ₹ 30 per share)			
	Equity share capital A/c	Dr.	30.00	
	Securities premium A/c	Dr.	60.00	
	To Equity Shares buy-back A/c			90.00
	(Being cancellation of shares bought back)			
	Revenue reserve A/c	Dr.	50.00	

Scanned with OKEN Scanner

	To Capital redemption reserve A/c			50.00
	(Being creation of capital redemption reserve account to the extent of the face value of preference shares redeemed and equity shares bought back as per the law)			
	10% Debentures A/c	Dr.	2.20	
	To Investment (own debentures) A/c			2.00
	To Profit on cancellation of own debentures A/c			0.20
	(Being cancellation of own debentures costing ₹ 2 lakhs, face value being ₹ 2.20 lakhs and the balance being profit on cancellation of debentures)			
	Bank A/c	Dr.	10.00	
	Employees stock option outstanding (Current liabilities) A/c	Dr.	5.00	
	To Equity share capital A/c			5.00
	To Securities premium A/c			10.00
	(Being the allotment to employees, of 50,000 shares of ₹ 10 each at a premium of 20 per share in exercise of stock options by employees)			
	Securities premium A/c	Dr.	2.00	
	To Premium on redemption of preference shares A/c			2.00
	(Being premium on redemption of preference shares adjusted through securities premium)			

Balance Sheet of Extra Ltd. as at 01.04.20X1

(in lakhs ₹)

		Particulars	Notes	₹
		Equity and Liabilities		
1		**Shareholders' funds**		
	A	Share capital	1	75.00
	B	Reserves and Surplus	2	66.20
2		**Non-current liabilities**		
		Long term borrowings	3	1.80
3		**Current liabilities**		
	A	Other Current Liabilities	4	65.00
		Total		**208**
		Assets		
1		**Non-current assets**		
	A	Property, plant and Equipment		50.00
	B	Non-current Investments	5	118.00
2		**Current assets**		
	A	Cash and Cash equivalents	6	40.00
		Total		**208**

Notes to accounts

No.	Particulars		₹
1	**Share Capital**		
	Equity shares of ₹ 10 each fully paid		100
	Less: Cancellation of bought back shares		(30)
	Add: Shares issued against ESOP		5
	Total		75
2	**Reserves and Surplus**		
	Capital Reserve		
	Opening balance	8.00	

Scanned with OKEN Scanner

	Add: Profit on cancellation of debentures	0.20	8.20
	Revenue reserves		
	Opening balance	50.00	
	Less: Creation of Capital Redemption Reserve	(50.00)	-
	Securities Premium		
	Opening balance	60.00	
	Less: Adjustment for cancellation of equity shares	(60.00)	
	Less: Adjustment for premium on redemption of preference shares	(2.00)	
	Add: Shares issued against ESOP at premium	10.00	8.00
	Capital Redemption Reserve		50.00
	Total		66.20
3	**Long term borrowings**		
	10% Debentures		4.00
	Less: Cancellation of own debentures		(2.20)
	Total		1.80
4.	**Other Current liabilities**		
	Opening balance		70.00
	Less: Adjustment for ESOP outstanding		(5.00)
	Total		65.00
5.	**Non-current investments**		
	Opening balance		120.00
	Less: Investment in own debentures		(2.00)
	Total		118.00
6.	**Cash and Cash Equivalents**		
	Opening balance		142.00
	Less: Payment to preference shareholders		(22.00)
	Less: Payment to equity shareholders		(90.00)
	Add: Share price received against ESOP		10.00
	Total		**40.00**

QUESTION 39

X Ltd. furnishes the following summarized Balance Sheet as at 31 -03-2018.

Liabilities	**(in Rs)**	**(in Rs)**
Share Capital		
Equity Share Capital of Rs 20 each fully paid up	50,00,000	
10,000, 10% Preference Shares of Rs 100 each fully paid up	10,00,000	60,00,000
Reserves & Surplus		
Capital Reserve	1,00,000	
Security Premium	12,00,000	
Revenue Reserve	5,00,000	
Profit and Loss	20,00,000	
Dividend Equalization Fund	5,50,000	43,50,000
Non-Current Liabilities		
12% Debenture		12,50,000
Current Liabilities and Provisions		5,50,000
Total		**1,21,50,000**
Assets		
Fixed Assets		
Tangible Assets		1,00,75,000
Current Assets		
Investment	3,00,000	
Inventory	2,00,000	

Scanned with OKEN Scanner

Cash and Bank	15,75,000	20,75,000
Total		**1,21,50,000**

The shareholders adopted the resolution on the date of the above-mentioned Balance Sheet to:

(1) Buy back 25% of the paid-up capital and it was decided to offer a price of 20% over market price. The prevailing market value of the company's share is Rs 30 per share.

(2) To finance the buy-back of shares, company:

(a) Issues 3000, 14% debentures of Rs 100 each at a premium of 20%.

(b) Issues 2500, 10% preference shares of Rs 100 each.

(3) Sell investment worth Rs 1,00,000 for Rs 1,50,000.

(4) Maintain a balance of Rs 2,00,000 in Revenue Reserve.

(5) Later the company issue three fully paid-up equity share of Rs 20 each by way of bonus share for every 15-equity share held by the equity shareholders.

You are required to pass the necessary journal entries to record the above transactions and prepare Balance Sheet after buy back.

SOLUTION:

In the books of X Limited

Journal Entries

	Particulars		Dr. Rs	Cr. Rs
1.	Bank A/c	Dr.	3,60,000	
	To 14 % Debenture A/c			3,00,000
	To Securities Premium A/c			60,000
	(Being 14 % debentures issued to finance buy back)			
2.	Bank A/c	Dr.	2,50,000	
	To 10% preference share capital A/c (Being 10% preference share issued to finance buy back)			2,50,000
3.	Bank A/c	Dr.	1,50,000	
	To Investment A/c			1,00,000
	To Profit on sale of investment (Being investment sold on profit)			50,000
4.	Equity share capital A/c (62,500 x Rs 20)	Dr.	12,50,000	
	Securities premium A/c (62,500 x Rs 16)	Dr.	10,00,000	
	To Equity shares buy back A/c (62,500 x Rs36)			22,50,000
	(Being the amount due to equity shareholders on buy back)			
5.	Equity shares buy back A/c	Dr.	22,50,000	
	To Bank A/c			22,50,000
	(Being the payment made on account of buyback of 62,500 Equity Shares as per the Companies Act)			
6.	Revenue reserve	Dr.	3,00,000	
	Securities premium	Dr.	2,60,000	
	Profit and Loss A/c	Dr.	4,40,000	
	To Capital redemption reserve A/c*			10,00,000
	(Being amount equal to nominal value of buy back shares from free reserves transferred to capital redemption reserve account as per the law) [12,50,000 less 2,50,000]			
7.	Capital redemption reserve A/c	Dr.	7,50,000	
	To Bonus shares A/c (W.N.1) (Being the utilization of capital redemption reserve to issue 37,500 bonus shares)			7,50,000
8.	Bonus shares A/c	Dr.	7,50,000	
	To Equity share capital A/c			7,50,000

Scanned with OKEN Scanner

	(Being issue of 3 bonus equity share for every 15equity shares held)		

*Alternatively, entry for combination of different amounts (from Revenue reserve, Securities premium and profit and Loss account.) may be passed for transferring the required amount to CRR.

Note: It may be noted that as per the provisions of the Companies Act, no buy-back of any kind of shares or other specified securities shall be made out of the proceeds of an earlier issue of the same kind of shares or same kind of other **specified securities**. Issue of debentures has been excluded for the purpose of **"specified securities"** and the entire amount of Rs 10,00,000 (after deducting only pref. share capital) has been credited to CRR while solving the question.

Balance Sheet (After buy back and issue of bonus shares)

Particulars	Note No	Amount Rs
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	57,50,000
(b) Reserves and Surplus	2	27,10,000
(2) Non-Current Liabilities		
(a) Long-term borrowings	3	15,50,000
(3) Current Liabilities		
(a) Trade payables		-
(b) current liabilities & Provisions		5,50,000
Total		1,05,60,000
II. Assets		
(1) Non-current assets		
(a) Property, Plant and Equipment		1,00,75,000
(2) Current assets		
(a) Investments		2,00,000
(b) Inventory		2,00,000
(c) Cash and cash equivalents (W.N. 2)		85,000
Total		**1,05,60,000**

Notes to Accounts

				Rs
1.	Share Capital			
	Equity share capital (Fully paid-up shares of Rs 20 each)			
	(2,50,000-62,500+37,500 shares)		45,00,000	
	10% preference shares @ Rs 100 each (10,00,000 + 2,50,000)		12,50,000	
2.	Reserves and Surplus			
	Capital Reserve		1,00,000	57,50,000
	Revenue reserve		2,00,000	
	Securities premium	12,00,000		
	Add: Premium on debenture	60,000		
	Less: Adjustment for premium paid on buy back (10,00,000)			
	Less: Transfer to CRR	(2,60,000)	Nil	
	Capital Redemption Reserve			
	Transfer due to buy-back of shares from P&L 10,00,000			
	Less: Utilisation for issue of bonus shares	(7,50,000)	2,50,000	
	Profit & Loss A/c	20,00,000		
	Add: Profit on sale of investment	50,000		
	Less: Transfer to CRR	(4,40,000)	16,10,000	
	Dividend equalization reserve	(5,50,000)	5,50,000	27,10,000

Scanned with OKEN Scanner

3.	Long-term borrowings - 12% Debentures 12,50,000			
	- 14% Debentures	3,00,000		15,50,000

Working Notes:

1. Amount of bonus shares = [(2,50,000 -25%)3/15] x 20 = 37,500 x 20=7,50,000
2. Cash at bank after issue of bonus shares

	Rs
Cash balance as on 30.3.2018	15,75,000
Add: Issue of debenture	3,60,000
Add: issue of preference shares	2,50,000
Add: Sale of investments	1,50,000
	23,35,000
Less: Payment for buy back of shares	(22,50,000)
	85,000

Scanned with OKEN Scanner

7. CASH FLOW STATEMENT

QUESTION 40

Prepare Cash flow for Gamma Ltd., for the year ending 31.3.20X1 from the following information:

(1) Sales for the year amounted to Rs135 crores out of which 60% was cash sales.

(2) Purchases for the year amounted to Rs55 crores out of which credit purchase was 80%.

(3) Administrative and selling expenses amounted to Rs. 18 crores and salary paid amounted to Rs22 crores.

(4) The Company redeemed debentures of Rs20 crores at a premium of 10%. Debenture holders were issued equity shares of Rs15 crores towards redemption and the balance was paid in cash. Debenture interest paid during the year was Rs1.5 crores.

(5) Dividend paid during the year amounted to Rs11.7 crores (including Dividend distribution tax) was also paid.

(6) Investment costing Rs12 crores were sold at a profit of Rs2.4 crores.

(7) Rs8 crores was paid towards income tax during the year.

(8) A new plant costing Rs21 crores was purchased in part exchange of an old plant. The book value of the old plant was Rs12 crores but the vendor took over the old plant at a value of Rs10 crores only. The balance was paid in cash to the vendor.

(9) The following balances are also provided:

	Rs in crores 1.4.20X0	Rs in crores 31.3.20X1
Debtors	45	50
Creditors	21	23
Bank	6	

SOLUTION

Gamma Ltd.
Cash Flow Statement for the year ended
31st March, 20X1 (Using direct method)

Particulars	Rs in crores	Rs in crores
CASH FLOWS FROM OPERATING ACTIVITIES		
Cash sales (60% of 135)	81	
Cash receipts from Debtors [45+ (135x40%) – 50]	49	
Cash purchases (20% of 55)	(11)	
Cash payments to suppliers [21+(55x80%)23]	(42)	
Cash paid to employees	(22)	
Cash payments for overheads (Adm. And selling)	(18)	
Cash generated from operations	37	
Income tax paid	(8)	
Net cash generated from operating activities		**29**
CASH FLOWS FROM INVESTING ACTIVITIES		
Sale of investments (12+ 2.40)	14.4	
Payments for purchase of fixed assets (21 – 10)	(11)	
Net cash used in investing activities		**3.4**
CASH FLOWS FROM FINANCING ACTIVITIES		
Redemption of debentures (22-15)	(7)	
Interest paid	(1.5)	
Dividend paid	(11.7)	
Net cash used in financing activities		**(20.2)**
Net increase in cash		12.2
Cash at beginning of the period		6.0
Cash at end of the period		18.2

Scanned with OKEN Scanner

QUESTION 41:

Following are the extracts of Balance Sheet of Ajay Ltd.:

			31.3.20X1	31.3.20X2
	Equity and Liabilities		Rs	Rs
	Shareholder's funds			
a.	Share Capital	1	5,00,000	5,00,000
b.	Reserves & surplus	2	50,000	90,000
	Non-current liabilities			
a.	Long-term borrowings	3	5,00,000	7,50,000
	Current liabilities			
a.	Other current liabilities	4	---	5,000
	Assets			
	Non-current assets			
a.	Intangible assets	5	2,05,000	1,80,000

Notes to accounts

		31.03.20X1 (Rs.)	31.03.20X2 (Rs.)
1	**Share Capital**		
	50,000 Equity Shares of Rs. 10 each	5,00,000	5,00,000
2	**Reserves & Surplus**		
	Profit & Loss A/c	50,000	90,000
3	**Long-term borrowings**		
	10% Debentures	5,00,000	7,50,000
4	**Other current liabilities**		
	Unpaid Interest	--	5,000
5	**Intangible assets**		
	Goodwill	2,05,000	1,80,000

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

SOLUTION

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

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

Cash flows from financing activities:

Proceeds from debentures	2,40,000
Interest paid on Debentures [less unpaid]	(70,000)
Net Cash from Financing Activities	**1,70,000**

QUESTION 42:

From the following Balance Sheet & information, prepare Cash Flow Statement of Ryan Ltd. by Indirect method for the year ended 31st March, 20X1:

Balance Sheet

	31st March, 20X1	31st March, 20X0
Liabilities		
Equity Share Capital	6,00,000	5,00,000

Scanned with OKEN Scanner

10% Redeemable Preference Share Capital	–	2,00,000
Capital Redemption Reserve	1,00,000	–
Capital Reserve	1,00,000	–
General Reserve	1,00,000	2,50,000
Profit and Loss Account	70,000	50,000
9% Debentures	2,00,000	–
Trade payables	1,15,000	1,10,000
Liabilities for Expenses	30,000	20,000
Provision for Taxation	95,000	60,000
Dividend payable	90,000	60,000
	15,00,000	**12,50,000**
	31st March,20X1	**31st March,20X0**
Assets		
Land and Building	1,50,000	2,00,000
Plant and Machinery	7,65,000	5,00,000
Investments	50,000	80,000
Inventory	95,000	90,000
Trade receivables	2,50,000	2,25,000
Cash and Bank	65,000	90,000
Voluntary Separation Payments	1,25,000	65,000
	15,00,000	**12,50,000**

Additional Information:

(i) A piece of land has been sold out for Rs 1,50,000 (Cost – Rs 1,20,000) and the balance land was revalued. Capital Reserve consisted of profit on sale and profit on revaluation.

(ii) On 1st April, 20X0 a plant was sold for Rs 90,000 (Original Cost – Rs 70,000 and W.D.V. – Rs 50,000) and Debentures worth Rs1 lakh was issued at par as part consideration for plant of Rs4.5 lakhs acquired.

(iii) Part of the investments (Cost – Rs 50,000) was sold for Rs 70,000.

(iv) Pre-acquisition dividend received Rs 5,000 was adjusted against cost of investment.

(v) Directors have declared 15% dividend for the current year.

(vi) Voluntary separation cost of Rs 50,000 was adjusted against General Reserve.

(vii) Income-tax liability for the current year was estimated at Rs 1,35,000.

Depreciation @ 15% has been written off from Plant account, but no depreciation has been charged on Land and Building.

SOLUTION

Cash Flow Statement of Ryan Limited
For the year ended 31st March, 20X1

	Particulars	Rs	
	CASH FLOW FROM OPERATING ACTIVITIES		
	Net Profit before taxation (W.N.1)	2,45,000	
	Adjustment for		
	Depreciation (W.N.3)	1,35,000	
	Profit on sale of plant (W.N.3)	(40,000)	
	Profit on sale of investments (W.N.3)	(20,000)	
	Interest on debentures (W.N.4)	18,000	
	Operating profit before working capital changes	**3,38,000**	
	Increase in inventory	(5,000)	
	Increase in trade receivables	(25,000)	
	Increase in Trade payables	5,000	
	Increase in accrued liabilities	10,000	
	Extraordinary items	(1,10,000)	
	Income taxes paid (W.N.8)	(1,00,000)	

Scanned with OKEN Scanner

	Net cash generated from operating activities		**1,13,000**
	CASH FLOW FROM INVESTING ACTIVITIES		
	Proceeds from sale of land (W.N.2)	1,50,000	
	Proceeds from sale of plant (W.N.3)	90,000	
	Proceeds from sale of investments (W.N.4)	70,000	
	Purchase of plant (W.N.3)	(3,50,000)	
	Purchase of investments (W.N.4)	(25,000)	
	Pre-acquisition dividend received (W.N.4)	5,000	
	Net cash used in investing activities		**(60,000)**
	CASH FLOW FROM FINANCING ACTIVITIES		
	Proceeds from issue of equity shares (6,00,000 – 5,00,000)	1,00,000	
	Proceeds from issue of debentures (2,00,000 – 1,00,000)	1,00,000	
	Redemption of preference shares	(2,00,000)	
	Dividends paid	(60,000)	
	Interest paid on debentures	(18,000)	
	Net cash used in financing activities		**(78,000)**
	Net decrease in cash and cash equivalents		(25,000)
	Cash and cash equivalents at the beginning of the year		90,000
Cash and Cash equivalents at the end of the year			65,000

Working Notes:

1. Net Profit before taxation

Particulars	Rs
Net profit before taxation	
Retained profit	1,00,000
Less: Balance as on 31.3.20X0	(50,000)
	20,000
Provision for taxation	1,35,000
Dividend payable	90,000
Net Profit before taxation	2,75,000

2. Land and Building Account

	Particulars	Rs		Particulars	Rs
To	Balance b/d	2,00,000	By	Cash (Sale)	1,50,000
To	Capital reserve (Profit on sale)	30,000	By	Balance c/d	1,50,000
To	Capital reserve (Revaluation profit)	70,000			
		3,00,000			**3,00,000**

3. Plant and Machinery Account

	Particulars	Rs		Particulars	Rs
To	Balance b/d	5,00,000	By	Cash (Sale)	90,000
To	Profit and loss account	40,000	By	Depreciation	1,35,000
To	Debentures	1,00,000	By	Balance c/d	7,65,000
To	Bank	3,50,000			
		9,90,000			**9,90,000**

4. Investments Account

Particulars	Rs	Particulars	Rs
To Balance b/d	80,000	By Cash (Sale)	70,000
To Profit and loss account	20,000	By Dividend (Pre acquisition)	5,000

Scanned with OKEN Scanner

To Bank (Balancing figure)	25,000	To Balance C/d	50000
	125000		**125000**

5. Capital Reserve Account

Particulars	Rs	Particulars	Rs
To Balance c/d	70,000	By Profit on revaluation of land	70,000
	70,000		**700,000**

6. General Reserve Account

Particulars	Rs	Particulars	Rs
To Capital redemption reserve	1,00,000	By Balance b/d	2,50,000
To Balance c/d	1,50,000		
	2,50,000		**2,50,000**

7. Dividend payable Account

	Particulars	Rs		Particulars	Rs
To	Bank (Balancing figure)	1,50,000	By	Balance b/d	60,000
To	Balance c/d	-	By	Profit & loss account	90,000
		1,50,000			**1,50,000**

8. Provision for Taxation Account

Particulars	Rs	Particulars	Rs
To Bank (Balancing figure)	1,00,000	By balance b/d	60,000
To Balance c/d	95,000	By Profit & loss account	1,35,000
	1,95,000		**1,95,000**

9. Other Current Assets Account

Particulars	Rs	Particulars	Rs
To Balance b/d	65,000	By Balance c/d	1,00,000
To Bank (Balancing figure)	35,000		
	1,00,000		**1,00,000**

QUESTION 43

The following information was extracted from the books of S Ltd. for the year ended 31.03.2020.

(1) Net profit before taking into account income tax and after taking into account the following items was Rs. 30 Lakhs
   - (a) Depreciation on Property, Plant and Equipment Rs. 7,00,000
   - (b) Discount on issue of debentures written off Rs. 45,000
   - (c) Interest on debentures paid Rs. 4,35,000
   - (d) Investment of Book value Rs. 3,50,000 sold for 3,75,000
   - (e) Interest received on investments Rs.70,000

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

(3) The company issued 60,000 equity shares of Rs. 10 each at a premium of 20% on 10.04.2019

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

(5) Dividend paid during the year amounted to Rs. 11,00,000 (Including dividend distribution tax)

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

(7) Company decided to value inventory at cost, whereas previously the practice was to value inventory at cost less 10%. The inventory according to books on 31.03.2020 was 14,76,000.
The Inventory on 31.03.2019 was correctly valued at Rs. 13,50,000

(8) Current assets and current liabilities in the beginning and at the end of the years 2019-2020 were as:

Scanned with OKEN Scanner

	As on 01.04.2019	As on 31.03.2020
	Rs.	Rs.
Inventory	13,50,000	14,76,000
Trade Receivables	3,27,000	3,13,200
Cash in Hand	2,40,700	3,70,500
Trade payables	2,84,700	2,87,300
Outstanding expenses	97,000	1,01,400

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

SOLUTION

S Ltd.

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

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

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

Scanned with OKEN Scanner

QUESTION 44:

Given below is the Statement of Profit and Loss of ABC Ltd. and relevant Balance Sheet information:

Extract of Balance sheet

		Particular	Notes	31.3.20X1 (Rs. In lakhs)	31.3.20X0 (Rs. In lakhs)
		Equity and Liabilities			
1		**Current liabilities**			
	A	Trade Payables		250	230
	B	Short term Provisions	1	200	180
	C	Other current liabilities	2	70	50
		Assets			
1		**Current assets**			
	A	Inventories		200	180
	B	Trade Receivable		400	250
	C	Other current assets	3	195	180

Statement of Profit and Loss of ABC Ltd.
for the year ended 31st March, 20X1

	Particulars	Notes	Rs. In lakhs
I	Revenue from operations		4,150
II	Other income	4	100
III	Total income (I + II)		**4250**
	Expenses:		
	Purchase on Stock-in-Trade		2,400
	Change in inventories of finished goods		(20)
	Employee benefits expense		800
	Depreciation expense		100
	Finance cost	5	60
	Other expenses		200
IV	**Total expenses**		**3,540**
V	Profit before tax (III -IV)		710
VI	Tax expense:		
	Current tax		200
VII	**Profit for the year from continuing operations**		**510**

Appropriations

Balance of profit and loss account brought forward	50
Transfer to general reserve	200
Dividend paid	330

Notes to accounts:

		20X1 (Rs. In lakhs)	20X0 (Rs. In lakhs)
1	**Short term provision**		
	Provision for tax	200	180
2	**Other current liabilities**		
	Outstanding wages	50	40
	Outstanding expenses	20	10
	Total	**70**	**50**
3	**Other current assets:**		
	Advance tax	195	180
4	**Other income:**		

Scanned with OKEN Scanner

	Interest and dividend	100	
5	**Finance cost:**		
	Interest	60	

Compute cash flow from operating activities using both direct and indirect method.

SOLUTION

By direct method

Computation of Cash Flow from Operating Activities

Particulars	**Rs in lakhs**	**Rs in lakhs**
Cash Receipts:		
Cash sales and collection from Trade receivables		
Sales + Opening Trade receivables – Closing Trade receivables (A)	4,150+250-400	4,000
Cash payments:		
Cash purchases & payment to Trade payables Purchases + Opening Trade payables – Closing Trade payables	2,400+230-250	2,380
Wages and salaries paid	800+40-50	790
Cash expenses	200+10–20	190
Taxes paid – Advance tax		195
(B)		3,555
Cash flow from operating activities (A – B)		**445**

By Indirect Method

Computation of Cash Flow from Operating Activities

	Rs in lakhs	**Rs in lakhs**
By Indirect method		
Profit before tax		710
Add: Non-cash items: Depreciation		100
Add: Interest: Financing cash outflow		60
Less: Interest and Dividend: Investment cash inflow		(100)
Less: Tax paid		(195)
Working capital adjustments		
Trade receivables	250-400 = (150)	
Inventories	180-200 = (20)	
Trade payables	250-230 =20	
Outstanding wages	50-40=10	
Outstanding expenses	20-10 =10	(130)
Cash flow from operating activities		**445**

MASTER QUESTION

Mr. Shubham provides us his Balance sheet as on 31/03/20X2 along with additional information:

		(₹ in Cr.)
EQUITY AND LIABILITIES	**Opening Balances**	**Closing Balances**
Equity Share Capital	50,00,000	69,00,000
8% pref. Sh. Capital	15,00,000	10,00,000
P&L Account	23,00,000	30,00,000
General Reserve	7,00,000	9,00,000
CRR	-	3,00,000
9% Bank Loan	70,00,000	76,00,000
Loan From Nidhi (Interest free)	9,00,000	-

Scanned with OKEN Scanner

Creditors	32,00,000	37,00,000
Bills Payable	5,00,000	6,00,000
Tax provision	17,00,000	21,50,000
O/s expenses	2,50,000	1,20,000
Dividend payable	5,50,000	70,000
	2,36,00,000	**2,69,70,000**

ASSETS		
Residential property	-	1,00,00,000
P&M (Gross Value)	12,00,000	15,00,000
(-) Provision For Dep	(3,50,000)	(4,75,000)
Investments	50,00,000	10,00,000
Loan to Mr. Jai	5,00,000	3,00,000
Goodwill	30,00,000	15,00,000
Trade Receivable	60,00,000	35,00,000
Inventory	40,00,000	50,00,000
Advance Tax	16,00,000	24,00,000
Prepaid Expenses	7,00,000	8,00,000
Advertisement Exp (Deferred)	13,00,000	10,00,000
Cash & Cash Equivalent	6,50,000	4,45,000
	2,36,00,000	**2,69,70,000**

Additional Information:-

1) Grant received for Business purpose Rs.7,50,000 & Charged to P&L.
2) Dividend received ₹ 6,00,000 out of which 1,50,000 is Pre-Acquisition.
3) Preferece Shares were redeemed at 10% premium & Premium is w/f in P&L.
4) Tax paid during the year 30,00,000.
5) Interim Dividend paid 4,00,000.
6) P&M of Org. Cost of 4,00,000 with Accumulated Depreciation of 2,50,000 was 37,500 sold at25% Profit.
7) New P&M purchased, 60% payment in Cash & remaining in the form of Issue of ESC.
8) Depreciation on P&M is 3,75,000.
9) Opening Inventory is measured at Cost less 50%. Closing Inventory is measured at cost + 25%
10) Advertisement Expenditure of 5,00,000 W/off directly from GR.
11) Bad-debts during the year charged to Profit and Loss A/c 3,00,000.
12) Exchange Loss due to Remeasurement of creditors as per AS 11 - 1,00,000 transfer to P&L.
13) Other Incomes includes Income from Instagram & YouTube 2,50,000 (considered as Extraordinary)
14) Investments were sold at 5% Profit.
15) Other incomes includes total Interest Earned 2,00,000 on which TDS is deducted. TDS 20,000 isa part of Closing Prepaid Expense in Balance Sheet.
16) Loss due to theft = 15,000 cash (Extraordinary)
17) Tax Refund = 50,000

Prepare Statement of Cash Flows as per Indirect Method.

SOLUTION

Statement of Cash Flows

Scanned with OKEN Scanner

1) Cash Flows from Operating Activities:

Particulars	Amount
Difference of P&L	7,00,000
(+) Transfer to GR	10,00,000
(+) Interim Dividend declared and Paid	4,00,000
(+) Final Dividend Declared in CY	7,00,000
(+) Premium on Redemption w/o in Profit and Loss A/c	5,000
Net Profit After Tax (NPAT)	**28,50,000**
(-) Stock adjustment	
Opening Stock adjustment	(40,00,000)
Closing Stock adjustement	(10,00,000)
(+) Tax provision	26,50,000
Net Profit Before Tax	**5,00,000**
(+/-) Adjustment for:-	
(+) Depreciation	3,75,000
(-) Gain on sale of P&M	(37,500)
(-) Advertisement Expenses Paid	(2,00,000)
(-) Gain on sale of Investment	(1,92,500)
(-) Post Acquisition Dividend Received	(4,50,000)
(+) Loss due to theft (extra-ordinary)	15,000
(+) Bad debts (Non-Cash)	3,00,000
(+) Ex. Loss on Creditors	1,00,000
(-) Insta & YT Income (Extra-ordinary)	(2,50,000)
(-) Interest on Investment Earned	(2,00,000)
(-) Tax Refund	(50,000)
(+) Interest on Bank Loan	6,84,000
(+) Amortisation of Goodwill	15,00,000
(+/-) Working Capital Adjustment	
(+) Creditors	4,00,000
(+) Bills Payable	1,00,000
(-) O/s Exp.	(1,30,000)
(+) Trade Receivable	2,00,000
(+) Inventory	40,00,000
(-) Prepaid exp.	(80,000)
Net Cash before Tax & Extra ordinary items	**85,84,000**
(-) Tax paid	(30,00,000)
(-) Loss due to theft	(15,000)
(+) Insta & YT	2,50,000
(+) Tax Refund	50,000
Net Cash generated from Operating Activity (a)	**5,869,000**

2) *Cash Flow from Investing Activity:*

Scanned with OKEN Scanner

Sale of P&M	1,87,500
(-) Payment for purchase for P&M	(4,20,000)
(+) Sale of Investments	4,042,500
(+) Dividend received	
Pre-acquisition	1,50,000
Post-acquisition	4,50,000
(+) Interest Collected	1,80,000
(-) Investment in Residential Property	(1,00,00,000)
(+) Loan repaid by Mr. Jai	2,00,000
Net Cash used in Investing Activity (b)	**(52,10,000)**

3) Cash Flow from Financing Activity:

(-) Interim Dividend Paid	(4,00,000)
(-) Final Dividend of PY Paid in CY	(5,50,000)
(-) Redemption of PSC	(5,50,000)
(+) Issue of ESC	16,20,000
(+) Bank Loan raised	6,00,000
(-) Interest on Bank Loan	(6,84,000)
(-) Loan Repaid to Nidhi	9,00,000
Net Cash used in Financing Activity (c)	**86,4,000**
Net cash outflow during the Year (a+b+c)	**2,05,000**
(+) Opening balance of Cash & CE	6,50,000
Closing balance of Cash & CE	**4,45,000**

Working Note - 1 **Tax a/c**

To Balance bld	16,00,000	By Balance b/d	17,00,000
To Bank (tax paid)	30,00,000	**By P&L (balancing fig.)**	**26,50,000**
To Balance c/f	21,50,000	By Balance c/f	24,00,000

Working Note – 2 **Plant & Machine (Gross)**

To Balance b/d	12,00,000	By Provision for Depreciation	2,50,000
To P&L (Gain)	37,500	By Bank	1,87,500
To Bank (bal. fig.)	**4,20,000**		
To ESC (bal. fig.)	**2,80,000**	By Balance c/d	15,00,000

Provision for Depreciation

To P&M	2,50,000	By Balance b/d	3,50,000
To Balance c/d	4,75,000	By Depreciation	3,75,000

Working Note - 3

ESC Opening	50 lacs
ESC Closing	69 lacs

Scanned with OKEN Scanner

Issued during the year	19 lacs
(-) issued for P&M (Non Cash)	2.8 lacs
Issued against Cash (bal. fig.)	**16.20 lacs**

Working Note - 4

Advertisement Expense (Asset)

To Balance b/d	13,00,000	BY GR	5,00,000
To Bank (bal. fig.)	**2,00,000**	By Balance c/d	10,00,000

WN-5

General Reserve

To Advertisement Exp.	5,00,000	By Balance b/d	7,00,000
To CRR	3,00,000	**By P&L (b/f)**	**10,00,000**
To Balance c/d	9,00,000		

Working Note – 6

Investment A/c

To Balance b/d	50,00,000	By Bank	1,50,000
To Gain (P&L)	192500	**By Bank (bal. fig.)**	**40,42,500**
		By Balance c/d	10,00,000

Working Note – 7

Trade Receivables	
Closing Balance as per B/s	35,00,000
Add: Bad-debts	3,00,000
Closing Trade Receivables before Bad-debts for the purpose of cash flow (since Bad-debt is a non-cash item)	38,00,000
Opening Trade Receivables	60,00,000
Working Capital change due to Trade Receivables	**22,00,000**
Creditors	
Closing Balance as per B/s	37,00,000
less: Exchange Loss	1,00,000
Closing Creditors before Exchange Loss for the purpose of cash flow (since Ex. loss is a non-cash item)	36,00,000
Opening Creditors Balance	32,00,000
Working Capital change due to Trade Receivables	**4,00,000**
Prepaid Expenses	
Closing Balance as per B/s	8,00,000
less: TDS included in Closing balance	20,000
Net Closing balance of Prepaid Exp.	7,80,000
Opening Balance	7,00,000
Working Capital change due to Trade Receivables	80,000

Scanned with OKEN Scanner

8. ACCOUNTING FOR RECONSTRUCTION OF COMPANIES

QUESTION 45

Recover Ltd decided to reorganize its capital structure owing to accumulated losses and adverse market condition. The Balance Sheet of the company as on 31st March 2020 is as follows:

		Particulars	Notes	Rs.
		Equity and Liabilities		
1		**Shareholders' funds**		
	A	Share capital	1	3,50,000
	B	Reserves and surplus	2	(70,000)
2		**Non-current liabilities**		
	A	Long-term borrowings	3	55,000
3		**Current liabilities**		
	A	Trade Payables		80,000
	B	Short term Borrowings – Bank overdraft		90,000
				5,05,000
		Assets		
1		**Non-current assets**		
	A	Property, Plant Equipment	4	3,35,000
	B	Intangible assets	5	50,000
	C	Non-current investments	6	40,000
2		**Current assets**		
	A	Inventories		30,000
	B	Trade receivables		50,000
				5,05,000

Notes to accounts:

1	**Share Capital**	**Rs.**
	Equity share capital:	
	20,000 Equity Shares of Rs. 10 each	2,00,000
	Preference share capital:	
	15,000 8% Cumulative Preference Shares of Rs. 10 each (preference dividend has been in arrears for 4 years)	1,50,000
		3,50,000
2	**Reserves and surplus**	
	Securities premium	10,000
	Profit and loss account (debit balance)	(80,000)
		(70,000)
3	**Long-term borrowings**	
	Secured	
	9% Debentures (secured on the freehold property	50,000
	Accrued interest on 9% debentures	5,000
		55,000
4	**Property, Plant and Equipment**	
	Freehold property	1,20,000
	Leasehold property	85,000
	Plant and machinery	1,30,000
		3,35,000
5	**Intangible assets**	
	Goodwill	50,000

Scanned with OKEN Scanner

		50,000
6	**Non-current investments**	
	Non-Trade investments at cost	40,000
		40,000

Subsequent to approval by court of a scheme for the reduction of capital, the following steps were taken:

i) The preference shares were reduced to Rs. 2.5 per share, and the equity shares to Rs. 1 per share.

ii) One new equity share of Rs. 1 was issued for the arrears of preferred dividend for past 4 years.

iii) The balance on Securities Premium Account was utilized and was transferred to capital reduction account.

iv) The debenture holders took over the freehold property at an agreed figure of Rs. 75,000 and paid the balance to the company after deducting the amount due to them.

v) Plant and Machinery was written down to Rs. 1,00,000.

vi) Non-trade Investments were sold for Rs. 32,000.

vii) Goodwill and obsolete stock (included in the value of inventories) of Rs. 10,000 were written off.

viii) A contingent liability of which no provision had been made was settled at Rs. 7,000 and of this amount, Rs. 6,300 was recovered from the insurance.

You are required (a) to show the Journal Entries, necessary to record the above transactions in the company's books and (b) to prepare the Balance Sheet, after completion of the scheme.

SOLUTION:

In the books of Recover Ltd

Journal entries

Particulars		**Dr. Rs.**	**Cr. Rs.**
8% Cumulative Preference share capital (Rs. 10) A/c	Dr.	1,50,000	
To 8% Cumulative Preference share capital (Rs. 2.5) A/c			37,500
To Capital reduction (Rs. 7.5) A/c			1,12,500
(Preference shares being reduced to shares of Rs. 2.5 per share and remaining transferred to capital reduction account as per capital reduction scheme)			
Equity share capital A/c (Rs. 10)	Dr.	2,00,000	
To Equity Share capital A/c (Rs. 1)			20,000
To Capital reduction A/c (Rs. 9)			1,80,000
(Equity shares reduced to Rs. 1 per share with the remaining amount transferred to capital reduction as a part of the internal reconstruction scheme.)			
Capital reduction A/c	Dr.	48,000	
To Equity share capital A/c			48,000
(Equity shares of Rs. 1 issued in lieu of the arrears of preference dividend for 4 years as a part of the internal reconstruction scheme)			
Securities Premium A/c	Dr.	10,000	
To Capital reduction A/c			10,000
(Amount from the securities premium utilized towards the capital reduction a/c as a part of the internal reconstruction scheme)			
9% Debentures A/c	Dr.	50,000	
Accrued interest on debentures A/c	Dr.	5,000	
Bank A/c	Dr.	20,000	
Capital reduction A/c	Dr.	45,000	
To Freehold property A/c			1,20,000
(Debenture holders being paid by the sale of property, which is sold at a loss debited to the capital reduction account. Amount received in excess being refunded to company by debenture holders as a part of the internal reconstruction scheme.)			
Capital reduction A/c	Dr.	90,000	
To Plant and Machinery Ac			30,000
To Goodwill A/c			50,000
To Inventory A/c			10,000

Scanned with OKEN Scanner

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

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

		Particulars	Notes	Rs.
		Equity and Liabilities		
1		**Shareholders' funds**		
	A	Share capital	1	1,05,500
	B	Reserves and surplus	2	30,800
2		**Non-current liabilities**		
	A	Long-term borrowings		-
3		**Current liabilities**		
	A	Trade Payables		80,000
	B	Short term Borrowings – Bank overdraft		90,000
				3,06,300
		Assets		
1		**Non-current assets**		
	A	Property, Plant Equipment	3	1,85,000
2		**Current assets**		
	A	Inventories		20,000
	B	Trade receivables		50,000
	C	Cash and cash equivalents	4	51,300
				3,06,300

Notes to Accounts

1	**Share Capital**	**Rs.**
	Equity share capital:	
	68,000 Equity Shares of Rs. 1 each	68,000
	Preference share capital:	
	15,000 8% Cumulative Preference Shares of Rs. 2.5 each	3,75,00
		1,05,500
2	**Reserves and surplus**	
	Capital Reserve	30,800

Scanned with OKEN Scanner

3	**Property, Plant and Equipment**	
	Leasehold property	85,000
	Plant and machinery	1,00,000
		1,85,000
4	**Cash and cash equivalents**	
	Bank A/c (20,000+32,000-7000+6,300)	51,300

QUESTION 46

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

Balance Sheet of Purple Limited as at 31st March, 2022

		Particulars	Notes	Rs
		Equity and Liabilities		
1		**Shareholders' funds**		
	a	Share capital	1	15,00,000
	b	Reserves & Surplus	2	(3,00,000)
2		**Current liabilities**		
	A	Trade Payables		2,20,000
	b	Short Term Borrowings – Bank Overdraft		2,00,000
		Total		**16,20,000**
		Assets		
1		**Non-current assets**		
	a	Property, Plant and Equipment	3	10,20,000
	b	Intangible assets	4	1,20,600
2		**Current assets**		
	a	Inventories		1,70,000
	b	Trade receivables		3,01,800
	c	Cash and cash equivalents		7,600
		Total		**16,20,000**

Notes to accounts:

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

Dividends on Preference shares are in arrears for 3 years.

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

(i) The preference shares are converted from 6% to 8% but revalued in a manner in which the total return on them remains unaffected.

(ii) The value of equity shares is brought down to Rs. 8 per share.

(iii) The arrears of dividend on preference shares are cancelled.

(iv) The debit balance of Goodwill account is written off entirely.

(v) Land & Building and Plant & Machinery are revalued at 85% and 80% of their respective book values.

(vi) Book debts amounting to Rs. 14,400 are to be treated as bad and hence to be written off.

Scanned with OKEN Scanner

(vii) The company expects to earn a profit at the rate of Rs. 90,000 per annum from the current year which would be utilized entirely for reducing the debit balance of Profit and loss accounts for 3 years. The Remaining balance of Said account would be written off at the time of capital reduction process.

(viii) The balance of total capital reduction is to be utilized in writing down patents.

(ix) A secured loan of Rs. 4,80,000 bearing interest at 12% per annum is to be obtained by mortgaging tangible fixed assets for repayment of bank overdraft and for providing additional funds for working capital.

You are required to give journal entries incorporating the above scheme of reconstruction, capital reduction account and prepare the reconstructed Balance Sheet.

SOLUTION:

Journal Entries In the books of Purple Ltd.

	Particulars		Debit (₹₹)	Credit (₹₹)
1.	6% Preference share capital A/c	Dr.	6,00,000	
	To 8% Preference share capital A/c			4,50,000
	To Capital reduction A/c			1,50,000
	(Being 6% preference shares converted to 8% preference shares so that return to pref. shareholders remains unaffected)			
2.	Equity share capital A/c (₹ 10)	Dr.	9,00,000	
	To Equity share capital A/c (₹ 8)			7,20,000
	To Capital reduction A/c			1,80,000
	(Being equity capital reduced to nominal value of ₹ 8 each)			
3.	Capital Reduction A/c	Dr.	3,30,000	
	To Goodwill A/c			84,600
	To Land and Building A/c			81,000
	To Plant and Machinery A/c			96,000
	To Trade Receivables A/c (Book debts)			14,400
	To Patents A/c (Bal. fig.)			24,000
	To Profit and loss A/c			30,000
	(Being losses and assets written off to the extent required)			
4.	Bank A/c	Dr.	4,80,000	
	To Bank Loan A/c			4,80,000
	(Being Loan taken)			
5.	Bank overdraft A/c	Dr.	2,00,000	
	To Bank A/c			2,00,000
	(Being Bank overdraft repaid)			

Capital Reduction Account

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

Scanned with OKEN Scanner

		3,30,000			**3,30,000**

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

		Particulars	Notes	₹
		Equity and Liabilities		
1		**Shareholders' funds**		
	a	Share capital	1	11,70,000
	b	Reserves and surplus	2	(2,70,000)
2		**Current liabilities**		
	a	Short term borrowings (Secured Bank Loan)		4,80,000
	b	Trade Payables		2,20,000
		Total		**16,00,000**
		Assets		
1		**Non-current assets**		
	a	Property, plant and equipment	3	8,43,000
	b	Intangible assets	4	12,000
2		**Current Assets**		
	a	Inventory		1,70,000
	b	Trade receivables	5	2,87,400
	c	Cash and cash equivalents (7,600+4,80,000-2,00,000)		2,87,600
		Total		**16,00,000**

Notes to Accounts:

			₹
1.	**Share Capital**		
	Authorized		
	Issued, subscribed and paid up:		
	90,000 equity shares of ₹ 8 each fully paid	7,20,000	
	8% Preference share capital*	4,50,000	11,70,000
2.	**Reserves and Surplus**		
	Profit and Loss Account (Dr. balance)		(2,70,000)
3.	**Property plant and equipment**		
	Land and Building	4,59,000	
	Plant and Machinery	3,84,000	8,43,000
4.	**Intangible assets**		
	Patent ₹ (36,000 - 24,000)		12,000
5.	**Trade Receivables**		
	Sundry Debtors	3,01,800	
	Less: Bad debts	(14,400)	2,87,400

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

Scanned with OKEN Scanner

Working Notes:

1. **Calculation of new Preference Shares**

Rate of return	6% on Preference Shares
Dividend	(6/100) x ₹6,00,000=₹36,000
Rate of return	8% on Preference Shares
Dividend	(8/100) x X = ₹36,000 X = (36,000/8) x 100 = 4,50,000
New Preference Share Capital	₹ 4,50,000
Old Preference Share Capital	₹ 6,00,000
Amount taken to capital Reduction A/C. (6,00,000-4,50,000)	₹1,50,000 Amount taken to Capital Reduction A/c.

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

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

Land & Building	= (85/100) x 5,40,000	= ₹ 4,59,000
Plant & Machinery	= (80/100) x 4,80,000	= ₹ 3,84,000
Reduced by:		
Land & Building	= (5,40,000 - 4,59,000)	= ₹ 81,000
Plant & Machinery	= (4,80,000 - 3,84,000)	= ₹ 96,000

QUESTION 47

Repair Ltd. is in the hands of a receiver for debenture holders who holds a charge on all assets except uncalled capital. The following statement shows the position as regards creditors as on 30th June, 20X1:

	₹
Property, plant and equipment (Cost₹ 3,90,000) - estimated at	1,50,000
Cash in hand of the receiver	2,70,000
Charged under debentures	4,20,000
Uncalled capital	1,80,000
Deficiency	7,50,000
6,000 shares of ₹ 60 each, ₹ 30 paid up	1,80,000
First debentures	3,00,000
Second debentures	6,00,000
Unsecured trade payables	4,50,000

A holds the first debentures for Rs. 3,00,000 and second debentures for Rs. 3,00,000. He is also an unsecured creditor for Rs. 90,000. B holds second debentures for Rs.3,00,000 and is an unsecured trade payables for Rs. 60,000. The following scheme of reconstruction is proposed:

1. A is to cancel Rs. 2,10,000 of the total debt owing to him, to bring Rs. 30,000 in cash and to take first debentures (in cancellation of those already issued to him) for Rs. 5,10,000 in satisfaction of all his claims.
2. B is to accept Rs. 90,000 in cash in satisfaction of all claims by him.
3. In full settlement of 75% of the claim, unsecured creditors (other than A and B) agreed to accept four shares of Rs. 7.50 each, fully paid against their claim for each share of Rs. 60. The balance of 25% is to be postponed and to be payable at the end of three years from the date of Court's approval of the scheme. The nominal share capital is to be increased accordingly.
4. Uncalled capital is to be called up in full and Rs. 52.50 per share cancelled, thus making the shares of Rs. 7.50 each.

Assuming that the scheme is duly approved by all parties interested and by the Court, give necessary journal entries.

Scanned with OKEN Scanner

SOLUTION:

Journal Entries

Particulars		Debit	Credit
First debentures A/c	Dr.	3,00,000	
Second debentures A/c	Dr.	3,00,000	
Unsecured creditors A/c	Dr.	90,000	
To A's A/c			6,90,000
(Being A's total liability ascertained)			
A's A/c	Dr.	2,10,000	
To Capital reduction A/c			2,10,000
(Being cancellation of debt upto ₹ 2,10,000)			
Bank A/c	Dr.	30,000	
To A's A/c			30,000
(Being cash received in course of settlement)			
A's A/c	Dr.	5,10,000	
To First debentures A/c			5,10,000
(Being liability of A, discharged against first debentures)			
Second debentures A/c	Dr.	3,00,000	
Unsecured creditors A/c	Dr.	60,000	
To B's A/c			3,60,000
(Being B's liability ascertained)			
B's A/c	Dr.	3,60,000	
To Bank A/c			90,000
To Capital reduction A/c			2,70,000
(Being B's liability discharged)			
Unsecured trade payables A/c	Dr.	3,00,000	
To Equity share capital A/c			1,12,500
To Loan (Unsecured) A/c			75,000
To Capital reduction A/c			1,12,500
(Being settlement of unsecured creditors)			
Share call A/c	Dr.	1,80,000	
To Share capital A/c			1,80,000
(Being final call money due)			
Bank A/c	Dr.	1,80,000	
To Share call A/c			1,80,000
(Being final call money received)			
Share capital A/c (Face value ₹ 60)	Dr.	3,60,000	
To Share capital (Face value ₹ 7.50)			45,000
To Capital reduction A/c			3,15,000
(Being share capital reduced to ₹ 7.50 each)			
Capital reduction A/c	Dr.	9,07,500	
To Profit and loss A/c			8,70,000
To Capital Reserve			37,500
(Being reconstruction surplus used to write off losses and balance transfer to capital reserve)			

Working Notes:

1.	Settlement of claim of remaining unsecured creditors	₹
	75% of ₹ 3,00,000	2,25,000
	Considering their claim for share of ₹ 60 each	
	2,25,000/60 =3,750 shares	
	Less: Number of shares to be issued	

Scanned with OKEN Scanner

	3,750 x 4= 15,000 shares of ₹ 7.5 each	
	Total value= 15,000 x 7.50	(1,12,500)
	Transferred to Capital reduction A/c	1,12,500

2. Ascertainment of profit and loss account's debit balance at the time of reconstruction.

	₹	₹
Asset		
Fixed assets	3,90,000	
Cash	2,70,000	6,60,000
Less: Capital & Liabilities:		
Share capital	1,80,000	
1st Debenture	3,00,000	
2nd Debenture	6,00,000	
Unsecured trade payables	4,50,000	(15,30,000)
Profit and loss A/c (Debit balance)		**(8,70,000)**

QUESTION 48

The summarised Balance Sheet of Preeti Limited as on 31st March 2019, was as follows:

	(Rs.)
Authorized and subscribed capital:	
20,000 Equity shares of Rs. 100 each fully paid	20,00,000
Unsecured loans:	
15% Debentures	6,00,000
Interest payable thereon	90,000
Current Liabilities:	
Trade payables	1,04,000
Provision for income tax	72,000
Property, plant and equipment:	
Machineries	7,00,000
Current Assets:	
Inventory	5,06,000
Trade receivables	4,60,000
Bank	40,000
Profit & loss A/c (Dr.)	11,60,000

It was decided to reconstruct the company for which necessary resolution was passed and sanctions were obtained from the appropriate authorities. Accordingly, it was decided that:

i) Each share be sub-divided into 10 fully paid up equity shares of Rs. 10 each.

ii) After sub-division, each shareholder shall surrender to the company 50% of his holding for the purpose of reissue to debenture holders and trade payables as necessary.

iii) Out of shares surrendered 20,000 shares of Rs. 10 each shall be converted into 10% Preference shares of Rs. 10 each fully paid up.

iv) The claims of the debenture holders shall be reduced by 50%. In consideration of the reduction, the debenture holder shall receive Preference Shares of Rs. 2,00,000 which are converted out of shares surrendered.

v) Trade payables claim shall be reduced by 25%. Remaining trade payables are to be settled by the issue of equity shares of Rs. 10 each out of shares surrendered.

vi) Balance of Profit and Loss account to be written off.

vii) The shares surrendered and not re-issued shall be cancelled.

Pass Journal Entries giving effect to the above.

Scanned with OKEN Scanner

SOLUTION:

Sr. No.	Particulars		Dr.	Cr.
1	Equity Share Capital A/c (Rs.10)	Dr.	20,00,000	
	To Share Surrender A/c			10,00,000
	To Equity Share Capital (Rs. 10) A/c			10,00,000
	(Sub-division of 20,000 equity shares of Rs. 100 each into 2,00,000 equity shares of Rs. 10 each and surrender of 1,00,000 of such sub-divided shares as per capital reduction scheme)			
2	15% Debentures Account	Dr.	3,00,000	
	Interest payable A/c (proportionate 50%)	Dr.	45,000	
	To Reconstruction A/c			3,45,000
	(Transferred 50% of the claims of the debenture holders to Reconstruction A/c in consideration of which 10% Preference shares are being issued, out of share surrender A/c as per capital reduction scheme)			
3	Trade payables A/c	Dr.	1,04,000	
	To Reconstruction A/c			1,04,000
	(Transferred claims of the trade payables to Reconstruction A/c, 25% of which is reduction and equity shares are issued in consideration of the balance amount)			
4	Share Surrender A/c	Dr.	10,00,000	
	To 10% Preference Share Capital A/c			2,00,000
	To Equity Share Capital A/c			78,000
	To Reconstruction A/c			7,22,000
	(Issued preference and equity shares to discharge the claims of the debenture holders and the trade payables respectively as per scheme and the balance in share surrender account is transferred to reconstruction account)			
5	Reconstruction A/c	Dr.	11,71,000	
	To Profit & Loss A/c			11,60,000
	To Capital Reserve A/c 11,000			11,000
	(Adjusted debit balance of profit and loss account against reconstruction account and the balance is transferred to Capital Reserve account)			

Note: Alternative set of correct journal entries may be given for transfer of surrendered shares to trade payables and debenture holders.

QUESTION 49

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

				Rs
A.	EQUITY & LIABILITIES			
	1.	Shareholders' Fund:		
		(a)	Share Capital:	
			9,000 7% Preference Shares of Rs 100 each fully paid	9,00,000
			10,000 Equity Shares of Rs 100 each fully paid	10,00,000
		(b)	Reserve & Surplus:	
			Profit & Loss Account	(2,00,000)
	2.	Non-current liabilities:		
			"A" 6% Debentures (Secured on Bombay Works)	3,00,000
			"B" 6% Debentures (Secured on Chennai Works)	3,50,000
	3.	Current Liabilities and Provisions:		
		(a)	Workmen's Compensation Fund:	
			Bombay Works	10,000
			Chennai Works	5,000
		(b)	Trade Payables	1,25,000

Scanned with OKEN Scanner

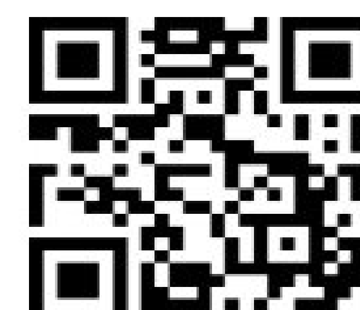
			TOTAL	**24,90,000**
B.	**ASSETS:**			
	Non- current Assets:			
	1.	**PPE:**		
			Bombay Works	9,50,000
			Chennai Works	7,75,000
	2.	**Investment:**		
			Investments for Workman's Compensation Fund	15,000
	3.	**Current Assets:**		
		(a)	Inventories	4,50,000
		(b)	Trade Receivables	2,50,000
		(c)	Cash at Bank	50,000
			TOTAL	**24,90,000**

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

1. Paid up value of 7% Preference Share to be reduced to Rs 80, but the rate of dividend being raised to 9%.
2. Paid up value of Equity Shares to be reduced to Rs 10.
3. The directors to refund Rs 50,000 of the fees previously received by them.
4. Debenture holders forego their interest of Rs 26,000 which is included among the trade payables.
5. The preference shareholders agreed to waive their claims for preference share dividend, which is in arrears for the last three years.
6. "B" 6% Debenture holders agreed to take over the Chennai Works of Rs 4,25,000 and to accept an allotment of 1,500 equity shares of Rs 10 each at par, and upon their forming a company called Zia Ltd. (to take over the Chennai Works) they allotted 9,000 equity shares of Rs 10 each fully paid at par to Star Ltd.
7. The Chennai Workmen's compensation fund disclosed that there were actual liabilities of Rs 1,000 only. As a consequence, the investments of the fund were realized to the extent of the balance. Entire investments were sold at a profit of 10% on book value and the proceeds were utilized for part payment of the creditors.
8. Inventory was to be written off by Rs 1,90,000 and a provision for doubtful debts is to be made to the extent of Rs 20,000.
9. Chennai works completely written off.
10. Any balance of the Capital Reduction Account is to be applied as two-third to write off the value of Bombay Works and one-third to Capital Reserve.

Pass necessary Journal Entries in the books of Star Ltd. after the scheme has been carried into effect.

QUESTION 50:



The Balance Sheet of A & Co. Ltd. as at 31-3-20X2 is as follows:

		Particulars	Notes	₹
		Equity and Liabilities		
1		**Shareholders' funds**		
	A	Share capital	1	11,50,000
	B	Reserves and Surplus	2	(5,35,000)
2		**Non-current liabilities**		
	A	Long-term borrowings	3	3,75,000
3		**Current liabilities**		
	A	Trade Payables		3,00,000
	B	Short term borrowings - Bank Overdraft		1,95,000
	C	Other current liabilities	4	1,22,500
		Total		**16,07,500**
		Assets		
1		**Non-current assets**		
	A	Property, plant and equipment	5	4,75,000

Scanned with OKEN Scanner

	B	Intangible assets	6	1,67,500
	C	Non-current investments	7	55,000
2		**Current assets**		
	A	Inventories		4,25,000
	B	Trade receivables		4,85,000
		Total		**16,07,500**

Notes to accounts

		₹
1	**Share Capital**	
	Equity share capital:	
	75,000 Equity Shares of ₹ 10 each	7,50,000
	Preference share capital:	
	4,000 6% Cumulative Preference Shares of ₹ 100 each	4,00,000
		11,50,000
2	**Reserves and Surplus**	
	Debit balance of Profit and loss Account	(5,35,000)
		(5,35,000)
3	**Long-term borrowings**	
	Secured	
	6% Debentures (secured on the freehold property)	3,75,000
		3,75,000
4	**Other current liabilities**	
	Loan from directors	1,00,000
	Interest payable on 6% debentures	22,500
		1,22,500
5	**Property plant and Equipment**	
	Freehold property	4,25,000
	Plant	50,000
		4,75,000
6	**Intangible assets**	
	Goodwill	1,30,000
	Patents	37,500
		1,67,500
7	**Non-current investments**	
	Investments at cost	55,000
		55,000

The Court approved a Scheme of re-organization to take effect on 1-4-20X2, whereby:

(i) The Preference shares to be written down to ₹ 75 each and Equity Shares to ₹ 2 each.

(ii) Of the Preference Share dividends which are in arrears for four years, three fourths to be waived and Equity Shares of ₹ 2 each to be allotted for the remaining quarter.

(iii) Interest payable on debentures to be paid in cash.

(iv) Debenture-holders agreed to take over freehold property, book value ₹ 1,00,000 at a valuation of ₹ 1,20,000 in part repayment of their holdings and to provide additional cash of ₹ 1,30,000 secured by a floating charge on company's assets at an interest rate of 8% p.a.

(v) Patents and Goodwill to be written off.

(vi) Inventory to be written off by ₹ 65,000.

(vii) Amount of ₹ 68,500 to be provided for bad debts.

(viii) Remaining freehold property after giving to debenture holders, to be re-valued at ₹ 3,87,500.

(ix) Investments be sold for ₹ 1,40,000.

(x) Directors to accept settlement of their loans as to 90% thereof by allotment of equity shares of ₹ 2 each and as to

Scanned with OKEN Scanner

5% in cash, and balance 5% being waived.

(xi) There were capital commitments totalling ₹ 2,50,000. These contracts are to be cancelled on payment of 5% of the contract price as a penalty.

(xii) Ignore taxation and cost of the scheme.

You are requested to show Journal entries reflecting the above transactions (including cash transactions) and prepare the Balance Sheet of the company after completion of the Scheme.

SOLUTION

Journal of A & Co. Ltd.

			Dr.	Cr.
			₹	₹
20X2	Equity Share Capital A/c (₹ 10)	Dr.	7,50,000	
April 1	To Capital Reduction A/c			6,00,000
	To Equity Share Capital A/c (₹ 2)			1,50,000
	(Reduction of equity shares of ₹ 10 each to shares of ₹ 2 each as per Reconstruction Scheme dated...)			
"	6% Cum. Preference Share Capital A/c (₹ 100)	Dr.	4,00,000	
	To Capital Reduction A/c			1,00,000
	To Pref. Share Capital A/c (₹ 75)			3,00,000
	(Reduction of preference shares of ₹ 100 each to shares of ₹ 75 each as per reconstruction scheme)			
"	Capital Reduction Account	Dr.	24,000	
	To Equity Share Capital Account			24,000
	(Arrears of preference dividends satisfied by the issue of equity shares, 25% of the amount due, ₹ 96,000)			
"	Freehold Property A/c	Dr.	82,500	
	To Capital Reduction A/c			82,500
	(Appreciation in the value of property:			
	Book value — Revalued Figure			
	₹ 1,00,000 — ₹ 1,20,000			
	₹ 3,25,000 — ₹ 3,87,500			
	Total **₹ 4,25,000** — **₹ 5,07,500**			
	Profit on revaluation: ₹ 82,500)			
"	6% Debentures A/c	Dr.	1,20,000	
	To Freehold Property A/c			1,20,000
	(Claims of debenture-holders, in part, in respect of principal discharged by transfer of freehold property vide Scheme of Reconstruction)			
"	Interest payable A/c	Dr.	22,500	
	To Bank A/c			22,500
	(Debenture interest paid)			
"	Bank A/c	Dr.	1,30,000	
	To 8% Debentures A/c			1,30,000
	(8% Debentures issued for cash)			
"	Bank A/c	Dr.	1,40,000	
	To Investment A/c			55,000
	To Capital Reduction A/c			85,000
	(Sale of Investment for ₹ 1,40,000 cost being ₹ 55,000; profit credited to Capital Reduction Account)			
"	Directors' Loan A/c	Dr.	1,00,000	
	To Equity Share Capital A/c			90,000
	To Bank A/c			5,000
	To Capital Reduction A/c			5,000

Scanned with OKEN Scanner

	(Directors' loan discharged by issue of equity shares of ₹ 90,000, cash payments of ₹ 5,000 and surrender of ₹ 5,000, vide Scheme of Reconstruction)			
"	Capital Reduction A/c	Dr.	8,48,500	
	To Patents			37,500
	To Goodwill			1,30,000
	To Inventory			65,000
	To Provision for Doubtful Debts			68,500
	To Bank			12,500
	To Profit & Loss Account			5,35,000
	(Writing off patents, goodwill, profit and loss account and reducing the value of stock, making the required provision for doubtful debts and payment for cancellation of capital commitments)			

Note: Penalty charges for cancellation of the contract amounts to ₹ 12,500 (2,50,000X5%) being paid in cash.

Balance Sheet of A & Co. Ltd. (And Reduced) as at 1st April, 20X2

		Particulars	Notes	₹
		Equity and Liabilities		
1		**Shareholders' funds**		
	A	Share capital	1	5,64,000
2		**Non-current liabilities**		
	A	Long-term borrowings	2	3,85,000
3		**Current liabilities**		
	A	Trade Payables		3,00,000
				12,49,000
		Assets		
1		**Non-current assets**		
	A	Property, plant and equipment	3	4,37,500
	B	Intangible assets	4	-
2		**Current assets**		
	A	Inventories		3,60,000
	B	Trade receivables	5	4,16,500
	C	Cash and cash equivalents		35,000
		Total		**12,49,000**

Notes to accounts

	Share Capital		
	Equity share capital		
	1,32,000 Equity shares of ₹ 2 each (of the above 57,000 shares have been issued for consideration other than cash)		2,64,000
	Preference share capital		
	4,000 6% Preference shares of ₹ 75 each		3,00,000
	Total		**5,64,000**
2	**Long-term borrowings**		
	Secured		
	6% Debentures		2,55,000
	8% Debentures		1,30,000
	Total		**3,85,000**
3	**Property, plant and equipment**		
	Freehold property	4,25,000	
	Add: Appreciation under scheme of Reconstruction	82,500	
	Less: Disposed of	(1,20,000)	3,87,500

Scanned with OKEN Scanner

	Plant		50,000
	Net carrying value		4,37,500
	Intangible assets		
	Goodwill	1,30,000	
	Less: Written off under scheme of Reconstruction	(1,30,000)	
	Net carrying value		**NIL**
4	**Patents**	**37,500**	
	Less: Written off under scheme of Reconstruction	(37,500)	-
	Net carrying value	-	**NIL**
5	**Trade Receivables**	**4,85,000**	
	Less: Provision for doubtful debts	68,500	
			4,16,500

Scanned with OKEN Scanner

9. AMALGAMATION OF COMPANIES

QUESTION 51

Sun and Neptune (both companies) had been carrying on business independently. They agreed to amalgamate and form a new company Jupiter Ltd. with an authorised share capital of Rs. 4,00,000 divided into 80,000 equity shares of Rs. 5 each. On 31st March, 2021 Sun and Neptune provide the following information:

	Sun (Rs.)	Neptune (Rs.)
Fixed Assets	6,35,000	3,65,000
Current Assets	3,27,000	1,67,750
	9,62,000	5,32,750
Less: Current Liabilities	(5,97,000)	(1,80,250)
Representing Capital	3,65,000	3,52,500

Additional Information:

a. Revalued figures of Fixed and Current assets were as follows:

	Sun (Rs.)	Neptune (Rs.)
Fixed Assets	7,10,000	3,90,000
Current Assets	2,99,500	1,57,750

b. The debtors and creditors include Rs. 43,350 owed by Sun to Neptune.

The purchase consideration is satisfied by issue of the following shares and debentures.

i. 60,000 equity shares of Jupiter Ltd. to Sun and Neptune in the proportion to the profitability of their respective business based on the average net profit during the last three years which were as follows:

	Sun (Rs.)	Neptune (Rs.)
2019 Profit	4,49,576	2,73,900
2020 (Loss)/Profit	(2,500)	3,42,100
2021 Profit	3,77,924	3,59,000

ii. 15% debentures in Jupiter Ltd. at par to provide an income equivalent to 8% return business as on capital employed in their respective business as on 31 st March, 2021 after revaluation of assets.

You are required to:

1. Compute the amount of debentures and shares to be issued to Sun and Neptune.
2. A Balance sheet of Jupiter Ltd. showing the position immediately after amalgamation.

SOLUTION

(1) Computation of Amount of Debentures and Shares to be issued:

		Sun	Neptune
		Rs.	Rs.
(i)	**Average Net Profit**		
	Rs. (4,49,576-2,500+3,77,924)/3	= 2,75,000	
	Rs. (2,73,900+,3,42,100+3,59,000)/3		= 3,25,000

II. Equity Shares Issued

a. Ratio of distribution

Sun	:	Neptune
275	:	325

b. Number

Sun	:	27,500
Neptune	:	32,500
		60,000

c. Amount

Scanned with OKEN Scanner

III) Capital Employed (after revaluation of Assets

	₹	₹
Property, plant and equipment	7,10,000	3,90,000
Current Assets	2,99,500	1,57,750
	10,09,500	5,47,750
Less: Current Liabilities	(5,97,000)	(1,80,250)
	4,12,500	**3,67,500**

iv) Debentures issued

	₹	₹
8% Return on capital employed	33,000	29,400
15% Debentures to be issued to provide equivalent income:		
Sun: 33,000 x 100/15	2,20,000	
Neptune: 29,400 x 100/15		1,96,000

(1) Balance Sheet of Jupiter Ltd.

As at 31st March 2021 (after amalgamation)

Particulars	Note No	Rs.
I. Equity and Liabilities		
(1) Shareholders' Funds		
(a) Share Capital	1	3,00,000
(b) Reserves and Surplus	2	64,000
(2) Non-Current Liabilities		
(a) Long-term borrowings	3	4,16,000
(3) Current Liabilities		
(a) Other current liabilities		7,33,900
Total		**15,13,900**
II. Assets		
(1) Non-current assets		
(a) Fixed assets		11,00,000
(2) Current assets		
(a) Other current assets		4,13,900
Total		**15,13,900**

Notes to Accounts

		Rs.
1	**Share Capital**	
	Authorized	4,00,000
	80,000 Equity Shares of Rs. 5 each	
	Issued and Subscribed	
	60,000 Equity Shares of Rs. 5 each	3,00,000
	(All the above shares are allotted as fully paid-up pursuant to a contract without payment being received in cash)	
2	**Reserve and Surplus**	
	Capital Reserve	64,000
3	**Long-term borrowings**	
	Secured Loans	
	15% Debentures	4,16,000

Scanned with OKEN Scanner

Working Notes:

		Sun	Neptune	Total
		Rs.	Rs.	Rs.
(1)	**Purchase Consideration**			
	Equity Shares Issued	1,37,500	1,62,500	3,00,000
	15% Debentures Issued	2,20,000	1,96,000	4,16,000
		3,57,500	3,58,500	7,16,000
(2)	**Capital Reserve**			
(a)	Net Assets taken over			
	Fixed Assets	7,10,000	3,90,000	11,00,000
	Current Assets	2,99,500	1,14,400*	4,13,900
		10,09,500	5,04,400	15,13,900
	Less: Current Liabilities	(5,53,650**)	(1,80,250)	(7,33,900)
		4,55,850	3,24,150	7,80,000
(b)	Purchase Consideration	3,57,500	3,58,500	7,16,000
(c)	Capital Reserve [(a) - (b)]	98,350		
(d)	Goodwill [(b) - (a)]		34,350	
(e)	Capital Reserve [Final Figure(c) -(d)]			64,000

* 1,57,750–43,350= 1,14,400

** 5,97,000–43,350= 5,53,650

QUESTION 52

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

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

Details of Trade receivables and trade payables are as under:

	VT Ltd. (Rs.)	MG Ltd. (Rs.)
Trade Receivable		
Debtors	7,20,000	3,80,000
Bills Receivable	1,20,000	40,000
	8,40,000	4,20,000
Trade Payables		
Sundry Creditors	4,40,000	2,50,000
Bills Payable	60,000	50,000
	5,00,000	3,00,000

Scanned with OKEN Scanner

Fixed Assets of both the companies are to be revalued at 15% above book value. Inventory in Trade and Debtors are taken over at 5% lesser than their book value.

Both the companies are to pay 10% equity dividend, Preference dividend having been already paid.

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

(i) VT Ltd. will issue 16 Equity Shares of Rs. 10 each at par against 12 Shares of MG Ltd.

(ii) 10% Preference Shareholders of MG Ltd. will be paid at 10% discount by issue of 10% Preference Shares of Rs. 100 each, at par, in VT. Ltd.

(iii) 12% Debenture holders of MG Ltd. are to be paid at 8% premium, by 12% Debentures in VT Ltd., issued at a discount of 10%.

(iv) Rs. 60,000 is to be paid by VT Ltd. to MG Ltd. for Liquidation expenses.

(v) Sundry Debtors of MG Ltd. includes Rs. 20,000 due from VT Ltd. You are required to

prepare:

(1) Journal entries in the books of VT Ltd.

(2) Statement of consideration payable by VT Ltd.

SOLUTION

Journal Entries in the Books of VT Ltd.

		Dr. Rs.	Cr. Rs.
Fixed Assets	Dr.	2,10,000	
To Revaluation Reserve			2,10,000
(Revaluation of fixed assets at 15% above book value)			
Reserve and Surplus	Dr.	1,20,000	
To Equity Dividend			1,20,000
(Declaration of equity dividend @ 10%)			
Equity Dividend	Dr.	1,20,000	
To Bank Account			1,20,000
(Payment of equity dividend)			
Business Purchase Account	Dr.	9,80,000	
To Liquidator of MG Ltd.			9,80,000
(Consideration payable for the business taken over from MG Ltd.)			
Fixed Assets (115% of Rs. 5,00,000)	Dr.	5,75,000	
Inventory (95% of Rs. 6,40,000)	Dr.	6,08,000	
Debtors	Dr.	3,80,000	
Bills Receivable	Dr.	40,000	
Investment	Dr.	1,60,000	
Cash at Bank	Dr.	20,000	
(Rs. 80,000 –Rs.60,000 dividend paid)			
To Provision for Bad Debts (5% of Rs. 3,60,000)			18,000
To Sundry Creditors			2,50,000
To 12% Debentures in MG Ltd.			3,24,000
To Bills Payable			50,000
To Business Purchase Account			9,80,000
To Capital Reserve (Balancing figure)			1,61,000
(Incorporation of various assets and liabilities taken over from MG Ltd. at agreed values & difference of net assets & purchase consideration being credited to capital reserve)			
Liquidator of MG Ltd.	Dr.	9,80,000	
To Equity Share Capital			8,00,000
To 10% Preference Share Capital			1,80,000
(Discharge of consideration for MG Ltd.'s business)			
12% Debentures in MG Ltd. (Rs. 3,00,000 × 108%)	Dr.	3,24,000	
Discount on Issue of Debentures	Dr.	36,000	
To 12% Debentures			3,60,000

Scanned with OKEN Scanner

(Allotment of 12% Debentures to debenture holders of MG Ltd. at a discount of 10%)			
Sundry Creditors To Sundry Debtors (Cancellation of mutual owing)	Dr.	20,000	20,000
Goodwill To Bank (Being liquidation expenses reimbursed to MG Ltd.)	Dr.	60,000	60,000
Capital Reserve/P&L A/c To Goodwill (Being goodwill set off)	Dr.	60,000	60,000

(ii) Statement of Consideration payable by VT Ltd. for 60,000 shares (payment method) Shares to be allotted 60,000/12 × 16 = 80,000 shares of VT Ltd.

Issued 80,000 shares of Rs. 10 each i.e. Rs. 8,00,000 (i)

For 10% preference shares, to be paid at 10% discount

Rs. 2,00,000x 90/100 Rs. 1,80,000 (ii)

QUESTION 53

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

Particulars	Note No.	Aakash Limited (Rs.)	Ganga Limited (Rs.)
I. Equity and Liabilities:			
(1) Shareholder's Funds:			
(a) Share Capital	1	80,00,000	20,00,000
(b) Reserves and Surplus	2	(3,24,00,000)	56,00,000
(2) Non-Current Liabilities:			
(a) Secured Loans	3	3,20,00,000	1,60,00,000
(b) Unsecured Loans	4	1,72,00,000	-
(3) Current Liabilities:			
(a) Trade Payables		56,00,000	36,00,000
(b) Other Current Liabilities	5	2,04,00,000	56,00,000
Total		**5,08,00,000**	**3,28,00,000**
II. Assets:			
(1) Non-Current Assets:			
Property, Plant & Equipment		68,00,000	1,36,00,000
(2) Current Assets:			
(a) Inventories		3,68,00,000	-
(b) Other Current Assets		72,00,000	1,92,00,000
Total		**5,08,00,000**	**3,28,00,000**

Notes to Accounts:

		Aakash Limited (Rs.)	Ganga Limited (Rs.)
1.	**Share Capital**		
	Authorized, Issued, Subscribed & Paid up:		
	6,00,000 Equity Shares of Rs.10 each	60,00,000	-

Scanned with OKEN Scanner

	20,000 Preference Shares of Rs. 100 each	20,00,000	-
	2,00,000 Equity Shares of Rs. 10 each	-	20,00,000
		80,00,000	**20,00,000**
2.	**Reserves and Surplus**		
	General Reserve	8,00,000	56,00,000
	Surplus	(3,32,00,000)	-
		(3,24,00,000)	**56,00,000**
3.	**Secured Loans** (Secured Loans of Aakash Limited are secured against pledge of Inventories)	3,20,00,000	1,60,00,000
4.	**Unsecured Loans**	**1,72,00,000**	-
5.	**Other Current Liabilities**		
	Statutory Liabilities	1,44,00,000	20,00,000
	Liability to Employees	60,00,000	36,00,000
		2,04,00,000	**56,00,000**

Both the companies go into liquidation and a new company 'Aakash Ganga Limited' is formed to take over their business. The following information is given:

(i) All Current Assets of two companies, except pledged inventory are taken over by Aakash Ganga Limited. The realizable value of all the Current Assets (including pledged inventory) is 80% of book value in case of Aakash Limited and 70% for Ganga Limited.

(ii) Property, Plant and Equipment of both the companies are taken over at book value by Aakash Ganga Limited.

(iii) Secured Loans include Rs. 32,00,000 accured interest in case of Ganga Limited.

(iv) 4,00,000 Equity Shares of Rs. 10 each are allotted by Aakash Ganga Limited at par against cash payment of entire face value to the shareholders of Aakash Limited and Ganga Limited in the ratio of shares held by them in Aakash Limited and Ganga Limited.

(v) Preference Shareholders in Aakash Limited are issued Equity Shares in AakashGanga Ltd. worth Rs. 4,00,000 in lieu of their present holdings.

(vi) Secured Loan agree to continue the balance amount of their loans to AakashGanga Limited after adjusting realizable value of pledged asset in case of Aakash Limited and after waiving 50% of interest due in the case of Ganga Limited.

(vii) Unsecured Loans are taken over by AakashGanga Limited at 25% of loan amounts.

(viii) Employees are issued fully paid Equity Shares in AakashGanga Limited in full settlement of their dues.

(ix) Statutory Liabilities are taken over by AakashGanga Limited at full value and Trade Payables are taken over at 80% of the book value.

You are required to prepare the opening Balance Sheet of AakashGanga Limited as at 1.4.2021.

SOLUTION

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

Particulars	Note No.	(Rs.)
I. Equity and Liabilities		
(1) Shareholders' Funds		
(a) Share Capital	1	1,40,00,000
(2) Non-Current Liabilities		
(a) Long term borrowings	2	2,12,60,000
(3) Current Liabilities		
(a) Trade Payables	3	73,60,000
(b) Other current liabilities	4	1,64,00,000
Total		**5,90,20,000**
II. Assets		

Scanned with OKEN Scanner

(1) Non-current assets		
(a) Property, Plant & Equipment	5	2,04,00,000
(b) Intangible assets	6	1,54,20,000
(2) Current assets		
(a) Cash and cash equivalents		40,00,000
(b) Other current assets	7	1,92,00,000
Total		**5,90,20,000**

Notes to Accounts

			(Rs.)
1.	**Share Capital**		
	Issued, subscribed & paid up:		
	14,00,000 equity shares of Rs. 10 each, fully paid up (W.N.4)		1,40,00,000
	(Of the above 10,00,000 shares have been issued for consideration other than cash)		
2.	**Long Term borrowings**		
	Secured Loans		
	Aakash Limited 25,60,000		
	Ganga Limited 1,44,00,000	1,69,60,000	
	Unsecured Loans	43,00,000	2,12,60,000
3.	**Trade Payables (W.N.1)**		
	Aakash Limited	44,80,000	
	Ganga Limited	28,80,000	73,60,000
4.	**Other current liabilities**		
	Statutory Liabilities		
	Aakash Limited	1,44,00,000	
	Ganga Limited	20,00,000	1,64,00,000
5.	**Property, Plant & Equipment**		
	Aakash Limited	68,00,000	
	Ganga Limited	1,36,00,000	2,04,00,000
6.	**Intangible assets**		
	Goodwill (W.N.3)		1,54,20,000
7.	**Other Current Assets**		
	Aakash Limited	57,60,000	
	Ganga Limited	1,34,40,000	1,92,00,000

Working Notes:

1. Value of total liabilities taken over by Aakash Ganga Ltd. (Rs.)

	Aakash Limited		**Ganga Limited**	
Current liabilities				
Statutory liabilities	1,44,00,000		20,00,000	
Liability to employees	60,00,000		36,00,000	
Trade payables @ 80%	44,80,000	2,48,80,000	28,80,000	84,80,000
Secured loans				
Given in Balance Sheet	3,20,00,000		1,60,00,000	
Interest waived	-		16,00,000	1,44,00,000
Value of Inventory (80% of Rs. 3,68,00,000)	2,94,40,000	25,60,000		

Scanned with OKEN Scanner

Unsecured Loans (25% of Rs.1,72,00,000)		43,00,000		-
		3,17,40,000		**2,28,80,000**

2. Assets taken over by Aakash Ganga Ltd. (Rs.)

	Aakash Limited	Ganga Limited
	Rs.	**Rs.**
Property, Plant & Equipment	68,00,000	1,36,00,000
Current Assets (80% and 70% respectively of book value)	57,60,000	1,34,40,000
	1,25,60,000	**2,70,40,000**

3. Goodwill / Capital Reserve on amalgamation (Rs.)

Liabilities taken over (W.N. 1)		3,17,40,000	2,28,80,000
Equity shares to be issued to Preference Shareholders		4,00,000	-
	A	3,21,40,000	2,28,80,000
Less: Total assets taken over (W.N. 2)	B	(1,25,60,000)	(2,70,40,000)
	A-B	1,95,80,000	(41,60,000)
		Goodwill	Capital Reserve
Net Goodwill (1,95,80,000- 41,60,000)		**1,54,20,000**	

4. Equity shares issued by Aakash Ganga Ltd.

(i)	For Cash		40,00,000
	For consideration other than cash		
(ii)	In Discharge of Liabilities to Employees	96,00,000	
(iii)	To Preference shareholders	4,00,000	1,00,00,000
			1,40,00,000
	No. of shares @ Rs. 10		**14,00,000**

QUESTION 54:

The following are the Balance Sheets of A Ltd. and B Ltd. as at 31.3.20X1:

		Particulars	Notes	₹ A Ltd (in'000)	₹ B Ltd (in'000)
		Equity and Liabilities			
1		**Shareholders' funds**			
	A	Share capital	1	2,000	1,000
	B	Reserves and Surplus	2	1,000	(800)
2		**Non-current liabilities**			
	A	Long-term borrowings	3	750	450
3		**Current liabilities**			
	A	Trade Payables		300	300
	B	Short term Borrowings – Bank overdraft		--	50
		Total		**4,050**	**1,000**
		Assets			
1		**Non-current assets**			
	A	Property, Plant and Equipment		2,700	850
	B	Non-current investments		700	--
2		**Current assets**			
	A	Trade receivables		400	150
	B	Cash and Cash equivalents (cash at bank)		250	--
		Total		**4050**	**1000**

Scanned with OKEN Scanner

Notes to Accounts

1	**Share capital**	**A Ltd. ('000)**	**B Ltd. ('000)**
	Equity shares of ₹ 100 each	2000	1000
		2000	**1000**
2	**Reserves and Surplus**		
	General reserve	1000	--
	Profit and loss A/c (debit balance)	--	(800)
		1000	**(800)**
3	**Long term borrowings**		
	10% debentures	500	--
	Loan from banks	250	450
		750	**450**

B Ltd. has acquired the business of A Ltd. The following scheme of merger was approved:

(i) Banks agreed to waive off the loan of ₹ 60 thousands of B Ltd.

(ii) B Ltd. will reduce its shares to ₹ 10 per share and then consolidate 10 such shares into one share of ₹ 100 each (new share).

(iii) Shareholders of A Ltd. will be given one share (new) of B Ltd. in exchange of every share held in A Ltd.

(iv) Trade payables of B Ltd. includes ₹ 100 thousands payable to A Ltd.

Pass necessary entries in the books of B Ltd. and prepare Balance Sheet after merger

SOLUTION:

Calculation of purchase consideration

One share of B Ltd. will be issued in exchange of every share of A Ltd. (i.e. 20,000 equity shares of B Ltd. will be issued against 20,000 equity shares of A Ltd.)	20,000 shares

Journal Entries in the books of B Ltd.

Date		(₹in thousands)	
20X1		**Dr. ₹**	**Cr. ₹**
March,31	Loan from bank A/c Dr.	60	
	To Capital reduction A/c		60
	(Being loan from bank waived off to the extent of ₹ 60 thousand)		
	Equity share capital A/c (₹ 100) Dr.	1,000	
	To Equity share capital A/c (₹10)		100
	To Capital reduction A/c		900
	(Being equity shares of ₹100 each reduced to ₹ 10 each)		
	Equity share capital A/c (₹ 10) Dr.	100	
	To Equity share capital A/c (₹ 100 each)		100
	(Being 10 equity shares of ₹ 10 each consolidated to one share of ₹100 each)		
	Capital reduction A/c Dr.	960	
	To Profit and loss A/c		800
	To Capital reserve A/c		160
	(Being accumulated losses set off against reconstruction A/c and balance transferred to capital reserve account)		
	Property, Plant & Equipment A/c Dr.	2,700	
	Investment A/c Dr.	700	
	Trade receivables A/c Dr.	400	
	Cash at bank A/c Dr.	250	
	To Trade payables A/c		300
	To Loans from bank A/c		250
	To 10% Debentures A/c		500
	To Business purchase A/c		2,000
	To Reserves A/c		1,000

Scanned with OKEN Scanner

	(Being assets, liabilities and reserves taken over under pooling of interest method)		
	Liquidator of A Ltd. A/c Dr. To Equity share capital A/c (Being payment made to liquidators of A Ltd. by allotment of 20,000 new equity shares)	2,000	2,000
	Trade payables A/c Dr. To Trade receivables A/c (Being mutual owing cancelled)	100	100

Balance Sheet of B Ltd. after merger as on 31.3.20X1

		Particulars	Notes	₹ in '000
		Equity and Liabilities		
1		**Shareholders' funds**		
	A	Share capital	1	2,100
	B	Reserves and Surplus	2	1,160
2		**Non-current liabilities**		
	A	Long term borrowings	3	1,140
3		**Current liabilities**		
	A	Trade payables		500
	B	Short term borrowings	4	50
		Total		**4,950**
		Assets		
1		**Non-current assets**		
	A	Property, Plant and Equipment		3,550
	B	Non-current investments		700
2		**Current assets**		
	A	Trade receivables		450
	B	Cash and cash equivalents		250
		Total		**4,950**

Notes to accounts

			₹ in '000
1	**Share Capital**		
	21,000, Equity shares of ₹ 100 each fully paid		2,100
	(Out of the above, 20,000 shares have been issued for consideration other than cash)		
2	**Reserves and Surplus**		
	Capital reserve	160	
	General reserve	1,000	
	Total		**1,160**
3	**Long Term Borrowings**		
	10% Debentures	500	
	Loan from Bank (250+450-60)	640	1,140
4	**Short term borrowings**		
	Bank overdraft		50

QUESTION 55

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

Scanned with OKEN Scanner

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

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

PQ Ltd. will issue:

- 5 Preference shares of Rs 20 each @ Rs 18 paid up at a premium of Rs 4 per share for each pref. share held in both the companies.
- 6 Equity shares of Rs 20 each @ Rs 18 paid up a premium of Rs 4 per share for each equity share held in both the companies.
- 6% Debentures to discharge the 8% debentures of both the companies.
- 20,000 new equity shares of Rs 20 each for cash @ Rs 18 paid up at a premium of Rs 4 per share.
- PQ Ltd. will pay cash to equity shareholders of both the companies in order to adjust their rights as per the intrinsic value of the shares of both the companies.

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

SOLUTION

In the Books of P Ltd.

Realization Account

		Rs			Rs
To	Land & Building	4,50,000	By	8% Debentures	2,00,000
To	Plant & Machinery	6,20,000	By	Trade Payables	88,000
To	Furniture & Fitting	1,00,000	By	PQ Ltd.	16,02,100
To	Trade receivables	3,25,000		(Purchase consideration)	
To	Inventory/Stock	2,33,000	By	Equity Shareholders A/c	1,37,900
To	Cash at Bank	2,08,000		(loss)	
To	Cash in Hand	54,000			
To	Preference shareholders (Excess payment)	38,000			
		20,28,000			**20,28,000**

Equity Shareholders Account

		Rs			Rs
To	Realization A/c (loss)	1,37,900	By	Share capital	8,20,000
To	Equity Shares in PQ Ltd.	10,82,400	By	Profit & Loss A/c	3,52,000
To	Cash	1,01,700	By	General Reserve	1,50,000
		13,22,000			**13,22,000**

9% Preference Shareholders Account

		Rs			Rs
To	Preference Share in PQ Ltd.	4,18,000	By	Pref. Share Capital	3,80,000

Scanned with OKEN Scanner

			By	Realization A/c	38,000
		4,18,000			**4,18,000**

PQ Ltd. Account

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

8% Debentures holders Account

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

Books of Q Ltd.

Realization Account

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

Equity Shareholders Account

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

9% Preference Shareholders Account

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

PQ Ltd. Account

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

8% Debentures holders Account

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

Scanned with OKEN Scanner

Working Notes:

(a) Purchase consideration

	P Ltd. Rs	Q Ltd. Rs
Payable to preference shareholders:		
Preference share at Rs 22 per share	418000	308000
Equity shares at Rs 22 per share	1082400	422400
Cash [see W.N. (ii)	101700	61850
	1602100	**792250**

(ii) Value of Net Assets

	P Ltd. Rs	Q Ltd. Rs
Land & Building	4,50,000	3,40,000
Plant & Machinery less 10% Depreciation	5,58,000	4,05,000
Furniture and fittings less 10% Dep	90,000	45,000
Trade Receivable less 5%	3,08,750	1,42,500
Inventory less 5%	2,21,350	99,750
Cash at Bank	2,08,000	1,75,000
Cash in Hand	54,000	20,000
Less: Debentures	(2,00,000)	(1,00,000)
Trade Payables	(88,000)	(1,60,000)
Secured Loans	0	(1,75,000)
	16,02,100	**7,92,250**
Payable in Shares	15,00,400	7,30,400
Payable in Cash*	1,01,700	61,850

(iii)		P	Q
	Plant &Machinery	6,20,000	4,50,000
	Less: Depreciation 10%	62,000	45,000
		5,58,000	4,05,000
	Furniture & Fixtures	1,00,000	50,000
	Less: Depreciation 10%	10,000	5,000
		90,000	**45,000**

*This cash is paid to equity shareholders of both the companies for adjustment of their rights as per intrinsic value of both companies.

QUESTION 56

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

Liabilities	Amount	Assets	Amount
8,000 Equity shares of 100 each	8,00,000	Building	3,40,000
10% Debentures	4,00,000	Machinery	6,40,000
Loans	1,60,000	Inventory	2,20,000
Trade payables	3,20,000	Trade receivables	2,60,000
General Reserve	80,000	Bank	1,36,000
		Patent	1,30,000
		Share issue Expenses	34,000
Total	**17,60,000**	**Total**	**17,60,000**

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

- B Ltd. would take over all assets, except bank balance and Patent at their book values less 10%. Goodwill is to be valued at 4 year's purchase of super profits, assuming that the normal rate of return be 8% on the combined amount of share capital and general reserve.
- B Ltd. is to take over trade payables at book value.

Scanned with OKEN Scanner

- The purchase consideration is to be paid in cash to the extent of 6,00,000/- and the balance in fully paid equity shares of 100/- each at 125/- per share.
- The average profit is Rs. 1,24,400.
- The liquidation expenses amounted to Rs. 16,000.
- B Ltd. sold prior to 31st March, 2018 goods costing Rs. 1,20,000 to A Ltd. for Rs. 1,60,000. Rs. 1,00,000 worth of goods are still in Inventory of A Ltd. on 31st March, 2018.
- Trade payables of A Ltd. include Rs. 40,000 still due to B Ltd.

Show the necessary Ledger Accounts to close the books of A Ltd. and prepare the Balance Sheet of B Ltd. as at 1st April, 2019 after the takeover.

SOLUTION

Books of A Limited

Realization Account

Particulars	Rs.	Particulars	Rs.
To Building	3,40,000	By Trade payables	3,20,000
To Machinery	6,40,000	By B Ltd.	12,10,000
To Inventory	2,20,000	By Equity Shareholders (Loss)	76,000
To Trade receivables	2,60,000		
To Patent	1,30,000		
To Bank (Exp.)	16,000		
	16,06,000		**16,06,000**

Bank Account

To Balance b/d	1,36,000	By Realization (Exp.)	16,000
To B Ltd.	6,00,000	By 10% Debentures	4,00,000
		By Loan	1,60,000
		By Equity shareholders	1,60,000
	7,36,000		**7,36,000**

Equity Share Holders Account

To Realization Account	76,000	Equity share capital	8,00,000
To Share issue Expenses	34,000	General reserve	80,000
To Equity shares in B Ltd.	6,10,000		
To Bank	1,60,000		
	8,80,000		**8,80,000**

B Ltd

Balance Sheet as on 1st April, 2019 (An extract)

	Particulars	Notes	Rs.
	EQUITY AND LIABILITIES		
1	**Shareholders' funds**		
a	Share capital	1	4,88,000
b	Reserves and Surplus	2	1,07,000
2	**Current liabilities**		
a	Trade Payables	3	2,80,000
b	Bank overdraft		6,00,000
			14,75,000
	ASSETS		
1	**Non-current assets**		
	Property, Plant and Equipment		
A	Tangible assets	4	8,82,000
B	Intangible assets	5	2,16,000

Scanned with OKEN Scanner

2	**Current assets**		
a	Inventories	6	1,83,000
b	Trade receivables	7	1,94,000
			14,75,000

Notes to Accounts

Sr. No.	Particulars		Rs.
1	**Share Capital**		
	Equity share capital		
	4,880 Equity shares of 100 each (Shares have been issued for consideration other than cash)		4,88,000
	Total		4,88,000
2	**Reserves and Surplus (an extract)**		
	Securities Premium		1,22,000
	Profit and loss account		
	Less: Unrealized profit	(15,000)	(15,000)
	Total		1,07,000
3	**Trade payables**		
	Opening balance	3,20,000	
	Less: Inter-company transaction cancelled upon amalgamation	(40,000)	2,80,000
4	**Tangible assets**		
	Buildings		3,06,000
	Machinery		5,76,000
	Total		8,82,000
5	**Intangible assets**		
	Goodwill		2,16,000
6	**Inventories**		
	Opening balance	1,98,000	
	Less: Cancellation of profit upon amalgamation	(15,000)	1,83,000
7	**Trade receivables**		
	Opening balance	2,34,000	
	Less: Intercompany transaction cancelled upon amalgamation	(40,000)	1,94,000

Working Notes:

1. Valuation of Goodwill	**Rs.**
Average profit	1,24,400
Less: 8% of Rs. 8,80,000	(70,400)
Super profit	54,000
Value of Goodwill = 54,000 x 4	2,16,000
1. Net Assets for purchase consideration	
Goodwill as valued in W.N.1	2,16,000
Building	3,06,000
Machinery	5,76,000
Inventory	1,98,000
Trade receivables (2,60,000-26,000)	2,34,000
Total Assets	15,30,000
Less: Trade payables	(3,20,000)
Net Assets	**12,10,000**

Scanned with OKEN Scanner

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

3. Unrealized Profit on Inventory	**Rs.**
The Inventory of A Ltd. includes goods worth Rs. 1,00,000 which was sold by B Ltd. on profit. Unrealized profit on this Inventory will be 40,000. 40000 x 100000 / 160000	25,000
As B Ltd purchased assets of A Ltd. at a price 10% less than the book value, 10% need to be adjusted from the Inventory i.e., 10% of Rs. 1,00,000.	(10,000)
Amount of unrealized profit	**15,000**

QUESTION 57

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

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

Notes to Accounts:

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

Scanned with OKEN Scanner

	Inventory	2,15,000	85,000
	Trade Receivables	2,02,500	1,75,000
	Cash and Cash equivalents	95,000	1,05,000
		5,12,500	**3,65,000**

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

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

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

SOLUTION

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

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

Notes to Accounts

		(Rs.)	(Rs.)
1.	**Share Capital**		
	1,31,375 Equity Shares of Rs. 10 each [1,00,000 + 31,375]		13,13,750
	(of the above shares, 31,375 shares were issued to the vendors otherwise than for cash)		
2.	**Reserves and surplus**		

Scanned with OKEN Scanner

	General Reserve		5,05,000	
	Profit and Loss A/c		4,45,000	
	Securities Premium [31,375 x 30]		9,41,250	
	Export profit reserve	1,85,000		
	Add: Balance of Myth Ltd.	25,000	2,10,000	
	Amalgamation Adjustment Reserve		(25,000)	20,76,250
3.	**Long Term Borrowings**			
	12% Debentures issued to Myth Ltd.			1,75,000
4.	**Trade payables**			
	Trade payables		90,000	
	Add: Taken over		1,42,000	2,32,000
5	**Other Current Liabilities**			
	Truth Ltd.		50,000	
	Myth Ltd.		40,000	90,000
6.	**Property, Plant & Equipment**			
	Truth Ltd.		15,75,000	
	Myth Ltd.		6,80,000	22,55,000
7.	**Investment**			
	Truth Ltd.		1,87,500	
	Myth Ltd.		1,00,000	2,87,500

Working Notes:

(1) Valuation of Goodwill

(i) Capital Employed

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

(ii) Average Profit before Tax

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

Scanned with OKEN Scanner

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

(2) Intrinsic Value per Share

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

** 1,50,000 x 14%/12% = 1,75,000

(3) Purchase Consideration & manner of its discharge

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

QUESTION 58

A Limited and B Limited are carrying on business of same nature. On 31 st March, 2021 the information given by both these companies is as follows:

	A Ltd. (Rs.)	B Ltd. (Rs.)
Share Capital		
- Equity Shares 10 each (Fully Paid)	12,00,000	7,20,000
- 10% Preference Shares of Rs. 100 each	6,00,000	-
- 8% Preference Shares of Rs. 100 each	-	5,00,000
General Reserve	3,00,000	2,50,000
Investment Allowance Reserve	-	60,000
Security Premium	2,40,000	-
Export Profit Reserve	1,80,000	1,20,000
Profit & Loss Account	2,16,000	1,92,000
9% Debentures (Rs. 10 each)	3,00,000	2,00,000
Secured Loan	-	3,60,000
Sundry Creditors	3,12,000	2,04,000
Bills Payable	75,000	1,00,000
Other Current Liabilities	50,000	75,000
Land and Building	10,80,000	8,40,000
Plant and Machinery	6,00,000	5,60,000

Scanned with OKEN Scanner

Office Equipment	3,45,000	2,10,000
Investments	96,000	3,00,000
Stock in Trade	6,30,000	4,20,000
Sundry Debtors	4,90,000	3,20,000
Bills Receivables	60,000	70,000
Cash at Bank	1,72,000	61,000

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

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

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

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

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

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

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

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

SOLUTION

Journal Entries in the books of A Ltd.

Particulars		Debit Rs.	Credit Rs.
Business purchase A/c (W.N.1)	Dr.	13,75,000	
To Liquidator of B Ltd.			13,75,000
(Being business of B Ltd. taken over)			
Land & Building A/c	Dr.	8,40,000	
Plant and machinery A/c	Dr.	5,60,000	
Office equipment A/c	Dr.	2,10,000	
Investments A/c	Dr.	3,00,000	
Inventory A/c	Dr.	4,20,000	
Debtors A/c	Dr.	3,20,000	
Bills receivables A/c	Dr.	70,000	
Bank A/c	Dr.	61,000	
To General reserve A/c (W.N.2) (2,50,000-1,55,000)			95,000
To Export profit reserve A/c			1,20,000
To Investment allowance reserve A/c			60,000
To Profit and loss A/c			1,20,000
To Liability for 9% Debentures A/c (Rs. 100 each)			2,00,000
To Secured Loan			3,60,000
To Trade creditors A/c			2,76,000
To Bills payables A/c			1,00,000
To Other current liabilities A/c			75,000
To Business purchase A/c			13,75,000
(Being assets and liabilities taken over)			
Liquidator of B Ltd.	Dr.	13,75,000	
To Equity share capital A/c			8,00,000

Scanned with OKEN Scanner

To 10% Preference share capital A/c			4,00,000
To Securities premium A/c			1,75,000
(Being purchase consideration discharged)			
General Reserve* A/c	Dr.	12,000	
To Cash at bank			12,000
(Being expenses of amalgamation paid)			
Liability for 9% Debentures in B Ltd. A/c	Dr.	2,00,000	
To 9% Debentures A/c			2,00,000
(Being debentures in B ltd. discharged by issuing own 9% debentures)			
Bills payables A/c	Dr.	60,000	
To Bill receivables A/c (Cancellation of mutual owing on account of bills of exchange)			60,000

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

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

	Particulars	Notes	Rs.
	Equity and Liabilities		
1	**Shareholders' funds**		
a	Share capital	1	30,00,000
b	Reserves and Surplus	2	14,94,000
2	**Non-current liabilities**		
a	Long-term borrowings	3	8,60,000
3	**Current liabilities**		
a	Trade Payables	4	7,03,000
b	Other current liabilities	5	1,25,000
	Total		**61,82,000**
	Assets		
1	**Non-current assets**		
a	PPE	6	36,35,000
b	Investments	7	3,96,000
2	**Current assets**		
a	Inventories	8	10,50,000
b	Trade receivables	9	8,80,000
c	Cash and cash equivalents	10	2,21,000
	Total		**61,82,000**

Notes to accounts

			Rs.
1	**Share Capital**		
	Equity share capital		
	2,00,000 Equity shares of Rs. 10 each (Out of above, 80,000 shares were issued for consideration other than cash)		20,00,000
	Preference share capital		
	10,000 10% Preference shares of Rs. 100 each (Out of above, 4,000 shares were issued for consideration other than cash)		10,00,000
	Total		**30,00,000**
2	**Reserves and Surplus**		

Scanned with OKEN Scanner

	General Reserve		
	Opening balance	3,00,000	
	Add: Adjustment under scheme of amalgamation	95,000	
	Less: Amalgamation expense paid	(12,000)	3,83,000
	Securities premium (2,40,000+1,75,000)		4,15,000
	Export profit reserve		
	Opening balance	1,80,000	
	Add: Adjustment under scheme of amalgamation	1,20,000	3,00,000
	Investment allowance reserve		60,000
	Profit and loss account		
	Opening balance	2,16,000	
	Add: Adjustment under scheme of amalgamation	1,20,000	3,36,000
	Total		**14,94,000**
3	**Long-term borrowings**		
	Secured		
	9% Debentures	3,00,000	
	Add: Adjustment under scheme of amalgamation	2,00,000	
	Secured loan	3,60,000	8,60,000
4	**Trade payables**		
	Creditors: Opening balance	3,12,000	
	Add: Adjustment under scheme of amalgamation	2,76,000	5,88,000
	Bills Payables: Opening balance	75,000	
	Add: Adjustment under scheme of amalgamation	1,00,000	
	Less: Cancellation of mutual owning upon amalgamation	(60,000)	1,15,000
			7,03,000
5	**Other current liabilities**		
	Opening balance	50,000	
	Add: Adjustment under scheme of amalgamation	75,000	1,25,000
6	**PPE**		
	Land & Building- Opening balance	10,80,000	
	Add: Adjustment under scheme of amalgamation	8,40,000	19,20,000
	Plant and machinery- Opening balance	6,00,000	
	Add: Adjustment under scheme of amalgamation	5,60,000	11,60,000
	Office equipment- Opening balance	3,45,000	
	Add: Adjustment under scheme of amalgamation	2,10,000	5,55,000
	Total		**36,35,000**
7	**Investments**		
	Opening balance	96,000	
	Add: Adjustment under scheme of amalgamation	3,00,000	3,96,000
8	**Inventories**		
	Opening balance	6,30,000	
	Add: Adjustment under scheme of amalgamation	4,20,000	10,50,000
9	**Trade receivables**		
	Debtors: Opening balance	4,90,000	
	Add: Adjustment under scheme of amalgamation	3,20,000	8,10,000
	Bills Payables: Opening balance	60,000	
	Add: Adjustment under scheme of amalgamation	70,000	
	Less: Cancellation of mutual owning upon amalgamation	(60,000)	70,000
	Total		**8,80,000**
10	**Cash and cash equivalents**		

Scanned with OKEN Scanner

	Opening balance	1,72,000	
	Add: Adjustment under scheme of amalgamation	61,000	
	Less: Amalgamation expense paid	(12,000)	**2,21,000**

Working Notes:

1. Calculation of purchase consideration

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

2. Amount to be adjusted from general reserve

The difference between the amount recorded as share capital issued and the amount of share capital of transferor company should be adjusted in General Reserve.

Thus, General reserve will be adjusted as follows:

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

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

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

QUESTION 59

The financial position of X Ltd. and Y Ltd. as on 31st March, 2018 was as under:

	X Ltd. (Rs)	Y Ltd. (Rs)
Equity and Liabilities		
Equity Shares of Rs 10 each	30,00,000	9,00,000
9% Preference Shares of Rs 100 each	3,00,000	-
10% Preference Shares of Rs 100 each	-	3,00,000
General Reserve	2,10,000	2,10,000
Retirement Gratuity Fund (long term)	1,50,000	60,000
Trade Payables	3,90,000	2,40,000
Total	**40,50,000**	**17,10,000**
Assets		
Goodwill	1,50,000	75,000
Land & Buildings	9,00,000	3,00,000
Plant & Machinery	15,00,000	4,50,000
Inventories	7,50,000	5,25,000
Trade Receivables	6,00,000	3,00,000
Cash and Bank	1,50,000	60,000
Total	**40,50,000**	**17,10,000**

X Ltd. absorbs Y Ltd. on the following terms:

(i) 10% Preference Shareholders are to be paid at 10% premium by issue of 9% Preference Shares of X Ltd.

(ii) Goodwill of Y Ltd. on absorption is to be computed based on two times of average profits of preceding three financial years (2016-17: Rs 90,000; 2015-16: Rs 78,000 and 2014-15: Rs 72,000). The profits of 2014 -15 included credit of an insurance claim of Rs 25,000 (fire occurred in 2013-14 and loss by fire Rs 30,000 was booked

Scanned with OKEN Scanner

in Profit and Loss Account of that year). In the year 2015 -16, there was an embezzlement of cash by an employee amounting to Rs 10,000.

(iii) Land & Buildings are valued at Rs 5,00,000 and the Plant & Machinery at Rs 4,00,000.

(iv) Inventories are to be taken over at 10% less value and Provision for Doubtful Debts is to be created @ 2.5%.

(v) There was an unrecorded current asset in the books of Y Ltd. whose fair value amounted to Rs 15,000 and such asset was also taken over by X Ltd.

(vi) The trade payables of Y Ltd. included Rs 20,000 payable to X Ltd.

(vii) Equity Shareholders of Y Ltd. will be issued Equity Shares @ 5% premium.

You are required to

(i) Prepare Realisation A/c in the books of Y Ltd.

(ii) Show journal entries in the books of X Ltd.

(iii) Prepare the Balance Sheet of X Ltd. after absorption as at 31st March,2018.

SOLUTION

In the Books of Y Ltd. Realisation Account

	Rs			Rs
To Sundry Assets:			By Retirement Gratuity Fund	60,000
Goodwill	75,000			
Land & Building	3,00,000		By Trade payables	2,40,000
Plant & Machinery	4,50,000		By X Ltd. (Purchase	15,90,000
Inventory	5,25,000		Consideration)	
Trade receivables	3,00,000			
Bank	60,000	17,10,000		
To Preference Shareholders		30,000		
(Premium on Redemption)				
To Equity Shareholders				
(Profit on Realisation)		1,50,000		
		18,90,000		**18,90,000**

In the Books of X Ltd. Journal Entries

		Dr. Rs	Cr. Rs
Business Purchase A/c	Dr.	15,90,000	
To Liquidators of Y Ltd. Account (Being business of Y Ltd. taken over)			15,90,000
Goodwill Account	Dr.	1,50,000	
Land & Building Account	Dr.	5,00,000	
Plant & Machinery Account	Dr.	4,00,000	
Inventory Account	Dr.	4,72,500	
Trade receivables Account	Dr.	3,00,000	
Bank Account	Dr.	60,000	
Unrecorded assets Account	Dr.	15,000	
To Retirement Gratuity Fund Account			60,000
To Trade payables Account			2,40,000
To Provision for Doubtful Debts Account			7,500
To Business Purchase A/c (Being Assets and Liabilities taken over as per agreed valuation).			15,90,000
Liquidators of Y Ltd. A/c	Dr.	15,90,000	
To 9% Preference Share Capital A/c			3,30,000
To Equity Share Capital A/c			12,00,000
To Securities Premium A/c (Being Purchase Consideration satisfied as above).			60,000

Scanned with OKEN Scanner

Balance Sheet of X Ltd. (after absorption) as at 31st March, 2018

Particulars		Notes	Rs
Equity and Liabilities			
1	Shareholders' funds		
A	Share capital	1	48,30,000
B	Reserves and Surplus	2	2,70,000
2	**Non-current liabilities**		
A	Long-term provisions	3	2,10,000
3	**Current liabilities**		
A	Trade Payables	4	6,10,000
B	Short term provision	5	7,500
Total			59,27,500
Assets			
1	**Non-current assets**		
A	Fixed assets		
Tangible assets		6	33,00,000
Intangible assets		7	3,00,000
2	**Current assets**		
A	Inventories	8	12,22,500
B	Trade receivables	9	8,80,000
C	Other current Assets	10	15,000
D	Cash and cash equivalents	11	2,10,000
Total			**59,27,500**

Notes to accounts

		Rs
1	**Share Capital**	
Equity share capital		
4,20,000 Equity Shares of Rs. 10 each fully paid (Out of above 1,20,000 Equity Shares were issued in consideration other than for cash)		42,00,000
Preference share capital		
6,300 9% Preference Shares of Rs. 100 each (Out of above 3,300 Preference Shares were issued in consideration other than for cash)		6,30,000
Total		48,30,000
2	**Reserves and Surplus**	
Securities Premium		60,000
General Reserve		2,10,000
Total		2,70,000
3	**Long-term provisions**	
Retirement Gratuity fund		2,10,000
4	**Trade payables** (3,90,000 + 2,40,000 - 20,000*) *** Mutual Owings eliminated.**	6,10,000
5	**Short term Provisions**	
Provision for Doubtful Debts		7,500
6	**Tangible assets**	
Land & Buildings		14,00,000
Plant & Machinery		19,00,000
Total		**33,00,000**
7	**Intangible assets**	
Goodwill (1,50,000 +1,50,000)		3,00,000
8	**Inventories** (7,50,000 + 4,72,500)	12,22,500
9	**Trade receivables** (6,00,000 + 3,00,000 - 20,000)	8,80,000

Scanned with OKEN Scanner

10	**Other current Assets**	15,000
11	**Cash and cash equivalents** (1,50,000 +60,000)	2,10,000

Working Notes:

1. Computation of goodwill **Rs**

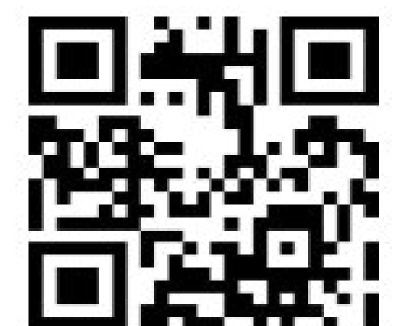
Profit of 2016-17	90,000
Profit of 2015-16 adjusted Rs 78,000 + 10,000)	88,000
Profit of 2014-15 adjusted (Rs 72,000 – 25,000)	47,000
	2,25,000
Average profit	**75,000**

Goodwill to be valued at 2 times of average profits = Rs 75,000 x 2 = RS 1,50,000

2.

Purchase Consideration:		**Rs**
Goodwill		1,50,000
Land & Building		5,00,000
Plant & Machinery		4,00,000
Inventory		4,72,500
Trade receivables		3,00,000
Unrecorded assets		15,000
Cash at Bank		60,000
		18,97,500
Less: Liabilities:		
Retirement Gratuity	60,000	
Trade payables Provision for doubtful debts	2,40,000 7,500	(3,07,500)
Net Assets/ Purchase Consideration		15,90,000
To be satisfied as under:		
10% Preference Shareholders of Y Ltd.		3,00,000
Add: 10% Premium		30,000
9% Preference Shares of X Ltd.		3,30,000
Equity Shareholders of Y Ltd. to be satisfied by issue of 1,20,000		
equity Shares of X Ltd. at 5% Premium		12,60,000
Total		**15,90,000**

QUESTION 60



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

	Rs.
Share capital:	
Equity shares of Rs. 10 each	3,00,000
6,000, 9% cumulative preference shares of Rs. 10 each	60,000
Profit and Loss Account (Dr. balance)	1,70,000
10% Debentures of Rs. 100 each	2,00,000
Interest payable on Debentures	20,000
Trade Payables	1,50,000
Property, Plant and Equipment	3,40,000
Goodwill	10,000
Inventory	80,000
Trade Receivables	1,10,000
Bank Balance	20,000

Scanned with OKEN Scanner

A new company Ravi Ltd. is formed with authorised share capital of Rs. 4,00,000 divided into 40,000 Equity Shares of Rs. 10 each. The new company will acquire the assets and liabilities of Mohan Ltd. on the following terms:

i)

a) Mohan Ltd.'s debentures are paid by similar debentures in new company and for outstanding accrued interest on debentures, equity shares of equal amount are issued at par.

b) The trade payables are paid by issue of 12,000 equity shares at par in full and final settlement of their claims.

c) Preference shareholders are to get equal number of equity shares issued at par. Dividend on preference shares is in arrears for three years. Preference shareholders to forgo dividend for two years. For balance dividend, equity shares of equal amount are issued at par.

d) Equity shareholders are issued one share at par for every three shares held in Mohan Ltd.

ii) Current Assets are to be taken at book value (except inventory, which is to be reduced by 10%). Goodwill is to be eliminated. The Property, plant and equipment is taken over at Rs. 3,08,400.

iii) Remaining equity shares of the new company are issued to public at par fully paid up.

iv) Expenses of Rs. 5,000 to be met from bank balance of Mohan Ltd. This is to be adjusted from the bank balance of Mohan Ltd. before acquisition by Ravi Ltd.

You are required to prepare:

(a) Realisation account and Equity Shareholders' account in the books of Mohan Ltd.

(b) Bank Account and Balance Sheet with notes to accounts in the books of Ravi Ltd.

SOLUTION

In the books of Mohan Ltd.

i) Realisation Account

	Rs.		Rs.
To Goodwill	10,000	By 10% Debentures	2,00,000
To Property, plant and Equipment	3,40,000	By Interest accrued on	20,000
To Inventory	80,000	By Trade payables	1,50,000
To Trade receivables	1,10,000	By Ravi Ltd. (Purchase consideration) (W.N. 1)	1,65,400
To Bank (20,000 - 5,000)	15,000	By Equity shareholders A/c (loss on realization) (Bal. fig.)	25,000
To Preference shareholders A/c (W.N.2)	5,400		
	5,60,400		**5,60,400**

ii) Equity shareholders' Account

	Rs.		Rs.
To Profit & loss A/c	1,70,000	By Equity Share capital	3,00,000
To Expenses*	5,000		
To Equity shares in Ravi Ltd.	1,00,000		
To Realization A/c	25,000		
	3,00,000		**3,00,000**

*Alternatively, expenses may be routed through Realization account.

In the books of Ravi Ltd.

i) Bank Account

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

ii) Balance Sheet as at 31st March, 2020

Particulars	Note No.	Rs.
I. Equity and Liabilities		
(1) Shareholder's Funds		

Scanned with OKEN Scanner

Share Capital	1	4,00,000
(2) Non-Current Liabilities		
Long-term borrowings	2	2,00,000
Total		**6,00,000**
II. Assets		
(1) Non-current assets		
(a) Property, plant and equipment		3,08,400
(2) Current assets		
(a) Inventories		72,000
(b) Trade receivables		1,10,000
(c) Cash and cash equivalents		1,09,600
Total		**6,00,000**

Notes to Accounts

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

Working Notes:

1. **Calculation of Purchase consideration**

	Rs.
Payment to preference shareholders	
6,000 equity shares @ Rs. 10	60,000
For arrears of dividend: (6,000 x Rs. 10) x 9%	5,400
Payment to equity shareholders	
(30,000 shares x 1/3) @ Rs. 10	1,00,000
Total purchase consideration	1,65,400

2. **Preference shareholders' Account in books of Mohan Ltd.**

	Rs.		**Rs.**
To Equity Shares in Ravi Ltd.	65,400	By Preference Share capital	60,000
		By Realization A/c (Bal. fig.)	5,400
	65,400		**65,400**

3. **Calculation of number of Equity shares issued to public**

	Number of shares	
Authorized equity shares		40,000
Less: Equity shares issued for		
Interest accrued on debentures	2,000	
Trade payables of Mohan Ltd.	12,000	
Preference shareholders of Mohan Ltd.	6,000	
Arrears of preference dividend	540	
Equity shareholders of Mohan Ltd.	10,000	(30,540)
Number of equity shares issued to public at par for cash		9,460

Scanned with OKEN Scanner

10. AS – 15 EMPLOYEE BENEFITS

QUESTION 61

An employee Roshan has joined a company XYZ Ltd. in the year 20X1. The annual emoluments of Roshan as decided is ₹14,90,210. The company also has a policy of giving a lump sum payment of 25% of the last drawn annual salary of the employee for each completed year of service if the employee retires after completing minimum 5 years of service. The salary of the Roshan is expected to grow @ 10% per annum.

The company has inducted Roshan in the beginning of the year and it is expected that he will complete the minimum five year term before retiring. Thus he will get 5 yearly increment.

What is the amount the company should charge in its Profit and Loss account every year as cost for the Defined Benefit obligation? Also calculate the current service cost and the interest cost to be charged per year assuming a discount rate of 8%.

(P.V factor for 8% - 0.735, 0.794, 0.857, 0.926, 1)

Solution

Calculation of Defined Benefit Obligation (DBO)

Expected last drawn salary	₹ 14,90,210 x 110% x 110% x 110% x 110% x 110%	**₹24,00,000**
Defined Benefit Obligation (DBO)	₹ 24,00,000 x 25% x 5	**₹30,00,000**

Amount of ₹ 6,00,000 will be charged to Profit and Loss Account of the company every year as cost for Defined Benefit Obligation.

Calculation of Current Service Cost

Year	Equal apportioned amount of DBO [i.e. ₹ 30,00,000/5 years]	Discounting @ 8% PV factor	Current service cost (Present Value)
a	B	c	d = b× c
1	6,00,000	0.735 (4 Years)	4,41,000
2	6,00,000	0.794 (3 Years)	4,76,400
3	6,00,000	0.857 (2 Years)	5,14,200
4	6,00,000	0.926 (1 Year)	5,55,600
5	6,00,000	1 (0 Year)	6,00,000

Calculation of Interest Cost to be charged per year

	Opening balance	Interest cost	Current service cost	Closing balance
a	B	C =b×8%	d	e = b + c + d
1	0	0	4,41,000	4,41,000
2	4,41,000	35,280	4,76,400	9,52,680,
3	9,52,680	76,214	5,14,200	15,43,094
4	15,43,094	1,23,447	5,55,600	22,22141
5	22,22,141	1,77,859*	6,00,000	30,00,000

*Due to approximations used in calculation, this figure is adjusted accordingly

Assume in **Q. 101** at Beginning of 3rd year. There is a change in Actuarial Assumptions & due to such Change the Revised Estimated DBO Liability at Beginning of 3rd year is Rs. 10,10,000/-

Solution:

Carrying Amt of DBO Payable at 2nd year. end/3rd Year Beginning	9,52,680
Revised Balance of DBO Payable	10,10,000
Increase in DBO Liability (Actuarial Loss)	57,320

	Dr	Cr
Actuarial Loss (P&L) Dr	57,230	
To DBO Payable A/c		57,230

Scanned with OKEN Scanner

Further Current Service Cost and Interest Cost from 3rd Year onwards will also be Revised based on New Revised Liability.

QUESTION 62

As on 1st April, 20X1 the fair value of plan assets was ₹1,00,000 in respect of a pension plan of Zeleous Ltd. On 30th September, 20X1 the plan paid out benefits of ₹19,000 and received inward contributions of ₹49,000. On 31st March, 20X2 the fair value of plan assets was ₹1,50,000 and present value of the defined benefit obligation was ₹1,47,920. Actuarial losses on the obligations for the year 20X1- 20X2 were ₹600.

On 1st April, 20X1, the company made the following estimates, based on its market studies, understanding and prevailing prices

	%
Interest & dividend income, after tax payable by the fund	9.25
Realised and unrealised gains on plan assets (after tax)	2.00
Fund administrative costs	(1.00)
Expected Rate of Return	**10.25**

You are required to find the expected and actual returns on plan assets.

Solution

Computation of Expected and Actual Returns on Plan Assets

		₹
Return on ₹ 1,00,000 held for 12 months at 10.25%		10,250
Return on ₹ 30,000 (49,000-19,000) held for six months at 5% (equivalent to 10.25% annually, compounded every six months)		1,500
Expected return on plan assets for 20X1-20X2		**11,750**
Fair value of plan assets as on 31 March, 20X2		1,50,000
Less: Fair value of plan assets as on 1 April,20X1	1,00,000	
Contributions received	49,000	(1,49,000)
		1,000
Add: Benefits paid		19,000
Actual return on plan assets		**20,000**

Alternatively, the above question may be solved without giving compound effect to rate of return.

QUESTION 63

Rock Star Ltd. discontinues a business segment. Under the agreement with employee's union, the employees of the discontinued segment will earn no further benefit. This is a curtailment without settlement, because employees will continue to receive benefits for services rendered before discontinuance of the business segment. Curtailment reduces the gross obligation for various reasons including change in actuarial assumptions made before curtailment. If the benefits are determined based on the last pay drawn by employees, the gross obligation reduces after the curtailment because the last pay earlier assumed is no longer valid.

Rock Star Ltd. estimates the share of unamortized service cost that relates to the part of the obligation at ₹ 18 (10% of ₹180). Calculate the gain from curtailment and liability after curtailment to be recognised in the balance sheet of Rock Star Ltd. on the basis of given information:

- Immediately before the curtailment, gross obligation is estimated at ₹6,000 based on current actuarial assumption.
- The fair value of plan assets on the date is estimated at ₹5,100.
- The unamortized past service cost is ₹180.
- Curtailment reduces the obligation by ₹600, which is 10% of the gross obligation.

Scanned with OKEN Scanner

Solution

Gain from curtailment is estimated as under:

	₹
Reduction in gross obligation	600
Less: Proportion of un-amortised past service cost	(18)
Gain from curtailment	**582**

The liability to be recognised after curtailment in the balance sheet is estimated as under:

	₹
Reduced gross obligation (90% of ₹ 6,000)	5,400
Less: Fair value of plan assets	(5,100)
Less: Un-amortised past service cost (90% of ₹180)	300
Liability to be recognised in the balance sheet	(162)
Liability to be recognised in the balance sheet	**138**

QUESTION 64

Balance of Present Value of Defined Benefit Obligations 15,00,000

Balance of Plan Assets 10,00,000

Actuary Report Specifies:

Current Service Costs 3,00,000

Interest Cost 20,000

Contributions to Plan Assets at the Mid of Year 1,50,000

Benefit Paid at the mid of year 2,40,000

Expected Return 12% p.a.

Closing Value of Present Value of Defined Benefit Obligations 17,00,000

Closing Value of Plan Assets at Fair Value 10,20,000

Journalise, Prepare ledgers and Extracts of Balance sheet and Profit and Loss account along with disclosures.

Solution:

DOB Payable a/c			
To Bank (Benefits)	2,40,000	By Opening Balance	15,00,000
		By Current Service Cost	30,00,000
		By Interest Cost	20,000
By Closing Balance	17,00,000	By Actuarial Loss (b/f)	1,20,000
Plan Asset			
To Opening Balance	10,00,000	By Bank A/c	2,40,000
To Bank	1,50,000	By Acturrial Loss B/F	
To Expected Return	1,14,753		
(a)1,20,000			
(b)5,247		By Closing Balance	10,20,000

QUESTION 65

Mr. Rajan is working for Infotech Ltd. Consider the following particulars:

Annual salary of Mr. Rajan = ₹ 30,00,000

Total working days in 20X0-X1 = 300 days

Leaves allowed in 20X0-X1 as per company policy = 10 days

Leaves utilized by Mr. Rajan in 20X0-X1 = 8 days

The unutilized leaves are settled by way of payment and accordingly, carry forward of such leaves to the subsequent period is not allowed.

Scanned with OKEN Scanner

Compute the total employee benefit expense for Infotech Ltd. in respect of 20X0-X1.

SOLUTION

Mr Rajan is entitled to a salary of ₹ 30,00,000 for 300 total working days.

Thus, per day salary works out to ₹ 30,00,000 ÷ 300 days = Rs. 10,000 per day

In the year 20X0-20X1, Mr. Rajan availed 8 out of 10 leaves allowed by the company.

Accordingly, leaves unutilized = 10 – 8 = 2 days

In line with the company policy, Infotech Ltd. will pay Mr. Rajan for the unutilized leave.

Thus, total expense for 20X0-20X1 = ₹ 30,00,000 + (2 days unutilized leaves x ₹ 10,000 per day) = ₹ 30,20,000.

Scanned with OKEN Scanner

11. AS 16 - BORROWING COSTS

QUESTION 66

Entity Borrowed on 1/4/22 9%, 30 lakhs for Construction of two Qualifying assets. Construction Begins from 1/4/22. The loan was availed on 1/4/22 & started utilizing in Qualifying Asset. Remaining funds were temporarily invested @7% p.a.

	QA 1	QA 2
Expenditure on 1/4/22	5,00,000	10,00,000
Expenditure on 1/10/22	5,00,000	10,00,000

Calculate Total Borrowing Cost & Capitalised Borrowing Cost.

Solution:

Particulars	QA 1	QA 2
Borrowing Cost	10,00,000 x 9% = 90,000	20,00,000 x 9% = 1,80,000
(-) Investment Income	5,00,000 x 7% x6/12 = (17,500)	10,00,000 x 7% x 6/12 = (35,000)
Net Borrowing Cost to be Capitalised	72,500	1,45,000
Total Cost of QA (After Capitalisation)	10,72,500	21,45,000

QUESTION 67

On 1st April, 2011, Amazing Construction Ltd. obtained a loan of ₹32 crores to be utilized as under:

i. Construction of sealink across two cities : ₹25 crores
(Work was held up totally for a month during the year due to high water levels)

ii. Purchase of equipments and machineries : ₹3 crores

ii. Working capital : ₹2 crores

ii. Purchase of vehicles : ₹50,00,000

ii. Advance for tools/cranes etc. : ₹50,00,000

ii. Purchase of technical know-how : ₹1 crores

ii. Total interest charged by the bank for the year ending 31st March, 2012 : ₹80,00,000

Show the treatment of interest by Amazing Construction Ltd.

SOLUTION

According to para 3 of AS 16 'Borrowing costs', qualifying asset is an asset that necessarily takes substantial period of time to get ready for its intended use.

As per para 6 of the standard, borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset should be capitalised as part of the cost of that asset. Other borrowing costs should be recognised as an expense in the period in which they are incurred.

Assumption: Additional Assets is used for same restoration, Hence QA.

The treatment of interest by Amazing Construction Ltd. can be shown as:

	Qualifying Asset	Interest to be capitalized	Interest to be charged to Profit & Loss A/c	
Construction of sea-link	Yes	62,50,000		[80,00,000*(25/32)]
Purchase of equipments and machineries	No		7,50,000	[80,00,000*(3/32)]
Working capital	No		5,00,000	[80,00,000*(2/32)]
Purchase of vehicles	No		1,25,000	[80,00,000*(.5/32)]
Advance for tools, cranes etc.	No.		1,25,000	[80,00,000*(.5/32)]
Purchase of technical know-how	No		2,50,000	[80,00,000*(1/32)]
Total		**62,50,000**	**17,50,000**	

Scanned with OKEN Scanner

QUESTION 68

Paras Ltd. had the following borrowings during a year in respect of capital expansion.

Plant	Cost of Asset	Remarks
Plant P	100 Lakhs	No Specific Borrowings
Plant Q	125 Lakhs	Bank Loan of Rs. 65 lakhs at 10%
Plant R	175 Lakhs	9% Debentures of Rs. 125 lakhs were issued.

In addition to the specific borrowings stated above, the company has obtained term loan from two banks (1) Rs. 100 lakhs at 10% from Corporation bank and (2) Rs. 110 lakhs at 11.50% from SBI to meet its capital expansion requirements. Determine the amount of borrowing costs to be capitalized in each of the above plants, as per AS 16.

SOLUTION

Calculation of Borrowing Cost to Qualified Asset

Q.A.	Amount	Source	Calculation	General B.C. capital	Specific B.C. capital	Total
Plant P	100 lacs	General	100 × 10.786%	10.786 /-	-	10.786 /-
Plant Q	125 lacs	Specific 65 lacs	65 × 10%	-	6.5 /-	12.972 /-
		General 60 lacs	60 × 10.786%	6.472 /-	-	
Plant R	175 lacs	Specific 125 lacs	125 × 9%	-	11.25 /-	16.643 /-
		General 50 lacs	50 × 10.786%	5.393 /-	-	
Total						**40.40 /-**

Working Note: Weighted Average Borrowing Rate: -

Loans	Amount of Loan	B.C
10% Corporation Bank	100 lacs	10 lacs
11.5% SBI	110 lacs	12.65 lacs
	210 lacs	**22.65 lacs**
Weighted Average borrowing Rate	22.65/210 × 100 = 10.786%	

QUESTION 69

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

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

(₹ In lakhs)

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

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

Solution

Computation of amount to be capitalized

No.	Particulars	₹
1.	Interest expense on loan ₹ 2,00,00,000 at 15%	30,00,000
2.	Total cost of Phases I and II (₹ 34,00,000 +64,00,000)	98,00,000
3.	Total cost of Phases III and IV (₹ 55,00,000 + ₹ 68,00,000)	1,23,00,000

Scanned with OKEN Scanner

4.	Total cost of all 4 phases	2,21,00,000
5.	Total loan	2,00,00,000
6.	Interest on loan used for Phases I & II, based on proportionate Loan amount = 30,00,000/2,21,00,000 x 98,00,000	3,30,317 (approx.)
7.	Interest on loan used for Phases III & IV, based on proportionate Loan amount = 30,00,000/2,21,00,000 x 1,23,00,000	16,69,683 (approx.)

Accounting treatment For Phase I and Phase II

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

For Phase III and Phase IV

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

QUESTION 70

On 1stApril, 2022 Workhouse Limited took a loan from a Financial Institution for ` 25,00,000 for the construction of Building. The rate of interest is 12%.

In addition to above loan, the company has taken multiple borrowings as follows:

(i) 8% Debentures ` 15,00,000

(ii) 15% Term Loan ` 30,00,000

(iii) 10% Other Loans ` 18,00,000

The company has utilised the above funds in construction / purchase of the following assets:

(i) Building ` 70,00,000

(ii) Furniture ` 22,00,000

(iii) Plant & Machinery ` 90,00,000

(iv) Factory Shed ` 43,00,000

The construction of Building, Plant & Machinery and Factory Shed was completed on 31st March 2023. Readymade Furniture was purchased directly from the market. The factory was ready for production on 1stApril 2023.

You are required to calculate the borrowing cost for both qualifying and non-qualifying assets.

SOLUTION

Interest to be Capitalized (on qualifying asset)

Particulars	**Computation**	`
i. On specific Borrowings	25,00,000x12%	3,00,000
ii. On non-specific borrowings	(W.N.1)	6,67,500
iii. Amount of interest to be Capitalised	(i+ii)	9,67,500

Interest transferred to P&L (on non-qualifying asset)

Particulars	**Computation**	`
i. On non-specific Borrowings	(W.N.1)	82,500

Working note:

1. Treatment of interest under AS 16 on non-specific borrowings

Particulars	**Qualifying asset**	**# Computation**	**Interest-Capitalized**	**Interest-charged to P&L A/c**

Scanned with OKEN Scanner

i. Building	Yes	45,00,000/2,00,00,000 x 63,00,000 x 11.9048%	1,68,750	-
ii. Furniture	No	22,00,000/2,00,00,000 x 63,00,000 x 11.9048%	-	82,500
iii. Plant & Machinery	Yes	90,00,000/2,00,00,000 x 63,00,000 x 11.9048%	3,37,500	-
iv. Factory shed	Yes	43,00,000/2,00,00,000 x 63,00,000 x 11.9048%	1,61,250	-
Total			**6,67,500**	**82,500**

NOTE: Alternative manner of presentation for Treatment of interest under AS 16 on non-specific borrowings:

Particulars	**Qualifying asset**	**Expenses Incurred `**	**Share in borrowings `**	**Interest – Capitalized `**	**Interest - charged to P&L A/c `**
i. Building	Yes	45,00,000	7,50,000 x 45/200	1,68,750	-
ii. Furniture	No	22,00,000	7,50,000 x 22/200	-	82,500
iii. Plant & Machinery	Yes	90,00,000	7,50,000 x 90 /200	3,37,500	-
iv. Factory shed	Yes	43,00,000	7,50,000 x 43 / 200	1,61,250	-
Total		**2,00,00,000**		**6,67,500**	**82,500**

2. Weighted Average interest rate for non-specific borrowings

Particulars	**Amount of loan (a)**	**Rate of interest (b)**	**Amount of interest (c) = (a) x (b)**
Debentures	15,00,000	8%	1,20,000
Term loan	30,00,000	15%	4,50,000
Other loans	18,00,000	10%	1,80,000
	63,00,000		7,50,000
	# Weighted Average Rate of Interest = 7,50,000 / 63,00,000 x 100 = 11.9048%		

QUESTION 71

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

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

SOLUTION

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

Scanned with OKEN Scanner

to conclude that substantially all the activities necessary to prepare the asset are complete. Thus, the borrowing cost incurred during the normal period of test runs (after the installation) are required to be capitalized.

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

QUESTION 72

Zebra limited begam construction of a new plant on 1st April, 2021 and obtained a special loan of Rs. 20,00,000 to finance the construction of the plant. The rate of interest on loan was 10%.

The expenditure that was incurred on the construction of plant was as follows:

	Rs.
1st April, 2021	10,00,000
1st August, 2021	24,00,000
1st January, 2022	4,00,000

The company's other outstanding non-specific loan was Rs. 46,00,000 at an interest rate of 12%

The construction of the plant completed on 31st March, 2022.

You are required to:

(a) Calculate the amount of interest to be capitalized as per the provision of AS 16 "Borrowing Cost".

(b) Pass a journal entry for capitalizing the cost and the borrowing cost in respect of the plant

SOLUTION

Total expenses to be capitalized for borrowings as per AS 16 "Borrowing Costs":

	Rs.
Cost of Plant (10,00,000 + 24,00,000 + 4,00,000)	38,00,000
Add: Amount of interest to be capitalized (W.N.)	3,24,000
	41,24,000

Journal Entry

		Rs.	Rs.
31st March, 2022	Plant A/c Dr.	41,24,000	
	To Bank A/c		41,24,000
	[Being amount of cost of plant and borrowing cost thereon capitalized]		

Working Note:

Computation of interest to be capitalized:

	Expenditure			Rs.
1st April, 2021	10,00,000	On specific borrowing	Rs. 10,00,000 x 10%	1,00,000
1st August, 2021	24,00,000	On specific borrowing	Rs. 10,00,000 x 10%	1,00,000
1st August, 2021		On non-specific borrowings	Rs. 14,00,000 x 8/12 x 12%	1,12,000
1st January, 2022	4,00,000	On non-specific borrowings	Rs. 4,00,000 x 3/12 x 12%	12,000
				3,24,000

Scanned with OKEN Scanner

Alternatively, interest cost to be capitalized can be derived by computing average accumulated expenses in the following manner.

Computation of Average Accumulated Expenses:

1st April, 2021	10,00,000 x 12/12	10,00,000
1st August, 2021	10,00,000 x 12/12	10,00,000
	14,00,000 x 8/12	9,33,333
1st January, 2022	4,00,000 x 3/12	1,00,000
		30,33,333

Computation of interest to be capitalized:

		Rs.
On specific borrowing	Rs. 20,00,000 x 10%	2,00,000
On non-specific borrowing	Rs. (30,33,333- 20,00,000) x 12%	1,24,000
		3,24,000

NOTE:

Since specific borrowings are earmarked for construction of a particular qualifying asset, it cannot be used for construction of any other qualifying asset except for temporary investment. Therefore, once the commencement of capitalization of borrowing cost criteria are met, actual borrowing cost incurred on specific borrowing shall be capitalized irrespective of the fact that amount had been utilized in parts.

Scanned with OKEN Scanner

12. AS – 10 PPE

QUESTION 73

Entity A exchanges car X with a book value of Rs 13,00,000 and a fair value of Rs 13,25,000 for cash of Rs 15,000 and car Y which has a fair value of Rs 13,10,000. The transaction lacks commercial substance as the company's cash flows are not expected to change as a result of the exchange. It is in the same position as it was before the transaction. What will be the measurement cost of the assets received?

Solution

The entity recognises the assets received at the book value of car X. Therefore, it recognises cash of Rs 15,000 and car Y as PPE with a carrying value of Rs 12,85,000.

QUESTION 74

On 1st April 20X1, an item of property is offered for sale at Rs. 10 million, with payment terms being three equal installments of Rs.33,33,333 over a two years period (payments are made on 1st April 20X1, 31st March 20X2 and 31st March 20X3).

The property developer is offering a discount of 5 percent (i.e., Rs. 0.5 million) if payment is made in full at the time of completion of sale. Implicit interest rate of 5.36 percent p.a.

Show how the property will be recorded in accordance of AS 10.

SOLUTION:

AS 10 requires that the cost of an item of PPE is the cash price equivalent at the recognition date. Hence, the purchaser that takes up the deferred payment terms will recognise the acquisition of the asset as follows

On 1st April, 20X1	**(Rs)**	**(Rs)**
Property, Plant and Equipment Dr.	95,00,000	
To Cash		33,33,333
To Accounts Payable		61,66,667
(Initial recognition of property)		
On 31st March 20X2		
Interest Expense Dr.	3,30,533	
Accounts payable Dr.	30,02,800	
To Cash		33,33,333
(Recognition of interest expense and payment of second installment)		
On 31st March 20X3		
Interest Expense Dr.	1,69,467	
Accounts payable Dr.	31,63,867	
To Cash		33,33,334
(Recognition of interest expense and payment of final installment)		

QUESTION 75

Akshar Ltd. installed a new Plant (not a qualifying asset), at its production facility, and incurred the following costs:

- Cost of the Plant (as per supplier's invoice): ₹ 30,00,000
- Initial delivery and handling costs: ₹ 1,00,000
- Cost of site preparation: ₹ 2,00,000
- Consultant fee for advice on acquisition of Plant: ₹ 50,000
- Interest charges paid to supplier against deferred credit: ₹ 1,00,000
- Estimate of Dismantling and Site Restoration costs: ₹ 50,000 after 10 years (Present Value is ₹ 30,000)
- Operating losses before commercial production: ₹ 40,000

The company identified motors installed in the Plant as a separate component and a cost of ₹ 5,00,000 (Purchase Price) and other costs were allocated to them proportionately. The company estimates the useful life of the Plant and those of the Motors as 10 years and 6 years respectively and SLM method of Depreciation is used.

Scanned with OKEN Scanner

At the end of Year 4, the company replaces the Motors installed in the Plant at a cost of ₹ 6,00,000 and estimated the useful life of new motors to be 5 years. Also, the company revalued its entire class of Fixed Assets at the end of Year 4. The revalued amount of Plant as a whole is ₹ 25,00,000. At the end of Year 8, the company decides to retire the Plant from active use and also disposed the Plant as a whole for ₹ 6,00,000.

There is no change in the Dismantling and Site Restoration liability during the period of use. You are required to explain how the above transaction would be accounted in accordance with AS 10.

Solution

1. Cost at Initial Recognition:

Particulars	₹
Cost of the Plant (as per Invoice)	30,00,000
Initial Delivery and Handling Costs	1,00,000
Cost of Site Preparation	2,00,000
Consultants' Fees	50,000
Estimated Dismantling and Site Restoration Costs	30,000
Total Cost of Plant including Motors	33,80,000
Less: Cost of Motors identified as a separate component (1/6)*	5,63,333
Cost of the Plant (excluding Motors – balance 5/6)	**28,16,667**

* Purchase price of Motors = ₹ 5,00,000 out of ₹ 30,00,000 i.e., 1/6 of value of Plant

Note: Since the asset is not a qualifying asset, payment of interest to the supplier is not capitalized. Further, operating losses of ` 40,000 incurred before commercial production is not a directly attributable cost, and hence excluded from cost of asset. These costs are expensed to the P/L as and when they are incurred.

2. Recognition of Motors Replacement

Particulars	₹
Cost of Motors determined above	5,63,333
Less: Depreciation for 4 years (as per SLM)	3,75,555
5,63,333 ÷ 6 years x 4 years	
Carrying Amount of Motors at the end of Year 4	**1,87,778**

Accounting: The company should derecognize the existing Carrying Amount of Motors replaced of ₹ 1,87,778. Further, the acquisition cost of new motors of ₹ 6,00,000 would be capitalized as a separate component. This amount will be depreciated over the next 5 years at ₹ 6,00,000 ÷ 5 years = ₹ 1,20,000 p.a.

3. Revaluation

Particulars	₹
Cost of the Plant at initial recognition [from (1) above]	28,16,667
Less: SLM Depreciation for 4 years: ₹ 28,16,667 ÷ 10 years x 4 years	11,26,667
Carrying Amount of Plant at the end of Year 4	16,90,000
Revalued Amount of Plant (Excluding Motors, since the same is treated as a separate component: ₹ 25,00,000 – ₹ 6,00,000)	19,00,000
Therefore, Gain on Revaluation credited to Revaluation Reserve	**2,10,000**
Revised Depreciation Charge p.a.: 19,00,000 ÷ 6 years	**3,16,667**

4. **Derecognition**

Particulars	Motors	Plant (excluding Motors)
Cost / Revalued Amount at end of Year 4	6,00,000	19,00,000
Less: Depreciation for Years 5-8	1,20,000 x 4 = 4,80,000	3,16,667 x 4 =12,66,668
Carrying Amount before Disposal / De- recognition	1,20,000	6,33,332

Scanned with OKEN Scanner

Less: Disposal Proceeds ₹ 6,00,000 allocated in ratio of carrying amount	95,575	5,04,425
Loss to be written off to P/L	**24,425**	**1,28,907**

Notes:

(a) The Revaluation Surplus of ` 2,10,000 would be transferred directly to Retained Earnings.

(b) The allocation of disposal proceeds of ` 6,00,000 for the plant as whole is apportioned based on carrying amount of motors and plant (excluding motors)

Alternatively, it may be apportioned as 1/6 towards motors and 5/6 plant (excluding motors) based on the reasoning that the initially, motors amounted to 1/6 of the entire plant. This approach may not be preferable because there has been a revaluation of the plant (excluding motors) and a disposal and subsequent acquisition of the Motor, which is not in the initial proportion of 5/6 and 1/6 respectively.

QUESTION 76

Bharat Infrastructure Ltd. acquired a heavy machinery at a cost of ₹ 1,000 lakhs, the breakdown of its components is not provided. The estimated useful life of the machinery is 10 years. At the end of Year 6, the turbine, which is a major component of the machinery, needed replacement, as further usage and maintenance was uneconomical. The remainder of the machine is in good condition and is expected to last for the remaining 4 years. The cost of the new turbine is ₹ 450 lakhs. Give the accounting treatment for the new turbine, assuming SLM Depreciation and a discount rate of 8%.

Solution

As per AS 10, Property, Plant and Equipment, the derecognition of the carrying amount of components of an item of Property, Plant and Equipment occurs regardless of whether the cost of the previous part / inspection was identified in the transaction in which the item was acquired or constructed. If it is not practicable for an enterprise to determine the carrying amount of the replaced part/ inspection, it may use the cost of the replacement or the estimated cost of a future similar inspection as an indication of what the cost of the replaced part/ existing inspection component was when the item was acquired or constructed.

In the given case, the new turbine will produce economic benefits to Bharat Infrastructure Ltd. and the cost is measurable. Since the recognition criteria is fulfilled, the same should be recognised as a separate item of Property, Plant and Equipment. However, since the initial breakup of the components is not available, the cost of the replacement of ₹ 450 lakhs can be used as an indication based on the guidance given above, discounted at 8% for the 6-year period lapsed. Thus, estimate of cost 6 years back = ₹ 450 lakhs ÷ 1.08^6 = ₹ 283.58 lakhs Current carrying amount of turbine (to be de-recognised) = Estimated cost ₹ 283.58 lakhs (–) SLM depreciation at 10% (useful life 10 years) for 6 years ₹ 170.15 lakhs= ₹ 113.43 lakhs.

Hence revised carrying amount of the machinery will be as under:

Particulars	₹ in lakhs
Historical Cost [₹ 1,000 lakhs (–) SLM Depreciation at 10% (10 year life) for 6 years]	400.00
Add: Cost of new turbine	450.00
Less: Derecognition of current carrying amount of old turbine	(113.43)
New Carrying Amount of Machinery	**736.57**

QUESTION 77

Preet Ltd. intends to set up a steel plant, for which it has acquired a dilapidated factor having an area of 5,000 acres at a cost of ₹ 60,000 per acre. Preet Ltd. has incurred ₹ 1.10 crores on demolishing the old Factory Building thereon. A sum of ₹ 63,00,000 (including 5% GST thereon) was realized from the sale of material salvaged from the site. Preet Ltd. incurred Stamp Duty and Registration Charges of 7% of land value, paid legal and consultancy charges ₹ 8,00,000 for land acquisition and incurred ₹ 1,25,000 on title guarantee insurance. Compute the value of the land acquired.

Scanned with OKEN Scanner

Solution

Particulars	₹
Purchase Price: 5,000 acres x ₹ 60,000 per acre	3,000.00
Stamp Duty and Registration Charges at 7%	210.00
Legal and Consultancy Fees	8.00
Title Guarantee Insurance	1.25
Demolition Expenses (Net of Salvage Income) [₹ 110 lakhs (–)₹ 60 lakhs (₹ 63 lakhs x 100/105)]	50.00
Cost of Land	**3,269.25**

QUESTION 78

In the books of Topmaker Limited, carrying amount of Plant and Machinery as on 1stApril, 2022 is ` 56,30,000. On scrutiny, it was found that a purchase of Machinery worth ` 21,12,000 was included in the purchase of goods on 1st June, 2022. On 30thJune, 2022 the company disposed a Machine having book value of ` 9,60,000 (as on 1stApril, 2022) for ` 8,25,000 in part exchange of a new machine costing ` 15,65,000.

The company charges depreciation @ 10% p.a. on written down value method on Plant and Machinery.

You are required to compute:

- Depreciation to be charged to Profit & Loss Account;
- Book value of Plant & Machinery as on 31stMarch, 2023; and
- Profit/Loss on exchange of Plant & Machinery.

Solution:

(i) Depreciation to be charged in the profit & Loss Account

Particulars	Amount in ₹
Depreciation on old machinery [10% on ₹ 56,30,000 for 3 months (01.04.2022 to (30.06.2022)]	1,40,750
Add: Depreciation on Machinery acquired on 01.06.2022 (₹21,12,000 × 10% × 10/12)	1,76,000
Add: Depreciation on machinery after adjustment of exchange [10% of ₹ 56,30,000 – 9,60,000 +15,65,000) for 9 months]	4,67,625
Total Depreciation to be charged in Profit & Loss A/c	**7,84,375**

(ii) Book Value of Plant & Machinery as on 31.3.2023

Particulars		Amount in ₹
Balance as books on 01.04.2022		56,30,000
Add: Included in purchases on 01.06.2022	21,12,000	
Add: Purchase on 30.06.2022	15,65,000	36,77,000
		93,07,000
Less: Book Value of Machine Sold on 30.06.2022		(9,60,000)
		83,47,000
Less: Depreciation on Machinery in use ₹ (7,84,375-24,000)		(7,60,375)
Book Value as on 31.03.2023		**75,86,625**

Note: The computation of depreciation and book value of plant and machinery can be presented in the following alternative manner

Particulars	Book value or Cost or Acquisition	Period	Deprecation	Book value as on 31.03.2023
Opening Value	46,70,000	01.04.2022 To	4,67,000 (46,70,000×10%)	42,03,00

Scanned with OKEN Scanner

	(56,30,000-9,60,000)	31.03.2023		
Sold	9,60,000	01.04.2022 to 30.06.2022	24,000 (9,60,000 x 10% x 3/12)	19,36,000
Purchases	21,12,000	01.06.2022 To 31.03.2023	1.17.375 (15,65,000 × 10%9/912	14,47,625
Total			**7,84,375**	**75,86,625**

(iii)Profit/Loss on Exchange of Machinery

Particulars	Amount in ₹
Balance as per books on 01.04.2022	9,60,000
Less: Depreciation for 3 months (₹ 9,60,000 ×10/100× 3/12)	(24,000)
W.D.V. as on 30.06.2022	9.36,000
Less: Exchange Value	(8,25,000)
Loss on exchange on Machinery	**1,11,000**

Scanned with OKEN Scanner

13. CONSOLIDATION

QUESTION 79

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

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

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

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

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

Calculate as on 31st March, 2021

(i) Cost of Control/Capital Reserve;

(ii) Minority Interest;

(iii) Consolidated Profit and Loss Account in each of the following cases:

. Before issue of bonus shares.

Immediately after issue of bonus shares.

SOLUTION

Shareholding pattern

Particulars	Number of Shares	% of holding
. P Ltd.		
(i) Purchased on 31.03.2015	1,05,000	
(ii) Bonus Issue (1,05,000/2)	52,500	
Total	1,57,500	70%
a. Minority Interest	67,500	30%

Calculations of (i) Cost of Control/Capital Reserve; (ii) Minority Interest; (iii) Consolidated Profit and Loss Account as on 31st March, 2021:

. **Before issue of bonus shares**

(i)	Cost of control/capital reserve	Rs.	Rs.
	Investment in Q Ltd.		12,00,000

Scanned with OKEN Scanner

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

b. Immediately after issue of bonus shares

(i)	**Cost of control/capital reserve**	**Rs.**	**Rs.**
	Face value of investments (Rs. 10,50,000 + Rs. 5,25,000)	15,75,000	
	Capital Profits (W.N.)	63,000	16,38,000
	Less: Investment in Q Ltd.		(12,00,000)
	Capital reserve		**4,38,000**
(ii)	**Minority Interest**		**Rs.**
	Share Capital (Rs. 4,50,000 + Rs. 2,25,000)		6,75,000
	Capital Profits (W.N.)		27,000
	Revenue Profits (W.N.)		4,54,500
			11,56,500
(iii)	**Consolidated Profit and Loss Account – P Ltd.**		**Rs.**
	Balance		15,75,000
	Add: Share in revenue profits of Q Ltd. (W.N.)		10,60,500
			26,35,500

Working Note:

Analysis of Profits of Q Ltd.

	Capital Profits	**Revenue Profits**	
	(Before and after issue of bonus shares) Rs.	**Before Bonus Issue Rs.**	**After Bonus Issue Rs.**
Pre-incorporation profits	30,000		
Profit and loss account on 31.3.2015	60,000		
General reserve*	90,000	19,05,000	19,05,000
Less: Bonus shares			(7,50,000)
			11,55,000

Profit for period of 1st April, 2015 to 31st March, 2021 (Rs. 4,20,000 – Rs. 60,000)		3,60,000	3,60,000
		22,65,000	15,15,000
P Ltd.'s share (70%)	63,000	15,85,500	10,60,500
Minority's share (30%)	27,000	6,79,500	4,54,500

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

Scanned with OKEN Scanner

QUESTION 80

A Ltd. acquired 70% of equity shares of B Ltd. on 1.4.2010 at cost of ₹10,00,000 when B Ltd. had an equity share capital of ₹10,00,000 & reserves & surplus of ₹80,000. In the four consecutive years, B Ltd. fared badly& suffered losses of ₹2,50,000, ₹4,00,000, ₹ 5,00,000 & ₹1,20,000 respectively. Thereafter in 2014- 15, B Ltd. experienced turnaround ®istered an annual profit of ₹ 50,000. In the next two years i.e., 2015-16 & 2016-17, B Ltd. recorded annual profits of ₹1,00,000 & ₹1,50,000 respectively. Show the minority interests& cost of control at the end of each year for the purpose of consolidation.

SOLUTION

The losses applicable to the minority in a consolidated subsidiary may exceed the minority interest in the equity of the subsidiary. The excess, and any further losses applicable to the minority, are adjusted against the majority interest except to the extent that the minority has a binding obligation to, and is able to, make good the losses. If the subsidiary subsequently reports profits, all such profits are allocated to the majority interest until the minority's share of losses previously absorbed by the majority has been recovered. Accordingly, the minority interests will be computed as follows:

Year	Profit/(Loss)	Minority Interest (30%)	Additional Consolidated P & L (Dr.) Cr.	Minority's Share of losses borne by A Ltd.		Cost of Control
				₹	Balance	
At the time of acquisition in 2010		3,24,000 (W.N.)	-			
2010-11	(2,50,000)	(75,000)	1,75,000			2,44,000
Balance		2,49,000				(W.N.)
2011-12	(4,00,000)	(1,20,000)	2,80,000			2,44,000
Balance		1,29,00				
2012-13	(5,00,000)	(1,50,000)	(3,50,000)			2,44,000
		(21,000)				
	Loss of minority borne by Holding Co	21,0000	(21,000)	21,000	21,000	
Balance		Nil	(3,71,000)			
2013-14	(1,20,000)	(36,000)	(84,000)			2,44,000
	Loss of minority borne by Holding Co.	36,000	(36,000)	36,000	57,000	
Balance		Nil	(1,20,000)			
2014-15	50,000	15,000	35,000			2,44,000
	Profit share of minority adjusted against losses of minority absorbed by Holding Co.	(15,000)	15,000	(15,000)	42,000	
Balance		Nil	50,000			
2015-16	1,00,000	30,000	70,000			
	Profit share of minority adjusted against losses of minority absorbed by Holding Co.	(30,000)	30,000	(30,000)	12,000	2,44,000
Balance		Nil	1,00,000			
2016-17	1,50,000	45,000	1,05,000	(12,000)	Nil	2,44,000
		(12,000)	(12,000)			
		33,000	1,17,000			

Scanned with OKEN Scanner

Calculation of Minority interest and Cost of control on 1.4.2010

Working Note:		Share of Holding Co.	Minority interest
	100%	70%	30%
	(₹)	(₹)	(₹)
Share Capital	10,00,000	7,00,000	3,00,000
Reserve	80,000	56,000	24,000
		7,56,000	3,24,000
Less: Cost of investment		(10,00,000)	
Goodwill		**2,44,000**	

QUESTION 81

A Ltd. and B Ltd. provide the following information:

	₹ '000s	
	A Ltd.	**B Ltd.**
Equity Shares	6,000	5,000
6% Preference Shares	NIL	1,000
General Reserve	1,200	800
Profit and Loss Account	1,020	1,790
Trade Payables	3,850	3,410
Dividend Payable	600	500
Goodwill	100	20
Property, Plant and Equipment	3,850	2,750
Investment	1,620	1,100
Inventory	1,900	4,150
Trade Receivables	4,600	4,080
Cash & Bank	600	400

A Ltd. purchased 3/4th interest in B Ltd. at the beginning of the year at the premium of 25%. Following other information is available:

a. Profit & Loss Account of B Ltd. includes ₹ 1,000 thousands bought forward from the previous year.

b. The General Reserve balance is brought forward from the previous year.

c. The directors of both the companies have declared a dividend of 10% on equity share capital for the previous and current year.

From the above information calculate Pre- and Post-acquisition Profits, Minority Interest and Cost of Control.

SOLUTION

(ICAI SUGGESTED ANSWER – THIS IS WRONG AS PER MY OPINION)

Calculation of Pre- and Post-Acquisition Profits:

	Pre-Acquisition Profits (₹)	Post-Acquisition Profits (₹)
Profit & Loss Account	10,00,000	7,90,000
General Reserve	8,00,000	NIL
	18,00,000	7,90,000
Less: Share of Minority Interest: (¼)	(4,50,000)	(1,97,500)
Attributable to Parent	13,50,000	5,92,500
	(Cost of Control)	(Post-acquisition Profits)

Calculation of Minority Interest:

Particulars	₹
Paid-up Equity Share Capital (₹ 50,00,000 x ¼)	12,50,000

Scanned with OKEN Scanner

Paid-up Preference Share Capital	10,00,000
Share in Reserves:	
Profit & Loss Account: ₹ 17,90,000 x ¼	4,47,500
General Reserve: ₹ 8,00,000 x ¼	2,00,000
Minority Interest	28,97,500

Calculation of Goodwill/Capital Reserve

	₹	₹
Cost of Investment in Subsidiary:	46,87,500	
₹ 50,00,000 x 75% x 125% (cost + 25% premium)		
Less: Pre-acquisition dividend	(3,75,000)	43,12,500
Less: Net Worth of B Ltd. on Date of Acquisition (attributable to A Ltd.):		
Paid-up Capital	37,50,000	
Pre-acquisition Reserves	13,50,000	(51,00,000)
Capital Reserve		7,87,500

QUESTION 82

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

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

The following revaluations have been agreed upon (not included in the above figures):

- Property, plant and equipment- up by 20% and Investments- down by 10%.
- King Ltd. purchased the shares of Queen Ltd. @ ₹20 per share (Face value - ₹10).

Calculate the amount of goodwill/capital reserve on acquisition of shares of Queen Ltd.

SOLUTION

Revalued net assets of Queen Ltd. as on 31st March, 20X1

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

QUESTION 83

Exe Ltd. acquires 70% of equity shares of Zed Ltd. as on 31st March, 2017 at a cost of ₹ 70 lakhs. The following information is available from the balance sheet of Zed Ltd. as on 31st March, 2017:

Scanned with OKEN Scanner

	₹ in lakhs
Property, plant & Equipment	120
Investments	55
Current Assets	70
Loans & Advances	15
15% Debentures	90
Current Liabilities	50

The following revaluations have been agreed upon (not included in the above figures):

Property, plant & Equipment — Up by 20%

Investments — Down by 10%

Zed Ltd. declared and paid dividend @ 20% on its equity shares as on 31st March, 2017. Exe Ltd. purchased the shares of Zed Ltd. @ ₹20 per share.

Calculate the amount of goodwill/capital reserve on acquisition of shares of Zed Ltd.

SOLUTION

Revalued net assets of Zed Ltd. as on 31st March, 2017

	₹ in lakhs	₹ in lakhs
Property, plant & Equipment [120 X 120%]		144.0
Investments [55 X 90%]		49.5
Current Assets		70.0
Loans and Advances		15.0
Total Assets after revaluation		278.5
Less: 15% Debentures	90.0	
Current Liabilities	50.0	(140.0)
Equity / Net Worth		138.5
Exe Ltd.'s share of net assets (70% of 138.5)		96.95
Exe Ltd.'s cost of acquisition of shares of Zed Ltd. (₹70 lakhs – ₹7 lakhs*)		63.00
Capital reserve		**33.95**

* Total Cost of 70 % Equity of Zed Ltd	₹ 70 lakhs
Purchase Price of each share	₹ 20
Number of shares purchased [70 lakhs /₹ 20]	3.5 lakhs
Dividend @ 20 % i.e., ₹ 2 per share	₹ 7 lakhs

Since dividend received is for pre-acquisition period, it has been reduced from the cost of investment in the subsidiary company.

QUESTION 84

On 31st March, 2022, H Ltd. and S Ltd. give the following information:

	H Ltd. (Rs. in 000's)	S Ltd. (Rs. in 000's)
Equity Share Capital – Authorised	5,000	3,000
Issued and subscribed in Equity Shares of Rs. 10 each fully paid	4,000	2,400
General Reserve	928	690
Profit and Loss Account (Cr. Balance)	1,305	810
Trade payables	611	507
Provision for Taxation	220	180
Other Provisions	65	17

Scanned with OKEN Scanner

Plant and Machinery	2,541	2,450
Furniture and Fittings	615	298
Investment in the Equity Shares of S Ltd.	1,500	-
Inventory	983	786
Trade receivables	820	778
Cash and Bank Balances	410	102
Sundry Advances (Dr. balances)	260	190

Following Additional Information is available:

(a) H Ltd. purchased 90 thousand Equity Shares in S Ltd. on 1st April, 2021. On that date the following balances stood in the books of S Ltd.:

General Reserve Rs. 1,500 thousand; Profit and Loss Account Rs. 633 thousand.

(b) On 14th July, 2021 S Ltd. declared a dividend of 20% out of pre-acquisition profits. H Ltd. credited the dividend received to its Profit and Loss Account.

(c) On 1st November, 2021, S Ltd. issued 3 fully paid Equity Shares of Rs. 10 each, for every 5 shares held as bonus shares out of pre-acquisition General Reserve.

(d) On 31st March, 2021, the Inventory of S Ltd. included goods purchased for Rs. 50 thousand from H Ltd., which had made a profit of 25% on cost.

(e) Details of Trade payables and Trade receivables:

	H Ltd. (Rs. in 000's)	**S Ltd. (Rs. in 000's)**
Trade payables		
Bills Payable	124	80
Sundry creditors	487	427
	611	**507**
Trade receivables		
Debtors	700	683
Bills Receivables	120	95
	820	**778**

Prepare a consolidated Balance Sheet as at 31st March, 2022.

SOLUTION

Consolidated Balance Sheet of H Ltd. with its subsidiary S Ltd. as at 31st March, 2022

Particulars			Note No.	(Rs. in 000's)
I.	**Equity and Liabilities**			
(1)	**Shareholder's Funds**			
	(a)	Share Capital	1	4,000
	(b)	Reserves and Surplus	2	3,063
(2)	Minority Interest (W.N.6)			1,560
(3)	**Current Liabilities**			
	Trade payables		3	1,118
	Short term provisions		4	482
Total				**10,223**
II.	**Assets**			
(1)	**Non-current assets**			
	PPE		5	5,904
(2)	**Current assets**			
(a)	Inventories		6	1,759
(b)	Trade receivables		7	1,598

Scanned with OKEN Scanner

(c)	Cash and cash equivalents	8	512
(d)	Short term loans and advances	9	450
Total			**10,223**

Notes to Accounts

		(Rs. in 000's)	(Rs. in 000's)
1.	**Share Capital**		
	Authorised share capital		
	5 lakhs equity shares of Rs. 10 each		5,000
	Issued, Subscribed and Paid up		
	4 lakhs equity shares of Rs. 10 each fully paid		4,000
2.	**Reserves and surplus**		
	Capital Reserve (Note 5)	679.8	
	General Reserve	928	
	Profit and Loss Account:		
	H Ltd. Rs. 1,305 Add: Share in S Ltd Rs. 340.20		
	Rs. 1,645.20		
	Less: Dividend wrongly credited Rs. (180)		
	Rs. 1,465.20		
	Less: Unrealised profit (50 X 1/5) Rs. (10)	1,455.20	3,063
3.	**Trade payables**		
	H Ltd.	611	
	S Ltd.	507	1,118
4.	**Short –term provisions**		
	Provision for Taxation H Ltd. Rs. 220		
	S Ltd. Rs. 180	400	
	Other Provisions H Ltd Rs. 65		
	S Ltd. Rs. 17	82	482
5.	**PPE**		
	Plant and Machinery		
	H Ltd. Rs. 2,541		
	S Ltd. Rs. 2,450	4,991	
	Furniture and fittings		
	H Ltd. Rs. 615		
	S Ltd. Rs. 298	913	5,904
6.	**Inventories**		
	Inventory H Ltd. Rs. 983 S Ltd. Rs. 786	1,769	
	Less: Unrealised profit (Rs. 50 x 1/5)	(10)	1,759
7.	**Trade receivables**		
	H Ltd.	820	
	S Ltd.	778	1,598
8.	**Cash and cash equivalents**		
	Cash and Bank Balances H Ltd	410	
	S Ltd.	102	512
9.	**Short term loans and advances**		
	Sundry Advances H Ltd.	260	

Scanned with OKEN Scanner

	S Ltd.	190	450

Working Notes:

Share holding pattern

Particulars		Number of Shares	% of holding
a.	S Ltd. (i) Purchased on 01.04.2021	90,000	
	(ii) Bonus Issue (90,000/5 x 3)	54,000	
	Total	1,44,000	60% (1,44,000 /2,40,000*x 100)
b.	Minority Interest	96,000	40%

*2,40,000 is after issue of bonus shares as per balance sheet as at 31.3.2022

1. S Ltd. General Reserve

		(Rs. in 000)			(Rs. in 000)
To	Bonus to equity shareholders (2,400/8 x 3)	900	By	Balance b/d	1,500
To	Balance c/d	690	By	Profit and Loss A/c (Balancing figure)	90
		1,590			**1,590**

2. S Ltd.'s Profit and Loss Account

		(Rs. in 000)			(Rs. in 000)
To	General Reserve	90	By	Balance b/d	633
To	Dividend paid on 14.7.2021 (1,500/100 x 20)	300	By	Net Profit for the year (Bal. fig.)	567*
To	Balance c/d	810			
		1,200			**1,200**

* Out of Rs. 5,67,000 profit for the year, Rs. 90,000 has been transferred to reserves by S Ltd.

3. Distribution of Revenue Profits

	Rs. in '000
Revenue Profit as above	567.00
Share of H Ltd. (60%)	340.20
Share of Minority shareholders (567– 340.20)	226.80

4. Computation of Capital Profits

	Rs. in 000	Rs. in 000
General Reserve on the date of acquisition		1,500
Less: Bonus issue of shares		(900)
		600
Profit and Loss Account balance on the date of acquisition	633	
Less: Dividends paid	(300)	333
		933
Share of H Ltd. (60%)		559.80
Share of Minority shareholders		373.20

5. Computation of Capital Reserve

		Rs. in '000
60% of share capital of S Ltd.		1,440
Add: Share of H Ltd. in the capital profits as in W.N. (4)		559.80
		1,999.80

Scanned with OKEN Scanner

Less: Investments in S Ltd.	1,500	
Less: Dividends received out of pre- acquisition profits Rs. 300/100 x 60	(180)	(1,320)
		679.80

6. **Calculation of Minority Interest**

	Rs. in '000
40% of share capital of S Ltd.	960.00
Add: Share of Revenue Profits (Note 3)	226.80
Share of Capital Profits (Note 4)	373.20
	1,560.00

QUESTION 85

The Trial Balances of X Limited and Y Limited as on 31st March, 2021 were as under:

	X Limited (Rs. In 000)		**Y Limited (Rs. In 000)**	
	Dr.	**Cr.**	**Dr.**	**Cr.**
Equity Share capital (Share of Rs. 100 each)		2,000		400
7% Preference share capital		-		400
Reserves		600		200
6% Debentures		400		400
Trade Receivables/Trade Payables	160	180	100	120
Profit & Loss A/c balance		40		30
Purchases /Sales	1,000	1,800	1,200	1,900
Wages and Salaries	200		300	
Debenture Interest	24		24	
General Expenses	160	7	120	
Preference share dividend up to 30.09.2020			14	
Inventory (as on 31.03.2021)	200		100	
Cash at Bank	27		12	
Investment in Y Limited	1,056		-	
Fixed Assets	2,200		1,580	
Total	5,027	5,027	3,450	3,450

- **Investment in Y Limited was acquired on 1st July, 2020 and consisted of 80% of Equity Share Capital and 50% of Preference Share Capital.**
- After acquiring control over Y Limited, X Limited supplied to Y Limited goods at cost plus 25%, the total invoice value of such goods being Rs. 1,20,000, one fourth of such goods were still lying-in inventory at the end of the year.
- Depreciation to be charged @ 10% in X Limited and @ 15% in Y Limited on Fixed Assets.

You are required to prepare the Consolidated Statement of Profit and Loss for the year ended on 31st March, 2021.

SOLUTION

Consolidated Statement of Profit & Loss Account of X Ltd. and Y Ltd.
for the year ended 31st March, 2021

Particulars	**Note No.**	**Rs.**
I. Revenue from operations	1	35,80,000
II. Total revenue		**35,80,000**
III. Expenses		
Cost of Material purchased/Consumed	2	20,80,000
Changes of Inventories of finished goods		-
Employee benefit expense	3	5,00,000
Finance cost	4	48,000
Depreciation and amortization expense	5	4,57,000

Scanned with OKEN Scanner

Other expenses	6	2,80,000
Total expenses		33,65,000
IV. Profit before Tax (II-III)		**2,15,000**
Profit transferred to Consolidated Balance Sheet		
Profit After Tax		**2,15,000**
Preference dividend	7,000	
Preference dividend payable	7,000	(14,000)
		2,01,000
Share in pre-acquisition loss (WN 3)		1,800
Share of Minority interest in losses (WN 1)		1,800
Less: Investment Account- dividend for 3 months (prior to acquisition)		(3,500)
Inventory reserve (WN 2)		(6,000)
Profit to be transferred to consolidated balance sheet		**1,95,100**

Notes to Accounts

		Rs.	Rs.
1	**Revenue from Operations**		
	X Ltd.	18,00,000	
	Y Ltd.	19,00,000	
	Total	37,00,000	
	Less: Intra-group sales (X sold to Y)	(1,20,000)	35,80,000
2	**Cost of Materials Purchased/Consumed**		
	X Ltd.	10,00,000	
	Y Ltd.	12,00,000	
	Total	22,00,000	
	Less: Intra-group sales (X sold to Y)	(1,20,000)	20,80,000
3	**Employee benefit and expenses**		
	Wages and salaries		
	H Ltd.	2,00,000	
	S Ltd.	3,00,000	5,00,000
4	**Finance cost**		
	Interest		
	H Ltd.	24,000	
	S Ltd.	24,000	48,000
5	**Depreciation**		
	H Ltd.	2,20,000	
	S Ltd.	2,37,000	4,57,000
6	**Other expenses**		
	H Ltd.	1,60,000	
	S Ltd.	1,20,000	2,80,000

Working Notes:

1. **Profit of Subsidiary**

		Rs.
Revenue from Operations		19,00,000
Less: Expenses		
Cost of Material purchased/Consumed	12,00,000	
Changes of Inventories of finished goods	-	
Employee benefit expense	3,00,000	

Scanned with OKEN Scanner

Finance cost	24,000	
Depreciation and amortization expense	2,37,000	
Other expenses	1,20,000	
Total expenses		(18,81,000)
Profit Before Tax		19,000
Less: Preference Dividend	14,000	
Less: Preference Dividend Payable	14,000	(28,000)
Profit available for shareholders		(9,000)
Minority Share (20% of loss Rs. 9,000)		**(1,800)**

0. **Inventory reserve = 120,0004 x 25125=Rs. 6,000**
1. **Pre-acquisition loss** = 80% of 3 month's profit up to 30th June,2020 i.e. 80 % of ¼ of loss Rs. 9,000. Hence, pre-acquisition loss = Rs. 1,800
2. Investment account includes Preference dividend for 3 months prior to acquisition i.e. Rs. 4,00,000 x 50% x 7% x 1/4 = Rs. 3,500

QUESTION 86

Subsidiary B Ltd. provides the following balance sheet

Particulars	Note No.	20X0 (₹)	20X1 (₹)
Equity and Liabilities			
(I) Shareholder's Funds			
(a) Share Capital	1	5,00,000	5,00,000
(b) Reserves and Surplus	2	2,86,000	7,14,000
(2) Current Liabilities			
(a) Short term borrowings	3	--	1,70,000
(b) Trade Payables		4,90,000	4,94,000
(c) Short-term provisions	4	3,10,000	4,30,000
Total		**15,86,000**	**23,08,000**
II. Assets			
(1) Non-current assets			
(a) Property, Plant and Equipment	5	2,72,000	2,24,000
(b) Non-current Investment			4,00,000
(2) Current assets			
(a) Inventories		5,97,000	7,42,000
(b) Trade Receivables		5,94,000	8,91,000
(c) Cash & Cash Equivalents		51,000	3,000
(d) Other current assets	6	72,000	48,000
Total		**15,86,000**	**23,08,000**

Notes to Accounts

		20X0 (₹)	20X1 (₹)
1.	**Share capital**		
	5,000 equity shares of ₹10 each, fully paid up	5,00,000	5,00,000
2.	**Reserves and Surplus**		
	General Reserves	2,86,000	7,14,000
3.	**Short term borrowings**		
	Bank overdraft	--	1,70,000
4.	**Short term provisions**		
	Provision for taxation	3,10,000	4,30,000
5.	**Property, plant and equipment**		
	Cost	3,20,000	3,20,000

Scanned with OKEN Scanner

	Less: Depreciation Total	(48,000)	(96,000)
6.	**Other current Assets**	2,72,000	2,24,000
	Prepaid expenses	72,000	48,000

Also consider the following information:

(a) B Ltd. is a subsidiary of A Ltd. Both the companies follow calendar year as the accounting year.

(b) A Ltd. values inventory on weighted average basis while B Ltd. used FIFO basis. To bring B Ltd.'s values in line with those of A Ltd, its value of inventory is required to be reduced by ₹12,000 at the end of 20X0 and ₹ 34,000 at the end of 20X1.

(c) B Ltd. deducts 1% from Trade Receivables as a general provision against doubtful debts.

(d) Prepaid expenses in B Ltd. include advertising expenditure carried forward of ₹ 60,000 in 20X0 and₹ 30,000 in 20X1, being part of initial advertising expenditure of ₹ 90,000 in 20X0 which is being written off over three years. Similar amount of advertising expenditure of A Ltd. has been fully written off in 20X0.

Restate the balance sheet of B Ltd. as at 31st December, 20X1 after considering the above information, for the purpose of consolidation. Would restatement be necessary to make the accounting policies adopted by A Ltd. and B Ltd. uniform.

SOLUTION

As per para 20 and 21 of AS 21, Consolidated financial statements:

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

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

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

Adjusted reserves of B Ltd.:

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

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

Restated Balance Sheet of B Ltd. as at 31st December, 2016

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

Scanned with OKEN Scanner

(2)	Current assets		
(a)	Inventories	6	7,08,000
(b)	Trade Receivables	7	9,00,000
(c)	Cash & Cash Equivalents		3,000
(d)	Other current assets	8	18,000
	Total		**22,53,000**

Notes to Accounts

			₹
1.	**Share Capital**		
	5,000 equity shares of ₹ 10 each, Fully Paid		5,00,000
2.	**Reserves and Surplus**		
	Reserves (refer to W.N.)		6,59,000
3.	**Short term borrowings**		
	Bank overdraft		1,70,000
4.	**Short-term provision**		
	Provision for taxation		4,30,000
5.	**Tangible Assets**		
	Cost	3,20,000	
	Less: Depreciation to date	(96,000)	2,24,000
6.	**Inventory**		
	Cost	7,42,000	
	Less: Adjustment because of change in method of valuation	(34,000)	7,08,000
7.	Trade receivables		
	Cost	8,91,000	
	Add: Provision adjustment	9,000	9,00,000
8.	**Other current assets**		
	Prepaid expenses (48,000 – 30,000)		18,000

QUESTION 87

Variety Ltd. holds 46% of the paid-up share capital of VR Ltd. The shares were acquired at a market price of ₹ 17 per share. The balance of shares of VR Ltd. are held by a foreign collaborating company. A memorandum of understanding has been entered into with the foreign company providing for the following:

(a) The shares held by the foreign company will be sold to Variety Ltd. The price per share will be calculated by capitalising the yield at 15%. Yield, for this purpose, would mean 40% of the average of pre-tax profits for the last 3 years, which were ₹ 30 lakhs, ₹ 40 lakhs and ₹ 65 lakhs.

(b) The actual cost of the shares to the foreign company was ₹ 5,40,000 only. The profit that would accrue to them would be taxable at an average rate of 30%. The tax payable will be deducted from the proceeds and Variety Ltd. will pay it to the Government.

(c) Out of the net consideration, 50% would be remitted to the foreign company immediately and the balance will be an unsecured loan repayable after two years.

The above agreement was approved by all concerned for being given effect to on 1.4.20X1. The total assets of VR Ltd. as on 31st March, 20X1 was ₹ 1,00,00,000. It was decided to write down Property, Plant and Equipment by ₹ 1,75,000. Current liabilities of VR Ltd. as on the same date were ₹ 20,00,000. The paid-up share capital of VR Ltd. was ₹ 20,00,000 divided into 2,00,000 equity shares of ₹ 10 each.

Find out goodwill/capital reserve to Variety Ltd. on acquiring wholly the shares of VR Ltd.

Scanned with OKEN Scanner

SOLUTION

1. Computation of Purchase Consideration

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

2. Goodwill / Capital Reserve to Variety Ltd.

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

QUESTION 88

As on 1/4/23	Reserves & Surplus is 5,20,000
On 1/6	Abnormal Gain is 9,000
On 1/8 (DOA)	Market Value of Fixed Asset – 25,00,000; Depreciation rate = 12%
On 1/10	Upstream Transaction at 25% on Cost; Unsold Goods = 1,25,000
On 1/3	Bonus @ 1:4
31/3/24	Reserves & Surplus is 9,30,000; Dividend declared is 12%

Standalone Balance Sheet as on 31/3/24

Particular	H Ltd.	S Ltd.
Equity Share Capital	12,00,000	10,00,000
Reserves & Surplus	10,00,000	9,30,000
Liabilities	19,00,000	11,70,000
	41,00,000	**31,00,000**
Fixed Asset	12,00,000	18,00,000
Investment @75%	15,00,000	-
Current Asset	14,00,000	13,00,000
	41,00,000	**31,00,000**

Note: Bonus entry is already Passed

SOLUTION:

Working Note 1: Revaluation & its Depreciation

(a)	Book Value as on 31/3/23	18,00,000
(b)	Book value as on 1/4/23 18,00,000/88%	20,45,454

Scanned with OKEN Scanner

(c)	Book value as on 1/8/23	19,63,636
(d)	Market value as on 1/8/23	25,00,000
(e)	FV Gain (d-c)	5,36,364
(f)	Depreciation for Post Acquisition Period actually Charged by S (c-a)	1,63,636
(g)	Depreciation that should be Charged on Market Value	2,00,000
(h)	Additional Depreciation (g-f)	36,364

Working Note 2: Calculation of Unrealised Profit on Unsold Goods with H

Unsold goods with H (i.e., Sale by S) = 1,25,000

Subsidiary Margin (25% on Cost) = 1/5 on Sales

Profit = 1,25,000/5 = 25,000

Working Note 3: Analysis of Profit of S:

	CP	RP	Balance Sheet
Balance of Reserves & Surplus	5,20,000	4,10,000	9,30,000
(-) Abnormal Gain	-	(9,000)	
(+/-) Bonus	(2,00,000)	2,00,000	
Balance	**3,20,000**	**6,01,000**	
(+/-) Time adjustment for 4M	2,00,333	(6,01,000 x 4/12)	
	5,20,333	**4,00,667**	
(+) Abnormal Gain	9,000	-	
(-) Dividend (4M Pre & 8M Post)	(40,000)	(80,000)	
(+/-) Revaluation effect	5,36,364	(36,364)	
(-) Unrealised Profit (WN.2)	-	(25,000)	
	10,25,697	**2,59,303**	
H 75%	7,69,273	1,94,477	
MI 25%	2,56,424	64,826	

* Dividend shall be calculated on ESC including Bonus is already declared before CY Dividend. 10,00,000 x 12% = 1,20,000

*Dividend entry not yet passed

Working Note 4: Cost of Control

Investment	15,00,000
(-) Pre-Acquisition Dividend	30,000
(-) 75% ESC	(7,50,000)
(-) Capital Profit Share	(7,69,273)
Capital Reserve	**49,273**

Working Note 5: Minority Interest

Equity Share Capital	2,50,000
Share in Capital Profit	2,56,424
Share in Revenue Profit	64,826
	5,71,250

Working Note 6: Consolidated Reserves & Surplus

(a) Consolidated Free Reserves		12,54,477
Balance with H	10,00,000	
(+) Revenue Profit Share of H	1,94,477	
(+) Post Acquisition Share of Dividend	60,000	
(+) (b) Capital Reserve		49,273
Consolidated Reserves & Surplus		**13,03,750**

Scanned with OKEN Scanner

Consolidated Balance Sheet

Particulars			Amount
Equity Share Capital			12,00,000
Consolidated Reserves & Surplus			13,03,750
Minority Interest			5,71,250
Liability			31,00,000
H		19,00,000	
S		11,70,000	
+ Dividend Payable to MI	30,000		
			61,75,000
Fixed Asset			35,00,000
H	12,00,000		
S	18,00,000		
+ FV	5,36,364		
(-) Depreciation	(36,364)		
Current Assets			26,75,000
H	14,00,000		
S	13,00,000		
(-) Unrealised Profit	(25,000)		
			61,75,000

Scanned with OKEN Scanner

14. AS – 23 INVESTMENT IN ASSOCIATES

QUESTION 89:

A Ltd. acquired 10% stake of B Ltd. on April 01 and further 15% on October 01 during the same year. Other information is as follow:

Cost of Investment for 10% ₹ 1,00,000 and for 15% ₹ 1,45,000

Net asset on April 01 ₹ 8,50,000 and on October 01 ₹ 10,00,000.

Calculations for April 01:

Cost of investment	₹ 1,00,000
10% share in net asset	₹ 85,000
Goodwill	₹ 15,000

Calculations for October 01:

15% share in net asset	₹ 1,50,000
Cost of investment	₹ 1,45,000
Capital Reserve	₹ 5,000
Total goodwill (15,000 – 5,000)	₹ 10,000

QUESTION 90:

A Ltd. acquired 10% stake of B Ltd. on April 01 and further 15% on 1st October of the same year. Other information is as follow:

Cost of Investment for 10% ₹ 1,00,000 and for 15% ₹ 1,55,000

Net asset on 1st April ₹ 8,50,000 and on 1st October ₹ 10,00,000.

Calculations for April 01:

Cost of investment	₹ 1,00,000
10% share in net asset	₹ 85,000
Goodwill	₹ 15,000

Calculations for October 01:

Cost of investment	₹ 1,55,000
15% share in net asset	₹ 1,50,000
Goodwill	₹ 5,000
Total goodwill (15,000 + 5,000)	₹ 20,000

Case 2: Further acquisition in an associate in the same year:

QUESTION 91:

A Ltd. acquired 25% stake of B Ltd. on 1st April and further 5% on 1st October of the same year. Other information is as follow:

Cost of Investment for 25% ₹ 1,50,000 and for 5% ₹ 20,000

Net asset on 1st April ₹ 5,00,000.

Profit for the year ₹ 90,000 earned in the ratio 2:1 respectively.

Calculations for April 01:

Cost of investment	₹ 1,50,000
25% share in net asset	₹ 1,25,000
Goodwill	₹ 25,000

Scanned with OKEN Scanner

Calculations for October 01:

Profits for the first half (90,000/3) x 2	**₹ 60,000**
Additional share of A Ltd.	5%
Pre-acquisition profits i.e. capital reserve (60,000 x 5%)	₹ 3,000
5% share in net asset	₹ 25,000
Cost of investment	₹ 20,000
Capital Reserve	₹ 5,000
Cost of Investment on April 01	₹ 1,50,000
Less: Goodwill	₹ 25,000
Carrying Amount on April 01	₹ 1,25,000
Add: Additional Share in Net Asset on October 01	₹ 25,000
Add: Capital share of Profits for first half	₹ 3,000
Add: Revenue shares of Profits for first half (60,000 x 25%)	₹ 15,000
Add: Revenue shares of Profits for second half (30,000 x 30%)	₹ 9,000
Total Carrying Amount on March 31	**₹ 1,77,000**

QUESTION 92

On 01/04/23 Investments (25%) in Associate purchased at a Cost of 4,00,000. ESC & R&S as on 01/04/23 are 10,00,000 and 5,00,000. On 1st June, Dividend paid by Associate 50,000 & also received by Investor. Closing Balance Of R&S of Associate is 8,00,000 as on 31/03/24. show Equity method Accounting on DOA & on 31/03/24.

Solution:-

1) **Equity method on DOA**

Investment Cost	4,00,000
(-) Proportionate share in Net Assets of Associate Co. @25%:	
• ESC (10,00,000 ×25%)	(2,50,000)
• CP (4,50,000×25%)	(1,12,500)
Goodwill	**37,500**

2) **Analysis of Profit of Associate:-**

Particular	Pre-Acquisition Period Profit	Post Acquisition Period Profit	Balance on Balance Sheet
R&S	5,00,000	3,00,000	8,00,000
(+) Dividend	-	50,000	
Balance	5,00,000	3,50,000	
(+/-) Time adjustment	-	-	
(-) Dividend	(50,000)	-	
	4,50,000	3,50,000	
Share of Investor in Profits @ 25%	**1,12,500**	**87,500**	

3) **Equity method as B/S date :-**

Investment as on DOA (Including Goodwill – 37,500)	4,00,000
(+) Share in Post-Acquisition Profit (3,50,000 × 25%)	87,500
Investment Closing Balance 31/03/24	**4,87,500**

QUESTION 93

In Continuation of above **Q1,** During FY 24-25, suppose Associate co. earned Net profit after Tax of 3,00,000 & Distributed Dividend of 60,000

Scanned with OKEN Scanner

Solution:

Important Analysis:

Equity Method on 01/4/23	Equity Method on 31/03/24	Equity Method on 31/3/25
Net Assets - 14,50,000 Proportionate Share @25% is 3,62,500 + 37,500 Goodwill	Net Assets - 18,00,000 Proportionate Share @ 25% is 4,50,000 + 37,500 Goodwill	Net Assets - 20,40,000 Proportionate Share @ 25% is 5,10,000 + 37,500 Goodwill

Equity Method as on 31/03/25:-

Opening Balance (Carrying Amount) of Investment as on 01/04/24 (including Goodwill 37,500)	4,87,500
(+) Share in Post Acquisition profit 3,00,000 × 25%	75,000
(-) Dividend Received by Investor 60000 × 25%	(15,000)
Carrying Amount of Investments as on 31/03/25 (including Goodwill 37,500)	**5,47,500**

QUESTION 94

Date of Acquisition of Investments	01/04/23
Investment Cost @ 30%	2,70,000
ESC of Associate co. as on (01/04/23)	5,00,000
R&S as on (01/04/23)	3,00,000

On 01/04/23, One PPE whose BV was 7,00,000 having FV was 9,00,000 Depreciation rate = 10% Net profit of Associate for 23-24 is 2,00,000.

Apply Equity method:

a) On DOA; and

b) On B/S date

Solution:-

Alternate 1

1. Equity Method as on DOA

Investment cost	2,70,000
(-) Prop. Net Assets at FV	
ESC (BV)	1,50,000
R&S (BV)	90,000
FV Gain (9-7 × 30%)	60,000
Capital Reserve	**30,000**
Investment A/c Dr.	30,000
To Capital Reserve A/c	30,000
Revised Investment as on DOA (as per Equity method)	**3,00,000**

2. Equity method as B/S date

Carrying Amt. of Investment cost	3,00,000
(+) Share in Post-Acquisition profit	60,000
(-) Share in additional dep due to PPE FV (20,000 x 30%)	6,000
Revised Investment as on B/s Date (as per Equity method)	**3,54,000**

Alternate 2

AOP of Associate

Particulars	Pre-Profits	Post-Profits	On B/S Date
Reserves & Surplus	3,00,000	2,00,000	5,00,000
(+) FV of PPE	2,00,000	-	
(-) Additional Depreciation	-	(20,000)	
Final Balance	**5,00,000**	**1,80,000**	
Share of Investor @ 30%	1,50,000	54,000	

Equity Method as on DOA & B/S

Investment cost	2,70,000
(-) Prop. Net Assets at FV	
ESC (BV)	1,50,000
Pre-Acquisition Profit	1,50,000
Capital Reserve	**30,000**
Revised Investment as on DOA (as per Equity method)	3,00,000
(+) Share in Post-Acquisition Profit	54,000
Carrying Amount of Investment as on BS date	**3,54,000**

Scanned with OKEN Scanner

QUESTION 95

Bright Ltd. acquired 30% of East India Ltd. shares for ₹ 2,00,000 on 01-06-20X1. By such an acquisition Bright can exercise significant influence over East India Ltd. During the financial year ending on 31-03-20X1 East India earned profits ₹ 80,000 and declared a dividend of ₹ 50,000 on 12-08-20X1. East India reported earnings of ₹ 3,00,000 for the financial year ending on 31-03-20X2 (assume profits to accrue evenly) and declareddividends of ₹ 60,000 on 12-06-20X2.

Calculate the carrying amount of investment in:

(i) Separate financial statements of Bright Ltd. as on 31-03-20X2;

(ii) Consolidated financial statements of Bright Ltd.; as on 31-03-20X2;

(iii) What will be the carrying amount as on 30-06-20X2 in consolidated financial statements?

SOLUTION

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

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

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

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

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

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

QUESTION 96

A Ltd. acquired 25% of shares in B Ltd. as on 31.3.20X1 for ₹ 3 lakhs. TheBalance Sheet of B Ltd. as on 31.3.20X1 is given below:

	₹
Share Capital	5,00,000
Reserves and Surplus	5,00,000
	10,00,000
Fixed Assets	5,00,000
Investments	2,00,000
II. Current Assets	3,00,000
	10,00,000

During the year ended 31.3.20X2 the following are the additional informationavailable:

1) A Ltd. received dividend from B Ltd., for the year ended 31.3.20X1 at40% from the Reserves.
2) B Ltd., made a profit after tax of ₹ 7 lakhs for the year ended 31.3.20X2.
3) B Ltd., declared a dividend @ 50% for the year ended 31.3.20X2 on30.4.20X2.

A Ltd. is preparing Consolidated Financial Statements in accordance with AS21 for its various subsidiaries. Calculate:

(i) Goodwill if any on acquisition of B Ltd.'s shares.

Scanned with OKEN Scanner

(ii) How A Ltd., will reflect the value of investment in B Ltd., in theConsolidated Financial Statements?

(iii) How the dividend received from B Ltd. will be shown in the ConsolidatedFinancial Statements?

SOLUTION

In terms of AS 23, B Ltd. will be considered as an associate company ofA Ltd. as shares acquired represent to more than 20%.

(i) Calculation of Goodwill

	(₹ in lakhs)
Amount paid towards acquisition of stake in B Ltd.	3.00
Less: Pre-acquisition dividend (₹5,00,000 x 40% x 25%)	0.50
Cost of Investment in B Ltd.	2.50
Less: Share in the value of Equity of B Ltd.as at the date of investment [25% of ₹10 lakhs (₹5 lakhs + ₹5 lakhs)]	(2.50)
Goodwill	**NIL**

(ii) A Ltd.

Consolidated Profit and Loss Account for the year ended 31st March, 20X2

(An extract)

		₹ in lakhs
Other income:		
Share of profits in B Ltd.		1.75
Pre-acquisition Dividend received from B Ltd.	0.50	
Transfer to investment A/c	(0.50)	Nil

Consolidated Balance Sheet as on 31.3.20X2 (An extract)

		₹ in lakhs
Non-current investments		
Investment in B Ltd.		
Cost of Investment in B Ltd.	2.50	
Share of profit for year 20X1 – 20X2	1.75	
	4.25	
Add: Goodwill	NIL	4.25

Working Notes:

1. Pre-acquisition dividend received from B Ltd. amounting to ₹0.50 lakhs will be reduced from investment value in the booksof A Ltd.
2. B Ltd. made a profit of ₹7 lakhs for the year ended 31st March, 20X2. A Ltd.'s share in the profits of ₹7 lakhs is ₹1.75 lakhs.
3. Investment in B Ltd. will be increased by ₹1.75 lakhs and consolidated profit and loss account of A Ltd. will be creditedwith ₹1.75 lakhs in the consolidated financial statement of A Ltd.
4. Dividend declared on 30th April, 20X2 will not be recognized in the consolidated financial statement of A Ltd.

Scanned with OKEN Scanner

15. AS – 27 JOINT VENTURES

QUESTION 97

Balance Sheet of J Ltd. (31/3/24)

Equity Share Capital	10,00,000
Reserves and Surplus	6,00,000
Liabilities	14,00,000
	30,00,000
Non-Current Assets	18,00,000
Current Assets	12,00,000
	30,00,000

- J Ltd. is a J.V. Of A Ltd. & B Ltd. with 50% Investment by each.
- A Ltd. Invested in J Ltd. on 1/4/23, When R&S Balance of J Ltd. was 2,00,000/-
- Investment made by A Ltd. Was 6,50,000
- How A Ltd Shall accounts for this Investment in J Ltd. in its Consolidated Financial Statement.

Solution:-

A Ltd. (Venturer) Shall apply Proportionate Consolidation Method as under :-

Working Note 1 - Cost of Control as on DOA

Investment Cost	6,50,000
(-) 50% of Net Assets ESC 10 Lacs × 50% Pre-Acquisition Profit 2 Lacs × 50%	 (5,00,000) (1,00,000)
Goodwill	**50,000**

Working Note 2 - Share in Post Acquisition Profit of JCE :-

4,00,000 × 50% = 2,00,000

(Note: Minority Interest will never be Calculated)

A Ltd.

Consolidation B/s (Extract)

Equity Share Capital	XXX
Consolidated R&S :- A's Balance + Post Acquisition Profit Share	 XXX 2,00,000
Liability A Ltd. Share in JV	XXX 7,00,000
Non-Current Assets A Ltd. JV	 XXX 9,00,000
Goodwill Current Assets A Ltd. JV	50,000 XXX 6,00,000

QUESTION 98

A Ltd. is a Venturer has invested in a JV AB Ltd. with 50% Share. Another Venturer is B Ltd. A Ltd. sold one Asset to JV (AB Ltd.) whose cost is Rs. 1,00,000 and Sold at 1,25,000. How to treat this transaction in the books of A Ltd. and B Ltd. Describe with the help of Journal Entry.

Scanned with OKEN Scanner

Answer

A Ltd. has total Gain of 25,000 out of which 12,500 (50% share) earned from B Ltd. (i.e. Outside party) and rest 12,500 earned from itself. A Ltd. shall not record its own share of Gain earned from itself.

Books of JV (AB Ltd. – Purchaser)	Books of B Ltd. (Venturer)	Books of A Ltd. (Seller and Venturer)
Asset A/c Dr. 1,25,000 To A Ltd. 1,25,000	Share in JV's Asset Dr. 62,500 To Share in JV's Liability (A Ltd.) A/c 62,500	B Ltd. A/c Dr. 62,500 Share in JV's Asset Dr. 50,000 To Assets A/c 1,00,000 To Gain on Sale A/c 12,500

QUESTION 99

AB Ltd. (JV of A Ltd. and B Ltd.) sold one Asset costing Rs. 1,00,000 to A Ltd. at 1,30,000. Pass necessary journal entries.

Answer

JV Ltd. has total Gain of 30,000 out of which 15,000 (50% share) of B Ltd. (i.e. Outside party) and 15,000 of A Ltd. A Ltd. shall not record its own share of Gain earned from itself.

Books of JV (AB Ltd. – Seller)	Books of B Ltd. (Venturer)	Books of A Ltd. (Purchaser and Venturer)
A Ltd. A/c Dr. 1,30,000 To Asset A/c 1,00,000 To Gain A/c 30,000	A Ltd. A/c Dr. 65,000 To Share in Asset A/c 50,000 To Gain A/c 15,000	Asset A/c Dr. 1,15,000 To B Ltd. A/c 65,000 To Share in Asset A/c 50,000

QUESTION 100

A Ltd. a UK based company entered into a joint venture with B Ltd. in India, wherein B Ltd. will import the goods manufactured by A Ltd. on account of joint venture and sell them in India. A Ltd. and B Ltd. agreed to share the expenses & revenues in the ratio of 5:4 respectively whereas profits are distributed equally. A Ltd. invested 49% of total capital but has equal share in all the assets and is equally liable for all the liabilities of the joint venture.

Following is the trial balance of the joint venture at the end of the first year:

Particulars	Dr. (₹)	Cr. (₹)
Purchases	9,00,000	
Other Expenses	3,06,000	
Sales		13,05,000
Property, Plant and Equipment	6,00,000	
Current Assets	2,00,000	
Unsecured Loans		2,00,000
Current Liabilities		1,00,000
Capital		4,01,000

Closing inventory was valued at ₹ 1,00,000.

You are required to prepare the Consolidated Financial Statement.

Solution

Consolidated Profit & Loss Account

Particulars	Note No.	(₹)
Revenue from operations	1	13,05,000
Total Revenue (A)		13,05,000
Less: Expenses		
Purchases	2	9,00,000
Other expenses	3	3,06,000
Changes in inventories of finished goods	4	(1,00,000)
Total Expenses (B)		11,06,000
Profit Before Tax (A-B)		1,99,000

Scanned with OKEN Scanner

Consolidated Balance Sheet

		Note No.	(₹)
I	**Equity and liabilities**		
	1. Shareholders' funds:		
	Share Capital	5	4,01,000
	Reserves and Surplus	6	1,99,000
	2. Non-current liabilities		
	Long term borrowings	7	2,00,000
	3. Current Liabilities	8	1,00,000
			9,00,000
II	**Assets**		
	Non-current Assets		
	Property, Plant and Equipment	9	6,00,000
	Current Assets		
	Inventories	10	1,00,000
	Other current assets	11	2,00,000
			9,00,000

Notes to Accounts

	Particulars		(₹)
1.	**Revenue from operations**		
	Sales:		
	A Ltd.	7,25,000	
	B Ltd.	5,80,000	13,05,000
2.	**Purchases**		
	A Ltd.	5,00,000	
	B Ltd.	4,00,000	9,00,000
3.	**Other expenses**		
	A Ltd.	1,70,000	
	B Ltd.	1,36,000	3,06,000
4.	**Closing Inventory**		
	A Ltd.	50,000	
	B Ltd.	50,000	1,00,000
5.	**Share Capital**		
	A Ltd.	1,96,490	
	B Ltd.	2,04,510	4,01,000
6.	**Reserves and Surplus**		
	Profit & Loss Account:		
	A Ltd.	99,500	
	B Ltd.	99,500	1,99,000
7.	**Long Term Borrowings**		
	Unsecured Loans:		
	A Ltd.	1,00,000	
	B Ltd.	1,00,000	2,00,000
8.	**Current Liabilities**		
	A Ltd.	50,000	
	B Ltd.	50,000	1,00,000
9.	**Property, Plant and Equipment**		
	A Ltd.	3,00,000	
	B Ltd.	3,00,000	6,00,000

Scanned with OKEN Scanner

10.	Inventories		
	A Ltd.	50,000	
	B Ltd.	50,000	1,00,000
11.	Other Current Assets		
	A Ltd.	1,00,000	
	B Ltd.	1,00,000	2,00,000

QUESTION 101

Standalone Balance sheets on 31/03/24

Particular	H	S	JV	ASS
ESC 10/- face Value	10,00,000	8,00,000	6,00,000	50,000
R&S	9,00,000	75,000	4,50,000	3,00,000
Liability	11,00,000	6,50,000	5,50,000	4,00,000
	30 Laksh	22 Laksh	16 Laksh	12 Laksh
Investments:				
In S 80%	11,00,000	-	-	-
In JV 50%	5,00,000	-	-	-
In Ass. 30%	1,60,000	-	-	-
Other Assets	12,40,000	22,00,000	16,00,000	12,00,000

1) Date of Acquisition of all Investments is 01/07/23.
2) Opening Balance of R&S on 01/04/23

S Ltd.	4,80,000
JV Ltd.	1,50,000
Associate Ltd.	1,20,000

Prepare Consolidated Balance Sheet for H Ltd.

Solution:-

1) **Subsidiary Consolidation**

Analysis of Profit (AOP)			
Particulars	**Pre**	**Post**	**B/S**
R&S	4,80,000	2,70,000	7,50,000
(+/-) Time Adjustement	67,500	(2,70,000 × 3/12)	
	5,47,500	**2,02,500**	
Share of H Ltd.	4,38,000	1,62,000	
Share of M/I	1,09,500	40,500	

Minority Interest		
ESC	20%	1,60,000
(+) Pre-Acquisition	20%	1,09,500
(+) Post Acquisition	20%	40,500
		3,10,000
Cost of Control (COC)		
Investments in S Ltd.		11,00,000
(-) 80% Net Assets ESC 80% Share of Pre-Acquisition Profit		 (6,40,000) (4,38,000)
Goodwill		**22,000**

Scanned with OKEN Scanner

2) JV (Proportionate Consolidation Method)

Analysis of Profit (AOP)			
Particulars	**Pre**	**Post**	**B/S**
R&S	1,50,000	3,00,000	4,50,000
(+/-) Time Adjustment	75,000	(3,00,000 × 3/12)	
	2,25,000	2,25,000	
H 50%	**1,12,500**	**1,12,500**	

Cost of Control	
Investment	5,00,000
(-) 50% of Net Assets ESC 50% Share of Pre Acquisition	 3,00,000 1,12,500
Goodwill	**87,500**

3) Associate Consolidation (Equity Method):

Analysis of Profit			
	Pre	**Post**	**B/S**
R&S	1,20,000	1,80,000	3,00,000
(+/-) Time Adjustment	45,000	(1,80,000×3/12)	
	1,65,000	**1,35,000**	

Equity Method	
Investment Cost	1,60,000
(-) 30% N. Assets as on DOA	1,99,500
Equity Share Capital 5,00,000 Share of Pre-Acquisition 1,65,000 6,65,000 × 30%	
Capital Reserve on DOA (Investment to be Increased by 39,500)	39,500
Revised Carrying Amount of Investment	1,99,500
(+) Share in Post-Acquisition Period Profit 1,35,000× 30%	40,500
Closing Investment as on Balance Sheet	2,40,000

Consolidated P&L A/c of H Ltd.

Balance of R&S of H Ltd. as per SFS	9,00,000
(+) Share in Post Acquisition profit	
From S Ltd.	1,62,000
From JV Ltd.	1,12,500
From Associate Ltd.	40,500
Consolidation P&L	1,21,500
Capital Reserve from COC	39,500
Consolidation R&S	**12,54,500**

Consolidated Balance Sheet

Particulars	**Amount**
Equity Share Capital	10,00,000
Consolidation Reserves and Surplus	12,54,500
Minority Interest	3,10,000
Liability H 11,00,000	20,25,000
S 6,50,000	

Scanned with OKEN Scanner

JV 2,75,000	
	45,89,500
Investment in Associate as per Equity Method	2,40,000
Other Assets H 12,40,000	
I 22,00,000	
JV 8,00,000	
Goodwill S 22,000	1,09,500
JV 87,500	
	45,89,500

Scanned with OKEN Scanner

16. AS 2 - INVENTORIES

QUESTION 102

The closing inventory at cost of a company amounted to Rs. 2,84,700. The following items were included at cost in the total:

(a) 400 coats, which had cost Rs. 80 each and normally sold for Rs. 150 each. Owing to a defect in manufacture, they were all sold after the balance sheet date at 50% of their normal price. Selling expenses amounted to 5% of the proceeds.

(b) 800 skirts, which had cost Rs. 20 each. These too were found to be defective. Remedial work in April cost Rs. 5 per skirt, and selling expenses for the batch totaled Rs. 800. They were sold for Rs. 28 each.

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

Answer:

Valuation of Closing Stock

Particulars	Rs.	Rs.
Closing Stock at cost		2,84,700
Less: adjustment required for 400 defected coats		3,500
Cost of 400 coats (400 x 80)	32,000	
Net Realisable Value [400 x (75 – 5% of Rs. 75)]	28,500	
(400 coats should be measured at NRV which is lower i.e. 28,500 therefore adjustment of 3500 is required)		
Value of Closing Stock		**2,81,200**

Note: There is no adjustment for skirts because for skirts were sold at above cost.

QUESTION 103

A Limited is engaged in manufacturing of Chemical Y for which Raw Material X is required. The company provides you following information for the year ended 31st March,2020.

	Rs. Per unit
Raw Material X	
Cost price	400
Freight Inward	40
Replacement cost	320
Chemical Y	
Material consumed	440
Direct Labour	120
Variable Overheads	80

Additional Information:

(a) Total fixed overhead for the year was Rs. 4,00,000 on normal capacity of 25,000 units.

(b) Closing balance of Raw Material X was 1,000 units and Chemical Y was 2,400 units.

You are required to calculate the total value of closing stock of Raw Material X and Chemical Y according to AS 2, when Net realizable value of Chemical Y is Rs. 600 per unit.

SOLUTION

Net Realizable Value of the Chemical Y (Finished Goods) is Rs. 600 per unit which is less than its cost Rs. 656 per unit. Hence, Raw Material is to be valued at replacement cost and Finished Goods are to be valued at NRV since NRV is less than the cost.

Value of Closing Stock:

Scanned with OKEN Scanner

	Qty.	Rate (Rs.)	Amount (Rs.)
Raw Material X	1,000	320	3,20,000
Finished Goods Y	2,400	600	14,40,000
Total Value of Closing Stock			17,60,000

Working Note:

Statement showing cost calculation of Raw material X and Chemical Y

Raw Material X	**Rs.**
Cost Price	400
Add: Freight Inward	40
Cost	440
Chemical Y	**Rs.**
Materials consumed	440
Direct Labour	120
Variable overheads	80
Fixed overheads (Rs.4,00,000/25,000 units)	16
Cost	656

QUESTION 104

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

Details of cost for these products are:

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

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

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

SOLUTION

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

Product – A

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

Product – B

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

Scanned with OKEN Scanner

QUESTION 105

Following information of Sarah Limited is given:

Sarah Limited uses Raw Material 'A' for production of production of Finished Goods 'B'

Closing balance of Raw Material 'A' in units on 31st March, 2022	750
	Price Per Unit in ₹
Cost Price	150
Freight inward	10
Replacement Cost	152
Closing balance of Finished Good 'B' in units on 31st March,2022	1,600
	Price Per Unit in ₹
Material Consumed	225
Direct Labour	75
Direct variable overhead	60

Total Fixed Overheads amounts to ₹ 1,00,000 on normal capacity of 20,000 units.

You are required to calculate the value of Closing Stock of Raw materials and Closing Stock of Finished Goods, as on 31st March, 2022, as per AS 2, when selling price of Finished Goods 'B' is ₹ 360 per unit.

SOLUTION

Raw Material A	**₹**
Cost Price	150
Add: Freight Inward	10
Cost per unit	160
Replacement cost per unit of raw material	152

As per AS 2 (Revised) "Valuation of Inventories", the inventories are to be valued at lower of cost or net realizable value. Materials and other supplies held for use in the production of inventories are written down below cost if the selling price of finished product containing the material does not exceed the cost of the finished product. In the given case, net realizable value of the Product 'B' (Finished Goods) is ₹ 360 per unit which is less than its cost ₹ 365 per unit. Raw Material is to be valued at replacement cost.

Value of the closing stock of raw material on 31/03/2022 would be ₹ 1,14,000 (750 units X ₹152 per unit).

Finished Goods B	**₹**
Materials consumed	225
Direct Labour	75
Direct Variable overheads	60
Fixed overheads (₹ 1,00,000/20,000 units)	5
Cost per unit	365
Net realizable value per unit	360

As per AS 2 (Revised) "Valuation of Inventories", the inventories are to be valued at lower of cost or net realizable value. Hence, Finished Goods are to be valued at NRV since NRV is less than the cost.

Value of the closing stock of Finished goods as on 31/03/2022 would be ₹ 5,76,000 (1,600 units X ₹ 360 per unit).

QUESTION 106

Particulars		**Kg.**	**Rs**
Opening Inventory:	Finished Goods	1,000	25,000
	Raw Materials	1,100	11,000
Purchases of Raw Material		10,000	1,00,000
Labour			76,500
Overheads (Fixed)			75,000
Sales		10,000	2,80,000
Closing Inventory:	Raw Materials	900	
	Finished Goods	1200	

Scanned with OKEN Scanner

The expected production for the year was 15,000 kg of the finished product. Due to fall in market demand the sales price for the finished goods was Rs. 20 per kg and the replacement cost for the raw material was Rs. 9.50 per kg on the closing day. You are required to calculate the closing inventory as on that date.

SOLUTION

Calculation of cost for closing inventory

Particulars	Rs
Cost of Purchase (10,200 x 10)	1,02,000
Direct Labour	76,500
Fixed Overhead 75,000X10,200/15,000	51,000
Cost of Production	2,29,500
Cost of closing inventory per unit (2,29,500/10,200)	Rs 22.50
Net Realisable Value per unit	Rs 20.00

Since net realisable value is less than cost, closing inventory will be valued at Rs. 20.

As NRV of the finished goods is less than its cost, relevant raw materials will be valued at replacement cost i.e. Rs. 9.50.

Therefore, value of closing inventory: Finished Goods (1,200 x 20) Rs. 24,000

Raw Materials (900 x 9.50) =Rs. 8,550

Total =Rs. 32,550

Scanned with OKEN Scanner

17. AS 13 - INVESTMENTS

QUESTION 107

On 1.4.20X1, Sundar had 25,000 equity shares of 'X' Ltd. at a book value of ₹ 15 per share (Nominal value ₹ 10). On 20.6.20X1, he purchased another 5,000 shares of the company at ₹16 per share. The directors of 'X' Ltd. announced a bonus and rights issue. No dividend was payable on these issues. The terms of the issue are as follows:

Bonus basis 1:6 (Date 16.8.20X1).

Rights basis 3:7 (Date 31.8.20X1) Price ₹ 15 per share. Due date for payment 30.9.20X1.

Shareholders were entitled to transfer their rights in full or in part. Accordingly, Sundar sold 33.33% of his entitlement to Sekhar for a consideration of ₹ 2 per share.

Dividends: Dividends for the year ended 31.3.20X1 at the rate of 20% were declared by X Ltd. and received by Sundar on 31.10.20X1. Dividends for shares acquired by him on 20.6.20X1 are to be adjusted against the cost of purchase.

On 15.11.20X1, Sundar sold 25,000 equity shares at a premium of ₹ 5 per share. You are required to prepare in the books of Sundar.

1. Investment Account
2. Profit & Loss Account.

For your exercise, assume that the books are closed on 31.12.20X1and shares are valued at average cost.

Solution

Books of Sundar Investment Account
(Scrip: Equity Shares in X Ltd.)

		No.	Amount ₹			No.	Amount ₹
1.4.20X1 20.6.20X1	To Bal b/d To Bank	25,000 5,000	3,75,000 80,000	31.10.20X1	By Bank (dividend on shares acquired on 20/6/20X1) (W.N.4)	—	10,000
16.8.20X1 30.9.20X1	To Bonus (W.N.1) To Bank (Rights Shares) (W.N.3)	5,000 10,000	— 1,50,000	15.11.20X1	By Bank (Sale of shares)	25,000	3,75,000
15.11.20X1	To Profit (on sale of shares)		44,444	31.12.20X1	By Bal. c/d (W.N.6)	20,000	2,64,444
		45,000	**6,49,444**			**45,000**	**6,49,444**

Profit and Loss Account (An extract)

To Balance c/d	1,04,444	By Profit transferred	44,444
		By Sale of rights (W.N.3)	10,000
	-	By Dividend (W.N.4)	50,000
	1,04,444		**1,04,444**

Working Notes:

1. Bonus Shares = (25,000 + 5,000)/6 = 5,000 shares
2. Right shares = (25,000 + 5,000 + 5,000) / 7 x 3 = 15,000 shares
3. Right shares renounced = 15,000×1/3 = 5,000 shares

   Sale of right shares = 5,000 x 2 = ₹ 10,000

   Right shares subscribed = 15,000 – 5,000 = 10,000 shares

   Amount paid for subscription of right shares = 10,000 x 15 = ₹ 1,50,000
4. Dividend received = 25,000 (shares as on 1st April 20X1) × 10 × 20% = ₹ 50,000

   Dividend on shares purchased on 20.6.20X1 = 5,000×10×20% = ₹ 10,000 is adjusted to Investment A/c
5. Profit on sale of 25,000 shares = Sales proceeds – Average cost

Scanned with OKEN Scanner

Sales proceeds = ₹ 3,75,000

Average Cost = (3,75,000 + 80,000 + 1,50,000 – 10,000) / 45,000 x 25,000 = ₹ 3,30,556

Profit = ₹ 3,75,000 – ₹ 3,30,556 = ₹ 44,444

6. Cost of shares on 31.12.20X1

(3,75,000 + 80,000 + 1,50,000 – 10,000) / 45,000 x 20,000 = ₹ 2,64,444

QUESTION 108

The following information is presented by Mr. Z (a stock broker), relating to his holding in 9% Central Government Bonds.

Opening balance (nominal value) ₹ 1,20,000, Cost ₹ 1,18,000 (Nominal value of each unit is ₹ 100).

Date	Details
1.3.20X1	Purchased 200 units, ex-interest at ₹ 98.
1.7.20X1	Sold 500 units, ex-interest out of original holding at ₹ 100.
1.10.20X1	Purchased 150 units at ₹ 98, cum interest.
1.11.20X1	Sold 300 units, ex-interest at ₹ 99 out of original holdings.

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

Solution

In the Books of Mr. Z

9% Central Government Bonds (Investment) Account

Particulars		Nominal Value	Interest	Principal	Particulars		Nominal Value	Interest	Principal
20X1		**₹**	**₹**	**₹**	**20X1**		**₹**	**₹**	**₹**
Jan.1	Balance b/d (W.N.1)	1,20,000	2,700	1,18,000	Mar. 31	By Bank A/c (W.N.3)	-	6,300	-
March 1	To Bank A/c (W.N.2)	20,000	750	19,600	July 1	By Bank A/c (W.N.4)	50,000	1,125	50,000
July 1	P&L A/c (W.N.5)	-	-	833	Sept. 30	By Bank A/c (W.N.6)	-	4,050	-
Oct. 1	To Bank A/c (150 x 98)	15,000	-	14,700	Nov. 1	By Bank A/c (W.N.7)	30,000	225	29,700
Nov. 1	To P&L A/c (W.N.8)	-	-	200	Dec. 31	By Balance c/d (W.N. 9 & W.N.10)	75,000	1,688	73,633
Dec. 31	To P&L A/c (b.f.) (Transfer)		9,938						
		1,55,000	**13,388**	**1,53,333**			**1,55,000**	**13,388**	**1,53,333**

Working Note:

1. Interest element in opening balance of bonds = 1,20,000 x 9% x 3/12 = ₹ 2,700
2. Purchase of bonds on 1. 3.20X1

   Interest element in purchase of bonds = 200 x 100 x 9% x 5/12 = ₹ 750

   Investment element in purchase of bonds = 200 x 98 = ₹ 19,600
3. Interest for half-year ended 31 March = 1,400 x 100 x 9% x 6/12 = ₹ 6,300

Scanned with OKEN Scanner

4. Sale of bonds on 1.7.20X1

Interest element = 500 x 100 x 9% x 3/12 = ₹ 1,125

Investment element = 500 x 100 = ₹ 50,000

5. Profit on sale of bonds on 1.7.20X1

Cost of bonds = (1,18,000/ 1,200) x 500 = ₹ 49,167

Sale proceeds = ₹ 50,000

Profit element = ₹ 833

6. Interest for half-year ended 30 September

= 900 x 100 x 9% x 6/12 = ₹ 4,050

7. Sale of bonds on 1.11.20X1

Interest element = 300 x 100 x 9% x 1/12 = ₹ 225

Investment element = 300 x 99 = ₹ 29,700

8. Profit on sale of bonds on 1.11.20X1

Cost of bonds = (1,18,000/ 1,200) x 300 = ₹ 29,500

Sale proceeds = ₹ 29,700

Profit element = ₹ 200

9. Closing value of investment

Calculation of closing balance:	**Nominal value**		**₹**
Bonds in hand remained in hand at 31st December 20X1			
From original holding (1,20,000 – 50,000 – 30,000)	40,000	1,18,000/1,20,000 x 40,000	39,333
Purchased on 1st March	20,000		19,600
Purchased on 1st October	15,000		14,700
	75,000		73,633

10. Interest element in closing balance of bonds = 750 x 100 x 9% x 3/12 = ₹ 1,688

QUESTION 109

Mr. Z has made following transactions during the financial year 2020-21:

Investment in 8% Corporate Bonds having face value Rs. 100/-

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

Interest on the bonds is received on 30th September and 31st March. Investment 2:

Equity Shares of G Ltd having face value Rs. 10

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

Scanned with OKEN Scanner

25-01-2021	Received interim dividend @ Rs. 3 per share for the year 2020-21.
31-03-2021	The shares were quoted in the stock exchange @ Rs. 260.

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

You are required to:

(i) Prepare Investment Accounts in the books of Mr. Z for the year 2020-21, assuming that the average cost method is followed.

(ii) Profit and loss Account for the year 2020-21, based on the above information.

Suggest values at which investment in equity shares should be reclassified in accordance with AS 13.

SOLUTION

(i) **In the books of Mr. Z**

Investment in 8% Corporate Bonds Account

For the period 01 April 2020 to 31 March 2021

Date	Particulars	No's	Interest (Rs.)	Amount (Rs.)	Date	Particulars	No's	Interest (Rs.)	Amount (Rs.)
1/6/20	To Bank A/c (WN1)	36,000	48,000	30,48,000	30/9/20	By Bank A/c (Interest 36,000 x 100 x 8% x 6/12)		1,44,000	
15/2/21	To P & L A/c (WN 3)			1,76,000	15/2/21	By Bank A/c (WN2)	24,000	72,000	22,08,000
31/3/21	To P & L A/c		2,16,000		31/3/21	By Bank A/c (Interest 12,000 x 100 x 8% x 6/12)		48,000	
						By Balance c/d (WN 4)	12,000		10,16,000
	Total	**36,000**	**2,64,000**	**32,24,000**		**Total**	**36,000**	**2,64,000**	**32,24,000**

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

Investment in Equity Shares of Z Ltd

For the period 1st April 2020 to 31 March 2021

Date	Particulars	No's	Dividend (Rs.)	Amount (Rs.)	Date	Particulars	No's	Dividend (Rs.)	Amount (Rs.)
01/4/20	To balance b/d	8,000		15,20,000	16/9/20	By Bank A/c (WN 7)		48,000	42,000
01/5/20	To Bank A/c (WN 5)	7,000		16,26,100	1/12/20	By Bank A/c (WN 8)	7000		18,01,800
15/6/20	To Bonus Shares	6,000			25/1/21	By Bank A/c (WN 10)		48,300	
25/8/20	To Bank A/c (Right Shares) (WN 6)	2,100		4,83,000	31/3/21	By Balance c/d (WN 11)	16,100		25,00,100

Scanned with OKEN Scanner

01/12/20	To P & L A/c (Sale of shares) (WN 9)			7,14,800					
31/3/21	To P & L A/c		96,300						
	Total	**23,100**	**96,300**	**43,43,900**		**Total**	**23,100**	**96,300**	**43,43,900**

Working Notes

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

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

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

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

3. Computation of Profit on Sale of Bonds on 15 Feb 2021

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

4. Valuation of Bonds as on 31 March 2021

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

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

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

Scanned with OKEN Scanner

6. Right Shares

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

7. Computation of Dividend Received on 16 Sept 2020

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

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

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

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

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

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

10. Computation of Amount of Interim Dividend

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

11. Valuation of Shares as on 31 March 2021

Cost of Shares	(15,20,000 + 16,26,100 + 4,83,000 – 42,000) / 23,100 x 16,100
	= 25,00,100
Market Value of Shares	= Rs. 260 x 16,100 = Rs. 41,86,000
Closing stock of equity shares has been value at Rs. 25,00,100 i.e., cost being lower than its market value.	

Scanned with OKEN Scanner

(ii) **Profit & Loss Account (Extract)**

For the period 01 April 2020 to 31 March 2021

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

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

Date of reclassification/transfer – 15 May 2021

Per Unit Cost of 16,100 shares held – Rs. 25,00,100/16,100 shares – Rs. 155.29 Market Price/Fair Value per share – Rs. 180

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

Note:

1. In the eight last line of the question, investment in equity shares of G Ltd. was wrongly printed as Z Ltd. in the question paper. In the above solution, it has been considered as investment in G Ltd. If considered as Investment in equity shares in Z Ltd. (some other investment and not investment in G Ltd.), then the cost of the investment for shares in Z Ltd. will not be available.
2. The entire amount of sale proceeds from rights has been credited to Profit and Loss account in the above solution. However, the sale proceeds of rights in respect of 7,000 shares (purchased cum right on 1.5.20) can be applied to reduce the carrying amount of such investments (without crediting it to profit and loss account) considering that the value of these shares has reduced after becoming their ex-right. In that case, Rs. 22,500 (67,500X 7/21) will be applied to reduce the carrying amount of investment and Rs. 45,000 will be credited to profit and loss account.

QUESTION 110

A Pvt. Ltd. follows the calendar year for accounting purposes. The company purchased 5,000 (nos.) 13.5% Convertible Debentures of Face Value of Rs. 100 each of P Ltd. on 1st May 2018 @ Rs. 105 on cum interest basis. The interest on these instruments is payable on 31st March & 30th September respectively. On August 1st 2018 the company again purchased 2,500 of such debentures @ Rs. 102.50 each on cum interest basis. On 1st October, 2018 the company sold 2,000 Debentures @ Rs. 103 each. On 31st December, 2018 the company received 10,000 equity shares of Rs. 10 each in P Ltd. on conversion of 20% of its holdings. Interest for 3 months on converted debentures was also received on 31.12.2018. The market value of the debentures and equity shares as at the close of the year were Rs. 106 and Rs. 9 respectively. Prepare the Debenture Investment Account & Equity Shares Investment Account in the books of A Pvt. Ltd. for the year 2018 on Average Cost Basis.

SOLUTION

Books of A Pvt. Ltd.

Investment in 13.5% Convertible Debentures in P Ltd. Account

(Interest payable 31st March & 30th September)

Date	Particulars	Nominal	Interest	Amount	Date	Particulars	Nominal	Interest	Amount
2018					2018				
May 1	To Bank	5,00,000	5,625	5,19,375	Sept. 30	By Bank		50,625	

Scanned with OKEN Scanner

						(6 months Int)			
Aug.1	To Bank	2,50,000	11,250	2,45,000	Oct.1	By Bank	2,00,000		2,06,000
Oct.1	To P&L A/c			2,167					
Dec. 31	To P&L A/c		52,313		Dec. 31	By Equity share	1,10,000		1,12,108
					Dec. 31	By Bank (See note)		3,713	
					Dec. 31	By Balance c/d	4,40,000	14,850	4,48,434
		7,50,000	69,188	7,66,542			7,50,000	69,188	7,66,542

Note 1: Rs. 3,713 received on 31.12.2018 represents interest on the debentures converted till date of conversion.

Note 2: Cost being lower than Market Value the debentures are carried forward at Cost.

Investment in Equity shares in P Ltd. Account

Date	Particulars	Nominal	Amount	Date	Particulars	Nominal	Amount
2018				2018			
Dec 31	To 13.5% Deb.	1,00,000	1,12,108	Dec.31	By P&L A/c		22,108
				Dec.31	By Bal. c/d	1,00,000	90,000
		1,00,000	1,12,108			1,00,000	1,12,108

Note 1: Cost being higher than Market Value the shares are carried forward at Market Value.

Working Notes:

1. Interest paid on Rs. 5,00,000 purchased on May 1st, 2018 for the month of April 2018, as part of purchase price: 5,00,000 x 13.5% x 1/12 = Rs. 5,625
2. Interest received on 30th Sept. 2018
   On Rs. 5,00,000 = 5,00,000 x 13.5% x ½ = 33,750
   On Rs. 2,50,000 = 2,50,000 x 13.5% x ½ = 16,875
   Total **Rs. 50,625**
3. Interest paid on Rs. 2,50,000 purchased on Aug. 1st 2018 for April 2018 to July 2018 as part of purchase price:
   2,50,000 x 13.5% x 4/12 = Rs. 11,250
4. Loss on Sale of Debentures
   Cost of acquisition
   (Rs. 5,19,375 + Rs. 2,45,000) x Rs. 2,00,000/Rs. 7,50,000 = 2,03,833
   Less: Sale Price (2,000 x 103) = 2,06,000
   Profit on sale **= Rs. 2,167**
5. Interest on 1,100 Debentures (being those converted) for 3 months i.e. Oct-Dec. 2018
   1,10,000 x 13.5% x 3/12 = Rs. 3,713
6. Cost of Debentures converted to Equity Shares
   (Rs. 5,19,375 + Rs. 2,45,000) x 1,10,000/7,50,000 = Rs. 1,12,108
7. Cost of Balance Debentures
   (Rs. 5,19,375 + Rs. 2,45,000) x Rs. 4,40,000/Rs. 7,50,000 = Rs. 4,48,434
8. Interest on Closing Debentures for period Oct.- Dec. 2018 carried forward (accrued interest) Rs. 4,40,000 x 13.5% x 3/12 = Rs. 14,850

Scanned with OKEN Scanner

18. AS 26 - "INTANGIBLE ASSETS"

QUESTION 111:

ABC Pvt. Ltd., recruited a player. As per the terms of the contract, the player is prohibited from playing for any other entity for the coming 5 years and has to be in employment with the company and cannot leave the entity without mutual agreement. The price the entity paid to acquire this right is derived from the skills and fame of the said player. The entity uses and develops the player through participation in matches. State whether the cost incurred to obtain the right regarding the player can be recognised as an intangible asset?

SOLUTION

As per AS 26, for an item to be recognised as an intangible asset, it must meet the definition of an intangible asset, i.e., identifiability, control over a resource and existence of future economic benefits and also recognition criteria.

With regard to establishment of control, AS 26 states that an entity controls an asset if the entity has the power to obtain the future economic benefits flowing from the underlying resource and to restrict the access of others to those benefits. The capacity of an entity to control the future economic benefits from an intangible asset would normally stem from legal rights that are enforceable in a court of law. In the absence of legal rights, it is more difficult to demonstrate control. However, legal enforceability of a right is not a necessary condition for control because an entity may be able to control the future economic benefits in some other way.

Further, AS 26 provides that an entity may have a team of skilled staff and may be able to identify incremental staff skills leading to future economic benefits from training. The entity may also expect that the staff will continue to make their skills available to the entity. However, an entity usually has insufficient control over the expected future economic benefits arising from a team of skilled staff and from training for these items to meet the definition of an intangible asset. For a similar reason, specific management or technical talent is unlikely to meet the definition of an intangible asset, unless it is protected by legal rights to use it and to obtain the future economic benefits expected from it, and it also meets the other parts of the definition.

Since the right in the instant case is contractual, identifiability criterion is satisfied. Based on the facts provided in the given case, the player is prohibited from playing in other teams by the terms of the contract which legally binds the player to stay with ABC Ltd for 5 years.

Accordingly, in the given case, the company would be able to demonstrate control. Future economic benefits are expected to arise from use of the player in matches. Further, the cost of obtaining rights is also reliably measurable. Hence, it can recognise the costs incurred to obtain the right regarding the player as an intangible asset. However, careful assessment of relevant facts and circumstances of each case is required to be made.

QUESTION 112

During 20X1-X2, an enterprise incurred costs to develop and produce a routine low risk computer software product, as follows:

Particular	Rs.
Completion of detailed program and design (Phase 1)	50,000
Coding and Testing (Phase 2)	40,000
Other coding costs (Phase 3&4)	63,000
Testing costs (Phase 3&4)	18,000
Product masters for training materials (Phase 5)	19,500
Packing the products (1,500 units) (Phase 6)	16,500

After completion of phase 2, it was established that the product is technically feasible for the market.

You are required to state how the above referred cost to be recognized in the books of accounts.

Scanned with OKEN Scanner

SOLUTION:

As per AS 26, costs incurred in creating a computer software product should be charged to research and development expense when incurred until technological feasibility / asset recognition criteria has been established for the product. Technological feasibility / asset recognition criteria have been established upon completion of detailed program design, coding and testing. In this case, Rs. 90,000 would be recorded as an expense (Rs. 50,000 for completion of detailed program design and Rs. 40,000 for coding and testing to establish technological feasibility/asset recognition criteria). Cost incurred from the point of technological feasibility/asset recognition criteria until the time when products costs are incurred are capitalized as software cost (63,000+18,000+19,500)=Rs.1,00,500. Packing cost Rs.16,500 should be recognized as expenses and charged to P&LA/c.

QUESTION 113

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

SOLUTION:

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

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

QUESTION 114

Vishnu Ltd. is engaged in research on a new process design for its product- It had incurred an expenditure of Rs. 265.37 lakhs on research upto 31st March, 2003. The development of the process began on 1st April, 2003 and the Development Phase Expenditure was Rs. 180 lakhs upto 31st March, 2004. From 1st April, 2004 the Company will implement the new process design which will result in a after-tax cost saving of Rs. 40 lakhs per annum for the next five years. The Company's Cost of Capital is 10%. At what cost should the asset be recorded and what is its amortisation amount?

SOLUTION

Research Expenditure: As per Para 41 of AS-26, the expenditure on research Rs. 265.37 lakhs should be expensed in the year in which it is incurred. It is presumed that the entire expenditure of Rs. 265.37 lakhs is incurred in financial year 2002-2003. Hence, it should be written off as an expense in that year itself.

Development Expenditure: As per para 44 of AS-26, the expenditure on development can be treated as an asset only if all the conditions listed in that paragraph are satisfied. It is presumed that the company has duly complied with this requirement.

Cost of internally generated intangible asset: Para 53 specifies the items which can be included in the cost of an internally generated intangible asset, while Para 54 specifies the exclusions there from. It is presumed that the expenditure of Rs.180 lakhs is determined in accordance with Para 53 and 54 of AS-26.

Discounting Future Cash Flows: As per Para 30 of AS-26, fair value of an intangible asset can be estimated by discounting estimated future net cash flows. Even if this paragraph is primarily related to estimation of fair value of an intangible asset acquired in the course of amalgamation in the nature of purchase, the concept can be extended for internally generated intangible asset also.

Cost savings from the new process design for five = Rs. 40 lakhs per year

Company's Cost of Capital = 10%

Scanned with OKEN Scanner

Annuity Factor at 10% for five years (from the annuity tables) = 3.7908

Present value of future cash flows = Rs. 40 x 3.7908= Rs. 151.63 lakhs

Carrying Amount of the Asset: Since the Present Value of Future Cash Flows is only Rs. 151.63 lakhs, (which is lower than the cost of Rs.180 lakhs), it is prudent to recognise an impairment loss of Rs. 180.00 lakhs - Rs. 151.63 lakhs = Rs. 28.37 lakhs in the financial year 2003-2004.

Amortisation Period and Amount: The Company can amortise Rs. 151.63 lakhs over a five-year period by charging Rs. 30.33 lakhs per annum from the financial year 2004-2005 onwards.

Scanned with OKEN Scanner

19. AS 28 – IMPAIRMENT OF ASSETS

QUESTION 115

Cost 1/4/2001 Rs. 10,00,000, Depreciation SLM life 10 years. On 31/3/2005, Recoverable Amount is. 3,00,000. On 311/3/2007, Recoverable Amount is 2,20,000. Calculate Impairment Loss and its Reversal.

QUESTION 116

Ergo Industries Ltd. gives the following estimates of cash flows relating to Property, Plant and Equipment on 31-12-20X1. The discount rate is 15%

Year	Cash Flow (₹ in lakhs)
20×2	4000
20×3	6000
20×4	6000
20×5	8000
20×6	4000

Residual value at the end of 20X6	= ₹ 1000 lakhs
Property, Plant and Equipment purchased on 1-1-20XX	= ₹ 40,000 lakh
Useful life	= 8 years
Net selling price on 31-12-20X1	= ₹20,000 lakhs

Calculate on 31-12-20X1:

a. Carrying amount at the end of 20X1

b. Value in use on 31-12-20X1

c. Recoverable amount on 31-12-20X1

d. Impairment loss to be recognized for the year ended 31-12-20X1

e. Revised carrying amount.

f. Depreciation charge for 20X2.

Note: The year 20XX is the immediate preceding year before the year 20X0.

Solution:

Calculation of Value in Use

Year	Cash flow	Discount as per 15%	Discounted cash flow
20×2	4,000	0.870	3,480
20×3	6,000	0.756	4,536
20×4	6,000	0.658	3,948
20×5	8,000	0.572	4,576
20×6	4,000	0.497	1,988
20×6	1,000 (Residual)	0.497	497
			19,025

a. Calculation of carrying amount:

i. Original cost = ₹ 40,000 lakhs

ii. Depreciation for 3 years = [(40,000-1000)×3/8] = ₹ 14,625 lakhs

iii. Carrying amount on 31-12-20X1 = [40,000-14,625] = ₹ 25,375 lakhs

a. Value in use = ₹ 19,025 lakhs

b. Recoverable amount = higher of value in use and net selling price i.e. ₹ 20,000 lakhs

c. Impairment Loss = ₹ (25,375-20,000) = ₹ 5,375 lakhs

Scanned with OKEN Scanner

d. Revised carrying amount = ₹ (25,375-5,375) = ₹ 20,000 lakhs

e. Depreciation charge for 20X2 = (20,000-1000)/5 = ₹ 3,800 lakhs

QUESTION 117

G Ltd., acquired a machine on 1st April, 20X0 for ₹ 7 crore that had an estimated useful life of 7 years. The machine is depreciated on straight line basis and does not carry any residual value. On 1st April, 20X4, the carrying value of the machine was reassessed at ₹ 5.10 crore and the surplus arising out of the revaluation being credited to revaluation reserve. For the year ended March, 20X6, conditions indicating an impairment of the machine existed and the amount recoverable ascertained to be only ₹ 79 lakhs. You are required to calculate the loss on impairment of the machine and show how this loss is to be treated in the books of G Ltd. G Ltd., had followed the policy of writing down the revaluation surplus by the increased charge of depreciation resulting from the revaluation.

Solution

Statement Showing Impairment Loss

	(₹ in crores)
Carrying amount of the machine as on 1st April, 20X0	7.00
Depreciation for 4 years i.e. 20X0-20X1 to 20X3-20X4 (7 crores / 7 years x 4 years)	(4.00)
Carrying amount as on 31.03.20X4	**3.00**
Add: Upward Revaluation (credited to Revaluation Reserve account)	2.10
Carrying amount of the machine as on 1st April, 20X4 (revalued)	**5.10**
Less: Depreciation for 2 years i.e. 20X4-20X5 & 20X5-20X6 (5.10/3 years x 2 years)	(3.40)
Carrying Amount as on 31.03.20x6	1.70
Less: Recoverable Amount	(0.79)
Impairment Loss	**0.91**
Less: Balance in revaluation reserve as on 31.03.20X6:	2.10
Balance in revaluation reserve as on 31.03.20X4:	1.40
Less: Enhanced Depreciation met from revaluation reserve	0.70
20X4-X5 AND 20X5-X6 = [(1.70 – 1.00) X 2 YEARS]	
	0.71
Impairment Loss set off against revaluation reserve balance	**0.21**
Impairment Loss to be debited to Profit and Loss Account	

QUESTION 118

A Ltd. gives following information

Asset	Carrying Amount	Cash generating unit
A	1,00,000	1
B	2,00,000	3
C	3,00,000	2
D	3,50,000	2
E	70,000	1
F	8,00,000	3
G	2,20,000	2
H	4,50,000	1
Goodwill X	90,000	Allocate in ratio 1:1:1
Goodwill Y	60,000	Unallocable
Corporate:		
Asset P	1,50,000	Allocate in ratio 3:2:1
Asset Q	2,00,000	Unallocable

Recoverable Amount of Cash generating Unit: 1 – 6,70,000; 2 – 8,40,000 and 3 – 10,30,000 Recoverable Amount of Entity: Case A – 25,50,000; Case B – 25,40,000. Calculate impairment loss.

Scanned with OKEN Scanner

QUESTION 119

Himalaya Ltd. which is in the business of manufacturing and exporting its product. Sometimes, back at the end of 20X4, the Government put restrictions on export of goods exported by Himalaya Ltd. and due to that restriction Himalaya Ltd. impaired its assets. Himalaya Ltd. acquired identifiable assets worth Rs 5,500 lakhs for Rs 6,000 lakh at the end of the year 20X0. The difference is treated as goodwill. The useful life of identifiable assets is 15 years and depreciated on a straight-line basis. When the Government put the restriction at the end of 20X4, the company recognised the impairment loss by determining the recoverable amount of assets for Rs 3,120 lakh. In 20X6 Government lifted the restriction imposed on the export and due to this favourable change, Himalaya Ltd. re-estimate recoverable amount, which was estimated at Rs 3,420 lakh.

Required:

I. Calculation and allocation of impairment loss in 20X4.

II. Reversal of impairment loss and its allocation as per AS 28 in 20X6.

Solution

(Assuming goodwill is amortised over 5 years as per AS 14)

i.Calculation and allocation of impairment loss in 20X4

(Amount in Rs.lakhs)

	Goodwill	Identifiable assets	Total
Historical cost	500	5,500	6,000
Accumulated depreciation/amortization (4 yrs.)	400	(1,467)	(1,467)
Carrying amount before impairment	100	4,033	4,133
Impairment loss*	(100)	(913)	(1013)
Carrying amount after impairment loss	**0**	**3,120**	**3,120**

***Notes:**

1. As per AS 28, an impairment loss should be allocated to reduce the carrying amount of the assets of the unit in the following order:
   - first, to goodwill allocated to the cash-generating unit (if any); and
   - then, to the other assets of the unit on a pro-rata basis based on the carrying amount of each asset in the unit.

Hence, first goodwill is impaired at full value and then identifiable assets are impaired to arrive at recoverable value.

(ii) Carrying amount of the assets at the end of 20X6 (Amount in Rs. lakhs)

End of 20X6	Goodwill	Identifiable assets	Total
Carrying amount in 20X6	0	2,553	2,553
Add: Reversal of impairment loss (W.N.2)	-	747	747
Carrying amount after reversal of impairment loss	-	**3,300**	**3,300**

Working Note:

1. **Calculation of depreciation after impairment till 20X6 and reversal of impairment loss in 20X6**

			(Amount in Rs lakhs)
	Goodwill	Identifiable assets	Total
A. Carrying amount after impairment loss in 20X4	0	3,120	3,120
B. Additional depreciation (i.e. (3,120/11) x 2)refer Note	–	(567)	(567)
C. Carrying amount	0	2,553	2,553
D. Recoverable amount			3,420
E. Excess of recoverable amount over carrying amount (D-C)			**867**

Note: It is assumed that the restriction by the Government has been lifted at the end of the year 20X6. Therefore, depreciation for 2 years is calculated (2005, 2006).

1. **Determination of the amount to be impaired by calculating depreciated historical cost of the identifiable assets without impairment at the end of 20X6**

Scanned with OKEN Scanner

(Amount in Rs lakhs)

End of 20X6	Identifiable assets
Historical cost	5,500
Accumulated depreciation	(366.67 x 6 years) = (2,200)
Depreciated historical cost	3,300
Carrying amount (in W.N. 1)	**2,553**
Amount of reversal of impairment loss	**747**

Notes:

As per AS 28, in allocating a reversal of an impairment loss for a cash-generating unit, the carrying amount of an asset should not be increased above the lower of:

a. its recoverable amount (if determinable); and

a. the carrying amount that would have been determined (net of amortization or depreciation) had no impairment loss been recognised for the asset in prior accounting periods.

Hence impairment loss reversal is restricted to Rs 747 lakhs only.

Note:

Impairment Loss on Goodwill shall not be reversed except certain conditions.

Scanned with OKEN Scanner

20. AS - 22 "ACCOUNTING FOR TAXES ON INCOME"

QUESTION 120

From the following information given below you are required to compute Deferred Tax Assets and Deferred Tax Liability for Ramanujam Ltd. as on 31st March, 20X1. The tax applicable is 35%.

1. The company has charged Rs. 7,42,900 in the books of accounts while as per Income Tax Computation, the depreciation available for the company is Rs. 8,65,400.
2. The Company has made provision for doubtful debts for Rs. 54,300 during the year.
3. The company has debited share issue expenses of Rs. 6,23,500 which will be available for deduction under the income tax Act from the next year.
4. The expenses of Rs. 7,84,500 has been charged to profit and loss account which are disallowed under the income tax act.
5. The company has made donation of Rs. 2,00,000 which has been debited to Profit and loss account and only 50% thereof will be allowed as deduction as per Income Tax law.

SOLUTION:

Timing Difference Amount	DTA/DTL	Remarks
122500 Liability	42875 DTL	-
54300 Assets	19005 DTA	
623500 Assets	218225 DTA	
-	-	Permanent Difference
-	-	Permanent Difference of Rs. 100000
	194355	**Net DTA**

QUESTION 121

The following particulars are stated in the Balance Sheet of Deep Limited as on 31st March, 2020:

	(Rs. In Lakhs)
Deferred Tax Liability (Cr.)	28.00
Deferred Tax Assets (Dr.)	14.00

The following transactions were reported during the year 2020 -2021:

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

ii. Expenses disallowed in 2019-20 and allowed for tax purposes in 2020-21 were Rs. 14 Lakhs.

iii. Share issue expenses allowed under section 35(D) of the Income Tax Act, 1961 for the year 2020-21 (1/10th of Rs. 70.00 lakhs incurred in 2019-20).

iv. Repairs to Plant and Machinery were made during the year for Rs. 140.00 Lakhs and was spread over the period 2020-21 and 2021-22 equally in the books. However, the entire expenditure was allowed for income-tax purposes in the year 2020-21.

Tax Rate to be taken at 40%.

You are required to show the impact of above items on Deferred Tax Assets and Deferred Tax Liability as on 31st March, 2021.

SOLUTION

Impact of various items in terms of deferred tax liability/deferred tax asset on 31.3.21

Transactions	**Analysis**	**Nature of difference**	**Effect**	**Amount (Rs.)**
Difference in depreciation	Generally, written down value method of depreciation is adopted under IT Act which leads to higher depreciation in earlier years	Responding timing difference	Reversal of DTL	28 lakhs × 40% = Rs. 11.20 lakhs

Scanned with OKEN Scanner

	of useful life of the asset in comparison to later years.			
Disallowances, as per IT Act, of earlier years	Tax payable for the earlier year was higher on this account.	Responding timing difference	Reversal of DTA	14 lakhs × 40% = 5.6 lakhs
Share issue expenses	Due to disallowance of full expenditure under IT Act, tax payable in the earlier years was higher.	Responding timing difference	Reversal of DTA	7 lakhs × 40% = Rs. 2.8 lakhs
Repairs to plant and machinery	Due to allowance of full expenditure under IT Act, tax payable of the current year will be less.	Originating timing difference	Increase in DTL	70 lakhs × 40% = 28 lakhs

QUESTION 122:

Rama Ltd. started business on 1st April 1998. The following details are available from the books of accounts and other records of Rama Ltd.

Profit before depreciation and taxes

1998-1999	14,45,500
1999-2000	18,20,200
2000-2001	24,56,560
2001-2002	30,22,280

The company purchased the following machines

Date of Purchase	Amount (Rs.)
1.4.1998	3,45,000
1.41999	2,75,000
1.4.2000	10,00,000
1.4.2001	3,62,000

The Company charges depreciation on machines @ 15% p.a. whereas the rates as per tax is 25% p.a. Tax rates for five years is 50%, 45%, 40% 35% and 35 % respectively.

You are required to prepare the profit and loss statement showing the provision for taxes under the AS-22.

Solution

Working Note 1: Fixed Assets Schedule (in the Books)

	1998	1999	2000	2001
Opening Asset	Nil	2,93,250	4,83,013	12,60,561
Purchases 1/4	3,45,000	2,75,000	10,00,000	3,62,000
Gross Total	3,45,000	5,68,250	14,83,013	16,22,561
Depreciation @15%	(51,750)	(85,238)	(2,22,452)	(2,43,384)
Closing 31/3	2,93,250	4,83,013	12,60,561	13,79,177

Working Note 2: Fixed Assets Schedule (As per IT)

	1998	1999	2000	2001
Opening Asset	Nil	2,58,750	4,00,312	10,50,234
Purchases 1/4	3,45,000	2,75,000	10,00,000	3,62,000
Gross Total	3,45,000	5,33,750	14,00,312	14,12,234
Depreciation @25%	(86,250)	(1,33,438)	(3,50,078)	(3,53,059)
Closing 31/3	2,58,750	4,00,312	10,50,234	10,26,175

Scanned with OKEN Scanner

Working Note 3: Calculation of A/c Income, Taxable Income & Tax thereon: -

	1998	1999	2000	2001
PBD&T	14,45,500	18,20,200	24,56,560	30,22,280
(-) Dep (Books) WN.1	(51,750)	(85,238)	(2,22,452)	(2,43,384)
A/c Income PBT	13,93,750	17,34,962	22,34,108	27,78,896
(+) Depreciation Disallowed	51,750	85,238	2,22,452	2,43,384
(-) Dep Allowed as per IT	(86,250)	(1,33,438)	(3,50,078)	(3,53,059)
Taxable Income	13,59,250	16,86,762	21,06,482	26,69,221
CT Rates	50%	45%	40%	35%
CT Expenses	6,79,625	7,59,043	8,42,593	9,34,227
Timing Difference	3,45,000	4,82,000	1,27,626	1,09,675
Cumulative Timing Difference	3,45,000	8,27,000	2,10,326	3,20,001
Tax Rate	45%	40%	35%	35%
DT Liability (B/S)	15,525	33,080	73,614	1,12,000
DT Liability (P&L)	15,525	17,555	40,534	38,386

Statement of P&L

	1998	1999	2000	2001
Profit Before Tax	13,93,750	17,34,962	22,34,108	27,78,896
(-) Tax Expense				
CT	6,79,625	7,59,043	8,42,593	9,34,227
+ DTL	15,525	17,555	40,534	38,386
Profit After Tax	6,98,600	9,58,364	13,50,981	18,06,283

QUESTION 123

ABC Company limited had an investment in Venture Capital amounting ₹10Crores. Venture capital in turn had invested in the below portfolio companies (New Start-ups) on behalf of ABC Limited:

Portfolio Companies	Amount of investment (₹ in Crores)
Oscar Limited	2
Zee Limited	3
Star Limited	4
Sony Limited	1
Total	**10**

During the FY 2019-2020, Venture Capital had sold their investment in Star Limited and realised an amount of ₹8 Crores on sale of shares of star Limited and entire proceeds of ₹8 Crores have been transferred by Venture Capital to ABC Company Limited.

The accounts manager has received the following additional information from venture capital on 31.03.2020:

1. 8 Crores has been deducted from the cost of investment and carrying amount of investment as at year end is 2 Crores.
2. Company had to pay a capital gain tax @20% on the net sale consideration of ₹ 4 Crores.
3. Due to COVID-19, the remaining start-ups (i.e. Oscar Limited, Zee Limited, and Sony Limited) are not performing well and will soon wind up their operations. Venture capital is monitoring the situation and if required they will provide an impairment loss in June 2020 Quarter.

You need to suggest the accounts manager what should be the correct accounting treatment as per AS 22 "Accounting for Taxes on Income".

SOLUTION

As company had to pay capital gain tax @20% on the net sale consideration as per income tax laws, the company has to recognise a current tax liability of 0.8 Crores computed as under:

Scanned with OKEN Scanner

Particulars	Amount (₹ in Crores)
Sales Consideration	8
Cost of Investment	4
Net gain on Sale	4
Tax@20%	**0.8**

As per AS 22, Timing differences are those differences between taxable income and accounting income for a period that originate in one period and are capable of reversal in one or more subsequent periods.

Particulars	Amount(₹ in Crores)	Rationale
Taxable Income	4	As per income tax laws
Accounting Income	Nil	As the same is deducted from the cost of investment
Timing Difference	4	

As per AS 22, deferred tax assets should be recognised and carried forward only to the extent that there is a reasonable certainty that sufficient future taxable income will be available against which such deferred tax assets can be realised. Since in current scenario, due to Covid 19 the portfolio companies are not performing well, thus the company may not have sufficient future taxable income which will reverse deferred tax assets. Therefore, the company should not recognise DTA of ₹ 0.8 Crores and company should recognise only current tax liability of ₹ 0.8 Crores.

Scanned with OKEN Scanner

21. FRAMEWORK

QUESTION 124:

Balance sheet of a trader on 31st March, 20X1 is given below:

Particulars	Rs
Assets	
Non-current assets	
Property, Plant and Equipment	65,000
Current assets	
Inventories	30,000
Financial assets	
Trade receivables	20,000
Other Assets	10,000
Bank Balance	5,000
Total	**1,30,000**
Equity and Liabilities	
Equity	
Share capital	60,000
Other Equity - Profit and Loss Account	25,000
Non-current liabilities	
10% Loan	35,000
Current liabilities	
Financial liabilities	
Trade payables	10,000
Total	**1,30,000**

Additional information:

(a) The remaining life of Property, Plant and Equipment is 5 years. The pattern of use of the asset is even. The net realisable value of Property, Plant and Equipment on 31.03.20X2 was Rs. 60,000.

(b) The trader's purchases and sales in 20X1-20X2 amounted to Rs. 4 lakh and Rs. 4.5 lakh respectively.

(c) The cost and net realisable value of inventories on 31.03.20X2 were Rs. 32,000 and Rs. 40,000 respectively.

(d) Employee benefit expenses for the year amounted to Rs. 14,900 (including interest of Rs. 3,500 on 10% Loan for the year).

(e) Other Assets is written off equally over 4 years.

(f) Trade receivables on 31.03.20X2 is Rs. 25,000, of which Rs. 2,000 is doubtful. Collection of another Rs. 4,000 depends on successful re-installation of certain product supplied to the customer.

(g) Closing Trade Payable is Rs. 12,000 which is likely to be settled at 5% discount.

(h) Bank balance on 31.03.20X2 is Rs. 37,100.

(i) There is an early repayment penalty for the loan Rs. 2,500.

The Profit and Loss Accounts and Balance Sheets of the trader are shown below in two cases

(j) Assuming going concern (ii) not assuming going concern.

SOLUTION:

Profit and Loss Account for the year ended 31st March, 20X2

	Case (i) Rs	Case (ii) Rs
Revenue from operations – Sales	4,50,000	4,50,000
Other Incomes	-	600
TOTAL INCOMES (A)	**4,50,000**	**4,50,600**
Expenses :		
Purchases	4,00,000	4,00,000

Scanned with OKEN Scanner

Changes in inventories	(2,000)	(10,000)
Employee benefit expenses	11,400	11,400
Finance cost (including penalty)	3,500	6,000
Depreciation and amortisation expenses (including w/off)	15,500	15,000
Other expenses - Provision for doubtful debts	2,000	6,000
Total Expenses (B)	**4,30,400**	**4,28,400**
Profit for the period (A-B)	19,600	22,200
Opening Reserves & Surplus	25,000	25,000
Closing Reserves and Suplus	**44,600**	**47,200**

Balance Sheet as at 31st March, 20X2

	Case (i) Rs	Case (ii) Rs
ASSETS		
Non-current assets		
Property, Plant and Equipment	52,000	60,000
Current Asset		
Inventories	32,000	40,000
Financial assets		
Trade receivables (less provision)	23,000	19,000
Other Assets	7,500	Nil
Cash and cash equivalents (after interest paid on loan)	37,100	37,100
Total	**1,56,100**	**1,56,100**
EQUITY AND LIABILITIES		
Shareholders Fund		
Share Capital	60,000	60,000
Reserves and Surplus	44,600	47,200
Non-current liabilities		
10% Loan	35,000	37,500
Current liabilities		
Trade payables	12,000	11,400
Total	**1,56,100**	**1,56,100**

QUESTION 125: –

Historical Cost Capital Maintenance

A trader commenced business on 01/01/20X1 with Rs. 12,000 represented by 6,000 units of a certain product at Rs. 2 per unit. During the year 20X1 he sold these units at Rs. 3 per unit and had withdrawn Rs. 6,000. Thus:

Opening Equity = Rs. 12,000 represented by 6,000 units at Rs. 2 per unit.

Closing Equity = Rs. 12,000 (Rs. 18,000 – Rs. 6,000) represented entirely by cash.

Retained Profit = Rs. 12,000 – Rs. 12,000 = Nil

The trader can start year 20X3 by purchasing 6,000 units at Rs. 2 per unit once again for selling them at Rs. 3 per unit. The whole process can repeat endlessly if there is no change in purchase price of the product.

QUESTION 126: –

Financial Capital Maintenance

In the previous **example 8,** suppose that the average price indices at the beginning and at the end of year are 100 and 120 respectively.

Opening Equity = Rs. 12,000 represented by 6,000 units at Rs. 2 per unit.

Opening equity at closing price = (Rs. 12,000 / 100) x 120 = Rs. 14,400 (6,000 x Rs. 2.40)

Closing Equity at closing price = Rs. 12,000 (Rs. 18,000 – Rs. 6,000) represented entirely by cash.

Retained Profit = Rs. 12,000 – Rs. 14,400 = (-) Rs. 2,400

Scanned with OKEN Scanner

The negative retained profit indicates that the trader has failed to maintain his capital. The available fund Rs. 12,000 is not sufficient to buy 6,000 units again at increased price Rs. 2.40 per unit. In fact, he should have restricted his drawings to Rs. 3,600 (Rs. 6,000 – Rs. 2,400).

Had the trader withdrawn Rs. 3,600 instead of Rs. 6,000, he would have left with Rs. 14,400, the fund required to buy 6,000 units at Rs. 2.40 per unit.

QUESTION 127: –

Physical Capital Maintenance

In the previous **example 8,** suppose that the price of the product at the end of year is 2.50 per unit. In other words, the specific price index applicable to the product is 125.

Current cost of opening stock = (Rs. 12,000 / 100) x 125 = 6,000 x Rs. 2.50 = Rs. 15,000

Current cost of closing cash = Rs. 12,000 (Rs. 18,000 – Rs. 6,000)

Opening equity at closing current costs = Rs. 15,000

Closing equity at closing current costs = Rs. 12,000

Retained Profit = Rs. 12,000 – Rs. 15,000 = (Rs. 3,000)

The negative retained profit indicates that the trader has failed to maintain his capital. The available fund Rs. 12,000 is not sufficient to buy 6,000 units again at increased price Rs. 2.50 per unit. The drawings should have been restricted to Rs. 3,000 (Rs. 6,000 – Rs. 3,000).

Had the trader withdrawn Rs. 3,000 instead of Rs. 6,000, he would have left with Rs. 15,000, the fund required to buy 6,000 units at Rs. 2.50 per unit.

Capital maintenance can be computed under all three bases as shown below:

Financial Capital Maintenance at historical costs

	Rs	Rs
Closing capital (At historical cost)		12,000
Less: Capital to be maintained		
Opening capital (At historical cost)	12,000	
Introduction (At historical cost)	Nil	(12,000)
Retained profit		Nil

Financial Capital Maintenance at current purchasing power

	Rs	Rs
Closing capital (At closing price)		12,000
Less: Capital to be maintained		
Opening capital (At closing price)	14,400	
Introduction (At closing price)	Nil	(14,400)
Retained profit		(2,400)

Physical Capital Maintenance

	Rs	Rs
Closing capital (At current cost)		12,000
Less: Capital to be maintained		
Opening capital (At current cost)	15,000	
Introduction (At current cost)	Nil	(15,000)
Retained profit		(3,000)

Scanned with OKEN Scanner

22. AS 1 – DISCLOURE OF ACCOUNTING POLICIES

QUESTION 128:

Jagannath Ltd. had made a rights issue of shares in 2012. In the offer document to its members, it had projected a surplus of ₹40 crores during the accounting year to end on 31st March, 2014. The draft results for the year, prepared on the hitherto followed accounting policies and presented for perusal of the board of directors showed a deficit of ₹10 crores. The board in consultation with the managing director, decided on the following:

(i) Value year-end inventory at works cost (₹50 crores) instead of the hitherto method of valuation of inventory at prime cost (₹30 crores).

(ii) Provide depreciation for the year on straight line basis on account of substantial additions in gross block during the year, instead of on the reducing balance method, which was hitherto adopted. As a consequence, the charge for depreciation at ₹27 crores is lower than the amount of ₹45 crores which would have been provided had the old method been followed, by ₹18 cores.

(iii) Not to provide for "after sales expenses" during the warranty period. Till the last year, provision at 2% of sales used to be made under the concept of "matching of costs against revenue" and actual expenses used to be charged against the provision. The board now decided to account for expenses as and when actually incurred. Sales during the year total to ₹600 crores.

(iv) Provide for permanent fall in the value of investments - which fall had taken place over the past five years - the provision being ₹10 crores.

As chief accountant of the company, you are asked by the managing director to draft the notes on accounts for inclusion in the annual report for 2013-2014.

Answer

As per AS 1, any change in the accounting policies which has a material effect in the current period or which is reasonably expected to have a material effect in later periods should be disclosed. In the case of a change in accounting policies which has a material effect in the current period, the amount by which any item in the financial statements is affected by such change should also be disclosed to the extent ascertainable. Where such amount is not ascertainable, wholly or in part, the fact should be indicated. Accordingly, the notes on accounts should properly disclose the change and its effect.

Notes on Accounts:

(i) During the year inventory has been valued at factory cost, against the practice of valuing it at prime cost as was the practice till last year. This has been done to take cognizance of the more capital-intensive method of production on account of heavy capital expenditure during the year. As a result of this change, the year-end inventory has been valued at ₹50 crores and the profit for the year is increased by ₹20 crores.

(ii) In view of the heavy capital-intensive method of production introduced during the year, the company has decided to change the method of providing depreciation from reducing balance method to straight line method. As a result of this change, depreciation has been provided at ₹27 crores which is lower than the charge which would have been made had the old method and the old rates been applied, by ₹18 crores. To that extent, the profit for the year is increased.

(iii) So far, the company has been providing 2% of sales for meeting "after sales expenses during the warranty period. With the improved method of production, the probability of defects occurring in the products has reduced considerably. Hence, the company has decided not to make provision for such expenses but to account for the same as and when expenses are incurred. Due to this change, the profit for the year is increased by ₹12 crores than would have been the case if the old policy were to continue.

The company has decided to provide ₹10 crores for the permanent fall in the value of investments which has taken place over the period of past five years. The provision so made has reduced the profit disclosed in the accounts by ₹10 crores.

Scanned with OKEN Scanner

QUESTION 129

You are required to comment on the following cases as per the provisions of Accounting Standard-1 'Disclosure of Accounting Policies':

(1) Bee Limited has not complied with AS-2 "Valuation of inventories" and the same is disclosed in the Notes on Accounts. Management is of the view that the financial statements give a true and fair view as non-compliance with AS-2 is disclosed.

(2) Cee Limited sold its Office Building for ` 10,00,000 on 1st March, 2023. The buyer has paid the full amount and taken possession of the building. The book value of the Office Building is ` 4,00,000. On 31st 2023, documentation and legal formalities are pending. The company has not recorded the disposal and the amount received is shown as an advance.

(3) Dee Limited has prepared its accounts on cash basis and the same is not disclosed.

(4) Jee Limited disclosed significant accounting policies adopted in the preparation of financial statements, in the Directors' Report.

Solution

(1) As per AS-I disclosure of accounting policies is not a remedy for wrong or inappropriate treatment in accounting. In the given case the financial statement does not give a true and fair view as they are not in compliance with AS-2.

(2) Considering the substance over form as per AS-I, documentation and legal formalities represent the form of the transaction, although the legal title has not been transferred, the economic reality and substance are that the rights and beneficial interest in the Office Building have been transferred. Therefore, recording of acquisition/ disposal (by the transferee and transferor respectively) would in substance represent the transaction entered into.

(3) Accrual is a fundamental accounting assumption. If it is not followed by the company, the facts should be disclosed under AS-I. Hence the company should disclose the fact that the cash basis of accounting has been followed in the notes on accounts.

(4) The practice followed by the company is not correct. It should be disclosed as part of financial statements (The director's report is not part of financial statements).

QUESTION 130

(i) ABC Ltd. up to 31.03.2020. Now, the company wants to make provision based on technical evaluation during the year ending 31.03.2021.

Total value of stock Rs. 133.75 lakhs

Provision required based on technical evaluation Rs. 4.00 lakhs

Provision required based on 12 months not issued Rs. 5.00 lakhs

(ii) In the books of M/s Kay Ltd, the closing stock as on 31st march, 2021 amounts to Rs. 1,24,000 (on the basis of FIFO method)

The company decides to change from FIFO method to weighted average method for ascertaining the cost of inventory from the year 2020-2021. On the basis of weighted average method, closing stock as on 31st march, 2021 amounts to Rs. 1,15,000. Realisable value of the inventory as on 31st march, 2021 amounts to Rs. 1,54,000.

Discuss disclosure requirements of change in accounting policy in above cases as per AS-1.

SOLUTION

(i) The decision of making provision for non-moving inventories on the basis of technical evaluation does not amount to change in accounting policy. Accounting policy of a company may require that provision for non-moving inventories should be made. The method of estimating the amount of provision may be changed in case a more prudent estimate can be made.

In the given case, considering the total value of inventory, the change in the amount of required provision of non-moving inventory from Rs. 5 lakhs to Rs. 4 lakhs are also not material. The disclosure can be made for such change in the following lines by way of notes to the accounts in the annual accounts of ABC Ltd. for the year 2020 -21:

"The company has provided for non-moving inventories on the basis of technical evaluation unlike preceding years. Had the same method been followed as in the previous year, the profit for the year and the corresponding effect on the year end net assets would have been lower by Rs. 1 lakh."

(ii) As per AS 1 "Disclosure of Accounting Policies", any change in an accounting policy which has a material effect

Scanned with OKEN Scanner

should be disclosed in the financial statements. The amount by which any item in the financial statements is affected by such change should also be disclosed to the extent ascertainable. Where such amount is not ascertainable, wholly or in part, the fact should be indicated. Thus, company should disclose the change in valuation method of inventory and its effect on financial statements. The company may disclose the change in accounting policy in the following manner:

"The company values its inventory at lower of cost and net realizable value. Since net realizable value of all items of inventory in the current year was greater than respective costs, the company valued its inventory at cost. In the present year i.e., 2020-21, the company has changed to weighted average method, which better reflects the consumption pattern of inventory, for ascertaining inventory costs from the earlier practice of using FIFO for the purpose. The change in policy has reduced current profit and value of inventory by Rs. 9,000."

Scanned with OKEN Scanner

23. AS – 7 "CONSTRUCTION CONTRACTS"

QUESTION 131

Contractual Term = 3 Years

Contract Revenue = 3000 Cr.

	1	2	3
Contract Cost incurred till date	800	1900	3200
Further Estimated cost to be incurred	1750	1300	-

Calculate Contract Profit/Loss every year.

SOLUTION:

	1	2	3
	800/2,550 x 100 = 31.37%	1,900/2,550 x 100 = 59.38%	100%
Cumulative Revenue	941	1,781	3,000
Current Year Revenue	941	840	1,219
Current Year Cost	800	1,100	1,219**
Current Year Profit/Loss	141	(260)	0
Loss till date Recognised	-	260-141 = 119	
Loss to be Recognised	-	200-119 = 81*	

* As per AS 7 (Contract Cost) when total Construction Cost is expected to be in excess of Contract Revenue then Loss should be provided for immediately.

**Cost to be recognised = 3,200 – 1,900	1,300
Cost to be Recognised	**1,219**

QUESTION 132:

X Ltd. Commenced a construction contract on 01/04/X1. The fixed contract price agreed was Rs. 2,00,000. The company incurred Rs. 81,000 in 20X1-X2 for 45% work and received Rs. 79,000 as progress payment from the customer. The cost incurred in 20X2-X3 was Rs. 89,000 to complete the rest of work. Show the Extract of the Profit and Loss A/c and Customer's A/c for the related years.

SOLUTION:

Profit & Loss Account

Year		Rs.000	Year		Rs.000
20X1-X2	To Construction Costs (for 45% work)	81	20X1-X2	By Contract Price (45% of Contract Price)	90
	To Net profit (for 45% work)	9			
		90			**90**
20X2-X3			20X2-X3		
	To Construction Costs (for 55% work)	89		By Contract Price (55% of Contract Price)	110
	To Net Profit (for 55% work)	21			
		110			**110**

Scanned with OKEN Scanner

Customer account

Year		Rs.000	Year		Rs.000
20X1-X2	To Contract Price	90	20X1-X2	By Bank	79
				By Balance c/d	11
		90			**90**
20X2-X3			20X2-X3		
	To Balance b/d	11		By Bank	121
	To Contract Price	110			
		121			**121**

QUESTION 133

AB contactors enters into a contract on 1st January 20X1 with XY to construct a 5-storied building. Under the contract, AB is required to complete the construction in 3 years (i.e., by 31st December 20X3). The following information is relevant:

Fixed price (agreed) ₹5crore

Material cost escalation (to the extent of 20% of increase in material cost) Labour cost escalation (up to 30% of increase in minimum wages)

In case AB is able to complete the construction in less than 2 years and 10 months, it will be entitled for an additional incentive of ₹ 50 lakh. However, in case the construction is delayed beyond 3 years and 2 months, XY will charge a penalty of ₹ 20 lakh. At the start of the contract, AB has a reason to believe that construction will be completed in 2 years and 8 months. Assume that the construction was actually completed in 2 years 9 months.

Labour cost was originally estimated to be ₹1.20 crore (based on initial minimum wages). However, the costs have increased by 25% during the construction period.

Material costs have increased by 40% due to short-supply. The total increase in material cost due to the 40% escalation is ₹ 80 lakh.

You are required to suggest what should be the contract revenue in above case?

Assume that in year 20X2, XY has requested AB to increase the scope of the contract. An additional floor is required to be constructed and there is an increase in contract fee by ₹ 1 crore.

AB has incurred a cost of ₹ 20 lakh for getting the local authority approvals which it will be entitled to claim from XY in addition to the increase in the fixed fee.

Also measure the total contract revenue in this case.

SOLUTION

Total Revenue after considering the escalation costs, claims and incentives:

Fixed Price:	5.00 crore
Incentive for early completion	0.50 crore
Material costs recovery (to the extent of 20%)	0.40 crore
Labour costs recovery (Actual increase is less than 30%)	0.30 crore [1.20 crore x 25%]
Total Contract Revenue	6.20 crore
Add: Variation to the contract	1.00 crore
Add: Claims recoverable from XY	0.20 crore
Total Contract Revenue	7.40 crore

QUESTION 134

Sarita Construction Co. obtained a contract for construction of a dam. The following details are available in records of company for the year ended 31st March, 2018:

	Rs In Lakhs
Total Contract Price	12,000
Work Certified	6,250
Work not certified	1,250
Estimated further cost to completion	8,750

Scanned with OKEN Scanner

Progress payment received	5,500
Progress payment to be received	1,500

Applying the provisions of Accounting Standard 7 "Accounting for Construction Contracts" you are required to compute:

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

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

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

(iv) Amount due from/to customers as at the year end.

SOLUTION:

(i)	**Loss for the year ended, 31st March, 2018**	**(Rs in lakhs)**
	Amount of foreseeable loss	
	Total cost of construction (6,250 + 1,250 + 8,750)	16,250
	Less: Total contract price	(12,000)
	Total foreseeable loss to be recognised as expense	4,250

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

Loss for the year ended, 31st March, 2018 amounting Rs 4,250 will be recognized.

(ii)	**Contract work-in-progress as on 31.3.18**	**(Rs in lakhs)**
	Contract work-in-progress i.e., cost incurred to date are Rs 7,500 lakhs:	
	Work certified	6,250
	Work not certified	1,250
		7,500

(iii) **Proportion of total contract value recognised as revenue**

Cost incurred till 31.3.18 is 46.15% (7,500/16,250×100) of total costs of construction.

Proportion of total contract value recognised as revenue:

46.15% of Rs 12,000 lakhs = Rs 5,538 lakhs

(iv) **Amount due from/to customers at year end**

(Contract costs + Recognised profits – Recognised Losses) – (Progress payments received + Progress payments to be received)

= (7,500 + Nil – 4,250) – (5,500 + 1,500) Rs in lakhs

= [3,250 – 7,000] Rs in lakhs

Amount due to customers = Rs 3,750 lakhs

QUESTION 135

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

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

(b) ABC Ltd., a construction contractor, undertakes the construction of commercial complex for XYZ Ltd. ABC Ltd. submitted separate proposals for each of 3 units of commercial complex. A single agreement is entered into between the two parties. The agreement lays down the value of each of the 3 units i.e. Rs. 50 lakh, Rs. 60 lakh and Rs. 75 lakh respectively. Agreement also lays down the completion time for each unit.

Comment, with reference to AS 7, whether ABC Ltd., should treat it as a single contract or three separate contracts.

SOLUTION

(a) According to AS 7 'Construction Contracts', incentive payments are additional amounts payable to the contractor if specified performance standards are met or exceeded. For example, a contract may allow for an incentive payment to

Scanned with OKEN Scanner

the contractor for early completion of the contract. Incentive payments are included in contract revenue when both the conditions are met:

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

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

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

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

(a) separate proposals have been submitted for each asset;

(b) each asset has been subject to separate negotiation and the contractor and customer have been able to accept or reject that part of the contract relating to each asset; and

(c) the costs and revenues of each asset can be identified.

ABC Ltd. has submitted separate proposals for each of the 3 units of commercial complex. Also, the revenue and completion time has been laid down for each unit separately which implies separate negotiation for them.

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

Scanned with OKEN Scanner

24. AS – 9 "REVENUE RECOGNITION"

QUESTION 136

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

(1) Trade discount and volume rebate received.

(2) Where goods are sold to distributors or others for resale.

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

(4) Insurance agency commission for rendering services.

(5) On 11-03-2019 cloths worth Rs 50,000 were sold to X mart, but due to refurbishing of their showroom being underway, on their request, clothes were delivered on 12-04-2019.

SOLUTION

(1) Trade discounts and volume rebates received are not encompassed within the definition of revenue, since they represent a reduction of cost. Trade discounts and volume rebates given should be deducted in determining revenue.

(2) When goods are sold to distributor or others, revenue from such sales can generally be recognized if significant risks of ownership have passed; however, in some situations the buyer may in substance be an agent and in such cases the sale should be treated as a consignment sale.

(3) For transactions, where seller concurrently agrees to repurchase the same goods at a later date that are in substance a financing agreement, the resulting cash inflow is not revenue as defined and should not be recognized as revenue.

(4) Insurance agency commissions should be recognized on the effective commencement or renewal dates of the related policies.

(5) On 11.03.2019, if X mart takes title and accepts billing for the goods then it is implied that the sale is complete and all risk and reward on ownership has been transferred to the buyers.

Revenue should be recognized for year ended 31st March, 2019 notwithstanding that physical delivery has not been completed so long as there is every expectation that delivery will be made and items were ready for delivery to the buyer at the time.

QUESTION 137

Following information of BS Products Ltd. is given:

I. Goods of ₹ 2,00,000 sold to Den Ltd. on 20-03-2023 but at the request of the buyer these were delivered on 10-04-2023.

II. On 15-01-2023 goods of ₹ 3,00,000 were sent on consignment basis, of which 20% of the goods unsold are lying with the consignee as on 31-03-2023.

III. ₹ 4,00,000 worth of goods were sold on approval basis on 01-12-2022. The period of approval was 3 months after which they were considered as sold. Buyer sent approval for 75% goods upto 31-01-2023 and no approval or disapproval received for the remaining goods till 31-03-2023.

IV. Apart from the above, BS Products Ltd. sells goods to dealers also. One of the condition of sale is that interest is payable @ 2% p.m. for delayed payments by dealers. Percentage of interest recovery is only 10% i.e. ₹ 50,000 on such overdue outstanding due to various reasons. During the year 2022-23, company wants to recognize the entire interest receivable of ₹ 60,000.

You are required to advise the accountant of BS Products Ltd., with valid reasons, the amount to be recognized as revenue in above cases in the context of AS-9 and also determine the total revenue to be recognized for the year ending 31-03-2023.

SOLUTION:

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

Scanned with OKEN Scanner

II. No significant uncertainty exists regarding the amount of the consideration that will be derived from the sale of the goods.

Case (i)

The sale is complete but delivery has been postponed at buyer's request. BS Products Ltd. should recognize the entire sale of ₹ 2,00,000 for the year ended 31st March, 2023.

Case (ii)

20% goods lying unsold with consignee should be treated as closing inventory and sales should be recognized for ₹ 2,40,000 (80% of ₹ 3,00,000). In case of consignment sale revenue should not be recognized until the goods are sold to a third party.

Case (iii)

In case of goods sold on approval basis, revenue should not be recognized until the goods have been formally accepted by the buyer or the buyer has done an act adopting the transaction or the time period for rejection has elapsed or where no time has been fixed, a reasonable time has elapsed. Therefore, revenue should be recognized for the total sales amounting ₹ 4,00,000 as the time period for rejecting the goods had expired.

Case (iv)

As per the standard, "where the ability to assess the ultimate collection with reasonable certainty is lacking at the time of raising any claim, the revenue recognition is postponed to the extent of uncertainty involved. In such cases, the revenue is recognized only when it is reasonably certain that the ultimate collection will be made". In this case, interest should be recognized only if the ultimate collection is certain and the company expects to realize interest for the delayed payments for ₹ 50,000 only. Hence, based on the past experience, the realization of interest for the delayed payments by the agent is certain only to the extent of this amount and not ₹ 60,000. Therefore, the interest income of ₹ 50,000 should be recognized in the books for the year ended 31st March, 2023.

Thus total revenue amounting ₹ 8,90,000 (2,00,000 + 2,40,000 + 4,00,000 + 50,000) will be recognized for the year ended 31st March, 2023 in the books of BS Products Ltd.

QUESTION 138

For the year ended 31st March 20X1, KY Enterprises has entered into the following transactions.

On 31 March 20X1, KY supplied two machines to its customer ST. Both machines were accepted by ST on 31 March 20X1. Machine 1 was a machine that was routinely supplied by KY to many customers and the installation process was very simple.

Machine 1 was installed on 2 April 20X1 by ST's employees.

Machine 2 being more specialised in nature requires an installation process which is more complicated, requiring significant assistance from KY. Machine 2 was installed between 2 and 5 April 20X1. Details of costs and sales prices are as follows:

	Machine 1	**Machine 2**
Sale Price	3,20,000	3,00,000
Cost of production	1,60,000	1,50,000
Installation fee	Nil	10,000

How should above transactions be recognized by KY Enterprises for the year ended 31st March 20X1?

SOLUTION

Machine 1: As the installation process is simple, revenue from Machine 1 will be recognized on 31 March 20X1.

Revenue (Machine 1)	₹ 3,20,000
Cost of Goods Sold	₹ 1,60,000
Profit during the period	₹ 1,60,000

Since the question specifies that the machine is already accepted by ST on 31 March 20X1, the revenue arising from sale of the machine needs to be recognized for the year ending 31 March 20X1. This is because acceptance of the machine

Scanned with OKEN Scanner

indicates that the risks and rewards pursuant to the ownership are transferred to ST.

Machine 2: Installation process for Machine 2 is more complicated, requiring significant assistance from KY Ltd. However, question specifies that the machine is already accepted by ST on 31 March 20X1. Assuming that there is no further approval/acceptance required from the buyer for the Machine sold, revenue from sale of Machine 2 can be recognized for the year ending 31 March 20X1.

Revenue (Machine 2)	₹ 3,00,000
Cost of Goods Sold	₹ 1,50,000
Profit during the period	₹ 1,50,000

However, installation fee which is for rendering installation services cannot be recognized until the installation is complete. Since the machine is pending installation, the revenue in respect of installation charges ₹ 10,000 needs to be recognized on 5 April 20X1 once the installation process gets completed

QUESTION 139

Sarita Publications publishes a monthly magazine on the 15th of every month. It sells advertising space in the magazine to advertisers on the terms of 80% sale value payable in advance and the balance within 30 days of the release of the publication. The sale of space for the March 2014 issue was made in February 2014. The magazine was published on its scheduled date. It received ₹ 2,40,000 on 10.3.2014 and ₹ 60,000 on 10.4.2014 for the March 2014 issue. Discuss in the context of AS 9 the amount of revenue to be recognized and the treatment of the amount received from advertisers for the year ending 31.3.2014. What will be the treatment if the publication is delayed till 2.4.2014?

SOLUTION:

As per para 12 of AS 9 "Revenue Recognition", In a transaction involving the rendering of services, performance should be measured either under the completed service contract method or under the proportionate completion method, whichever relates the revenue to the work accomplished.

In the given case, income accrues when the related advertisement appears before public. The advertisement service would be considered as performed on the day the advertisement is seen by public and hence revenue is recognized on that date. In this case, it is 15.03.2014, the date of publication of the magazine.

Hence, ₹ 3,00,000 (₹ 2,40,000 + ₹ 60,000) is recognized as income in March, 2014. The terms of payment are not relevant for considering the date on which revenue is to be recognized. ₹ 60,000 is treated as amount due from advertisers as on 31.03.2014 and ₹ 2,40,000 will be treated as payment received against the sale.

However, if the publication is delayed till 02.04.2014 revenue recognition will also be delayed till the advertisements get published in the magazine. In that case revenue of ₹ 3,00,000 will be recognized for the year ended 31.03.2015 after the magazine is published on 02.04.2014. The amount received from sale of advertising space on 10.03.2014 of ₹ 2,40,000 will be considered as an advance from advertisers for the year ended 31st March, 2014.

Scanned with OKEN Scanner

25. AS 12 - ACCOUNTING FOR GOVERNMENT GRANTS

QUESTION 140

How would you treat the following in the accounts in accordance with AS 12 'Government Grants'?

(i) Rs. 35 Lakhs received from the Local Authority for providing medical facilities to the employees.

(ii) Rs. 100 Lakhs received as Subsidy from the Central Government for setting up a unit in a notified backward area.

(iii) Rs. 10 Lakhs Grant received from the Central Government on installation of anti-pollution equipment.

SOLUTION

(i) Rs. 35 lakhs received from the local authority for providing medical facilities to the employees is a grant received in the nature of revenue grant. Such grants are generally presented as a credit in the profit and loss statement, either separately or under a general heading such as 'Other Income'. Alternatively, Rs. 35 lakhs may be deducted in reporting the related expense i.e., employee benefit expenses.

(ii) As per AS 12 'Accounting for Government Grants', where the government grants are in the nature of promoters' contribution, i.e., they are given with reference to the total investment in an undertaking or by way of contribution towards its total capital outlay and no repayment is ordinarily expected in respect thereof, the grants are treated as capital reserve which can be neither distributed as dividend nor considered as deferred income.

In the given case, the subsidy received from the Central Government for setting up a unit in notified backward area is neither in relation to specific fixed asset nor in relation to revenue. Thus, amount of Rs 100 lakhs should be credited to capital reserve.

(iii) Rs 10 lakhs grant received for installation anti-pollution equipment is a grant related to specific fixed asset. Two methods of presentation in financial statements of grants related to specific fixed assets are regarded as acceptable alternatives. Under first method, the grant is shown as a deduction from the gross value of the asset concerned in arriving at its book value. The grant is thus recognised in the profit and loss statement over the useful life of a depreciable asset by way of a reduced depreciation charge. Under the second method, grants related to depreciable assets are treated as deferred income which is recognised in the profit and loss statement on a systematic and rational basis over the useful life of the asset.

Thus, Rs 10 lakhs may either be deducted from the cost of equipment or treated as deferred income to be recognized on a systematic basis in profit & Loss A/c over the useful life of equipment.

QUESTION 141

Santosh Ltd. has received a grant of ₹8 crores from the Government for setting up a factory in a backward area. Out of this grant, the company distributed ₹2 crores as dividend. Also, Santosh Ltd. received land free of cost from the State Government but it has not recorded it at all in the books as no money has been spent. In the light of AS 12 examine, whether the treatment of both the grants is correct.

SOLUTION

As per AS 12 'Accounting for Government Grants', when government grant is received for a specific purpose, it should be utilised for the same. So the grant received for setting up a factory is not available for distribution of dividend.

In the second case, even if the company has not spent money for the acquisition of land, land should be recorded in the books of accounts at a nominal value. The treatment of both the elements of the grant is incorrect as per AS 12.

QUESTION 142

A Ltd. purchased a machinery for Rs 40 lakhs. (Useful life 4 years and residual value Rs 8 lakhs) Government grant received is Rs 16 lakhs.

Show the Journal Entry to be passed at the time of refund of grant in the third year and the value of the fixed assets, if:

(1) the grant is credited to Fixed Assets A/c.

(2) the grant is credited to Deferred Grant A/c.

Scanned with OKEN Scanner

SOLUTION

IN THE BOOKS OF A LTD.

Journal Entries (at the time of refund of grant)

(1) If the grant is credited to Fixed Assets Account:

		Rs	Rs
I.	Fixed Assets A/c Dr.		16 lakhs
	To Bank A/c	16 lakhs	
	(Being grant refunded) The amount of refund should be Rs 16 Lakhs		

The balance of fixed assets after two years depreciation will be Rs 16 lakhs (W.N.1) and after refund of grant it will become (Rs 16 lakhs + Rs 16 lakhs) = Rs 32 lakhs on which depreciation will be charged for remaining two years. Depreciation = (32-8)/2 = Rs 12 lakhs p.a. will be charged for next two years.

(2) If the grant is credited to Deferred Grant Account:

As per para 14 of AS 12 'Accounting for Government Grants,' income from Deferred Grant Account is allocated to Profit and Loss account usually over the periods and in the proportions in which depreciation on related assets is charged. Accordingly, in the first two years (Rs 16 lakhs /4 years) = Rs 4 lakhs p.a. x 2 years = Rs 8 lakhs were credited to Profit and Loss Account and Rs 8 lakhs was the balance of Deferred Grant Account after two years.

Therefore, on refund in the 3rd year, following entry will be passed:

		Rs	Rs
I.	Deferred Grant A/c Dr.	8 lakhs	
	Profit & Loss A/c Dr.	8 lakhs	
	To Bank A/c		16 lakhs
	(Being Government grant refunded)		

Deferred grant account will become Nil. The fixed assets will continue to be shown in the books at Rs 24 lakhs (W.N.2) and depreciation will continue to be charged at Rs 8 lakhs per annum for the remaining two years.

Working Notes:

i. **Balance of Fixed Assets after two years but before refund (under first alternative)**

Fixed assets initially recorded in the books = Rs 40 lakhs – Rs 16 lakhs = Rs 24 lakhs

Depreciation p.a. = (Rs 24 lakhs – Rs 8 lakhs)/4 years = Rs 4 lakhs per year

Value of fixed assets after two years but before refund of grant = Rs 24 lakhs – (Rs 4 lakhs x 2 years) = Rs 16 lakhs

ii. **Balance of Fixed Assets after two years but before refund (under second alternative)**

Fixed assets initially recorded in the books = Rs 40 lakhs

Depreciation p.a. = (Rs 40 lakhs – Rs 8 lakhs)/4 years = Rs 8 lakhs per year

Book value of fixed assets after two years = Rs 40 lakhs – (Rs 8 lakhs x 2 years)

= Rs 24 lakhs

Note: It is assumed that the question requires the value of fixed assets is to be given after refund of government grant.

QUESTION 143

Samrat Limited has set up its business in a designated backward area which entitles the company for subsidy of 25% of the total investment from Government of India. The company has invested Rs. 80 crores in the eligible investments. The company is eligible for the subsidy and has received Rs. 20 crores from the government in February 2019. The company wants to recognize the said subsidy as its income to improve the bottom line of the company.

Do you approve the action of the company in accordance with the Accounting Standard?

SOLUTION

As per AS 12 "Accounting for Government Grants", where the government grants are in the nature of promoters' contribution, i.e., they are given with reference to the total investment in an undertaking or by way of contribution towards

Scanned with OKEN Scanner

its total capital outlay (for example, Central Investment Subsidy Scheme) and no repayment is ordinarily expected in respect thereof, the grants are treated as capital reserve which can be neither distributed as dividend nor considered as deferred income.

The subsidy received by Samrat Ltd. for setting up its business in a designated backward area will be treated as grant by the government in the nature of promoter's contribution as the grant is given with reference to the total investment in an undertaking i.e., subsidy is 25% of the eligible investment and also no repayment is apparently expected in respect thereof.

Since the subsidy received is neither in relation to specific fixed assets nor in relation to revenue. Thus, the company cannot recognize the said subsidy as income in its financial statements in the given case. It should be recognized as capital reserve which can be neither distributed as dividend nor considered as deferred income.

QUESTION 144

On 1stApril 2021, Eleanor Limited purchased a manufacturing Plant for ` 60 lakhs, which has an estimated useful life of 10 years with a salvage value of ` 10 lakhs. On purchase of the Plant, a grant of ` 20 lakhs was received from the government.

You are required to calculate the amount of depreciation as per AS-12 for the financial year 2022-23 in the following cases:

(i) If the grant amount is deducted from the value of Plant.

(ii) If the grant is treated as deferred income.

(ii) If the grant amount is deducted from the value of Plant, but at the end of the year 2022-2023 grant is refunded to the extent of ` 4 lakhs, due to non-compliance of certain conditions.

(iv) If the grant is treated as the promoter's contribution.

(Assume depreciation on the basis of Straight-Line Method.)

SOLUTION

Calculation of depreciation as per AS 12 for the financial year 2022-23:

(i) If the grant amount is deducted from the value of Plant, then the amount of deprecation will be ` 3,00,000 p.a. (` 60,00,000 - ` 10,00,000 - ` 20,00,000) / 10 year.

(ii) If the grant is treated as deferred income, then amount of depreciation will be ` 5,00,000 p.a. (` 60,00,000 - ` 10,00,000) / 10 year.

(iii) If the grant amount is deducted from the value of plant, but at the end of the year 2022-23 grant is refunded to the extent of ` 4 lakh then the amount of depreciation will be ` 3,00,000 p.a. (` 60,00,000 - ` 10,00,000 - ` 20,00,000) /10 year for year 2021-22 and for the year 2022-23 Depreciation will be ` 3,00,000 calculated as follows, (` 60,00,000 - ` 10,00,000 - ` 20,00,000– ` 3,00,000) / 10 years.

Note: It is assumed that the depreciation for the year has been charged on the book value on the plant before making adjustment for grant. Alternatively, if it is considered otherwise then the depreciation will be charged after making adjustment for grant. In that case depreciation for the year 2022-23 will be as ` 3,44,444 calculated as follows, (` 60,00,000 - ` 10,00,000 - ` 20,00,000 + 4,00,000– ` 3,00,000 / 9 years

(iv) If the grant is treated as promoter's contribution, then the amount of depreciation will be ` 5,00,000 p.a. (` 60,00,000 -10,00,000) /10 year.

Note:

It is assumed that the depreciation for the year has been charged on the book value on the plant before making adjustment for grant. Alternatively, if it is considered otherwise then the depreciation will be charged after making adjustment for grant. In that case depreciation for the year 2022-23 will be as:

Cost of Plant	60,00,000
Less: Salvage Value	10,00,000
Less: Grant	20,00,000
Add: Grant Refundable	4,00,000

Scanned with OKEN Scanner

	34,00,000
Less: Depreciation for 2021-22	3,00,000
	31,00,000
Useful Life (years)	9
Depreciation for 2022-23	**3,44,4444**

QUESTION 145

Suraj Limited provides you the following information:

(i) It received a Government Grant @40% towards the acquisition of Machinery worth Rs. 25 crores.

(ii) It received a Capital Subsidy of Rs. 150 lakhs from Government for setting up a plant costing Rs. 300 lakhs in a notifies backward region.

(iii) It received Rs. 50 lakhs from Government for setting up a project for supply of arsenic fire water in a notified area.

(iv) It received Rs. 5 lakhs from a Local Authority for providing Corona Vaccine free of charge to its employees and their families.

(v) It also received a performance award of Rs. 500 Lakhs from government with a condition of major renovation in the power plant within 3 years. Suraj Limited incurred 90% of amount towards capital expenditure and balance for revenue expenditure.

State, how you will treat the above in the books of Suraj Limited.

SOLUTION

(i) As per AS 12 "Accounting for Govt. Grants", two methods of presentation in financial statements of grants related to specific fixed assets are regarded as acceptable alternatives. Under the first alternative, the grant of Rs. 10 crores (40% of 25 crores) is shown as a deduction from the gross value of the asset concerned in arriving at its book value. The grant is thus recognized the profit and loss statement over the useful life of a depreciable asset by way of a reduced depreciation charge. Under second alternative method, grant amounting Rs. 10 crores is treated as deferred income which is recognized in the profit and loss statement on a systematic and rational basis over the useful life of the asset.

(ii) In the given case, the grant amounting Rs. 150 lakhs received from the Central Government for setting up a plant in notified backward area may be considered as in the nature of promoters' contribution. Thus, amount of Rs. 150 lakhs should be credited to capital reserve and the plant will be shown at Rs. 300 lakhs.

(iii) Rs. 50 lakhs received from Govt. for setting up a project for supply of arsenic free water in notified area should be credited to capital reserve.

Alternatively, if it is assumed that the project consists of capital asset only, then the amount of Rs. 50 lakhs received from Govt. for setting up a project for supply of arsenic free water should either be deducted from cost of asset of the project concerned in the balance sheet or treated as deferred income which is recognized in the profit and loss statement on a systematic and rational basis over the useful life of the asset.

(iv) Rs. 5 lakhs received from the local authority for providing corona vaccine to the employees is a grant received in nature of revenue grant. Such grants are generally presented as a credit in the profit and loss account, either separately or under a general heading 'Other Income'. Alternatively, Rs. 5 lakhs may be deducted in reporting the related expense i.e., employee benefit expenses.

(v) Rs. 500 Lakhs will be reduced from the renovation cost of power plant or will be treated as deferred income irrespective of the expenditure done by the entity out of it as it was specifically received for the purpose major renovation of power plant. However, it may be, later on, decided by the Govt. whether the grant will have to be refunded or not due to non-compliance of conditions attached to the grant.

Scanned with OKEN Scanner

26. AS 17 – "SEGMENT REPORTING"

QUESTION 146:

X Ltd. provides the information of Following 10 Segments

Rs. In Crores

Particulars	A	B	C	D	E	F	G	H	I	J	Total
Segment Revenues	10	15	1	8	2	3	5	10	6	3	63
Segment Assets	10	20	2	10	4	3	2	1	2	10	64
Segment Results	5	2	1	4	1	0	(5)	(2)	(1)	10	16

Additional Information:

- Segment F was reported in Previous Year.
- Segment A Revenue Consist of Extraordinary Item of Rs. 2 Cr.
- Segment D has assets used for Head office worth of Rs. 3 Cr.

Identify the Reportable Segments.

SOLUTION:

a) Revenue of Segment A will be reduced by Rs. 2 Cr. As the Segment Revenue does not include the Revenue from Extraordinary Item. Therefore, the Revenue of Segment A will be Rs. 8 Cr.

b) Asset Value of Segment D will be reduced by Rs. 3 Cr. As the Segment Asset does not include the Asset value which is used for Head office. Therefore, the Asset Value of Segment D will be Rs. 7 Cr.

Revised Table of Segments will be

Particulars	A	B	C	D	E	F	G	H	I	J	Total
Segment Revenues	8	15	1	8	2	3	5	10	6	3	61
Segment Assets	10	20	2	7	4	3	2	1	2	10	61
Segment Results	5	2	1	4	1	0	(5)	(2)	(1)	10	16

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

(A) Its revenue from sales to external customers and from other transactions with other segments is 10% or more of the total revenue- external and internal of all segments; or

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

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

whichever is greater in absolute amount; or

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

If the total external revenue attributable to reportable segments constitutes less than 75% of total enterprise revenue, additional segments should be identified as reportable segments even if they do not meet the 10% thresholds until atleast 75% of total enterprise revenue is included in reportable segments.

Conclusion:

- On the Basis of Turnover Criteria segment A, B, D & H are Reportable Segments.
- On the Basis of Asset Criteria Segment A, B, D & J are Reportable Segments.
- On the Basis of Result Criteria Segment A, D, G & J are Reportable Segments.
- As Segment F was reported in Previous Year so segment F should be Reported even if it does not fulfill conditions of Para 27 this year.

QUESTION 147

M/s Nathan Limited has three segments namely P, Q and R. The assets of the company are Rs 15 crores. Segment P has 4 crores, Segment Q has 6 crores and Segment R has 5 crores. Deferred tax assets included in the assets of each segment are P - Rs 1 crore, Q - Rs 0.90 crores and R - Rs 0.80 crores. The accountant contends all these three segments are reportable segments. Comment.

Scanned with OKEN Scanner

SOLUTION:

According to AS 17 "Segment Reporting", segment Assets do not include income tax assets.

Therefore, the revised total assets are 12.3 crores [Rs 15 – (Rs 1 + 0.9 + 0.8).

Details of Segment wise assets

Segment P holds total assets of Rs 3 crores (Rs 4 crores – Rs 1 crores);

Segment Q holds Rs 5.1 crores (Rs 6 crores – 0.9 crores);

Segment R holds Rs 4.2 crores (Rs 5 crores – Rs 0.8 crores).

Thus, all the three segments hold more than 10% of the total assets, all segments are reportable segments.

Hence, the contention of the Accountant that all three segments are reportable segments is correct.

QUESTION 148:

Prepare a segmental report for publication in Diversifiers Ltd. from the following details of the company's three divisions and the head office:

	Rs. ('000)
Forging Shop Division	
Sales to Bright Bar Division	4,575
Other Domestic Sales	90
Export Sales	6,135
	10,800
Bright Bar Division	
Sales to Fitting Division	45
Export Sales to Rwanda	300
	345
Fitting Division	
Export Sales to Maldives	270

Particulars	Head Office Rs.('000)	Forging Shop Division Rs. ('000)	Bright Bar Division Rs. ('000)	Fitting Division Rs. ('000)
Pre-tax operating result		240	30	(12)
Head office cost reallocated		72	36	36
Interest costs		6	8	2
Fixed assets	75	300	60	180
Net current assets	72	180	60	135
Long-term liabilities	57	30	15	180

SOLUTION:

Diversifiers Ltd. Segmental Report

(Rs. '000)

Particulars	Divisions			Inter Segment Eliminations	Consolidated Total
	Forging shop	Bright Bar	Fitting		
Segment Revenue					
Sales:					
Domestic	90	-	-	-	90
Export	6,135	300	270	-	6,705
External Sales	6,225	300	270	-	6,795
Inter-Segment Sales	4,575	45	-	4,620	-
Total Revenue	10,800	345	270	4,620	6,795

Scanned with OKEN Scanner

Segment Result (Given)	240	30	(12)		258
Head Office Expenses					(144)
Operating Profit					114
Interest Expense					(16)
Profit Before Tax					98
Information in Relation to Assets and Liabilities:					
Fixed Assets	300	60	180	-	540
Net Current Assets	180	60	135	-	375
Segment assets	480	120	315	-	915
Unallocated Corporate Assets (75 + 72)	-	-	-	-	147
Total assets					1,062
Segment liabilities	30	15	180	-	225
Unallocated corporate liabilities					57
Total liabilities					282

Sales Revenue by Geographical Market

	Home Sales	Export Sales (by forging shop division)	Export to Rwanda	Export to Maldives	(Rs. '000) Consolidated Total
External sales	90	6,135	300	270	6,795

Scanned with OKEN Scanner

27. AS 25 - INTERIM FINANCIAL REPORTING

QUESTION 149

Sincere Corporation is dealing in seasonal product. Sales pattern of the product quarter-wise is as follows:

1st quarter 30th June 10%
2nd quarter 30th September 10%
3rd quarter 31st December 60%
4th quarter 31st March 20%

Information regarding the 1st quarter ended on 30th June, 20X1 is as follows:

Sales	80 crores
Salary and other expenses	60 crores
Advertisement expenses (routine)	4 crores
Administrative and selling expenses	8 crores

While preparing interim financial report for first quarter Sincere Corporation wants to defer ₹ 10 crores expenditure to third quarter on the argument that third quarter is having more sales, therefore, the third quarter should be debited by more expenditure. Considering the seasonal nature of business and the expenditures are uniform throughout all quarters, calculate the result of the first quarter as per AS 25. Also give a comment on the company's view.

Solution

Particulars	(₹ In crores)	
Result of first quarter ended 30th June, 20X1 Turnover Other Income	80 Nil	
Total (a)		80
Less: Changes in inventories		Nil
Salaries and other cost		60
Administrative and selling Expenses (4+8)		12
Total (b)		72
Profit (a)-(b)		8

According to AS 25, the Income and Expense should be recognized when they are earned and incurred respectively. Therefore, seasonal incomes will be recognized when they occur. Thus, the company's view is not as per AS 25.

QUESTION 150

What are the periods for which Interim financial Statements are required to be presented? You are required to answer your question in light of preparation of financial statements for the period ended and as at 31st December, 20X1. The Financial Year is FY 20X1-X2.

SOLUTION

As per Accounting Standard 25, Interim reports should include interim financial statements (condensed or complete) for periods as given below.

Statement	Current period	Comparative period
Balance sheet	End of current interim period	End of immediately preceding financial year
Statement of profit and loss	Current interim period and cumulatively for the year-to-date	Comparable interim period and year-to-date of immediately preceding financial year
Cash flow statement	Cumulatively for the current financial year- to-date	Comparable year-to-date of immediately preceding financial year

Scanned with OKEN Scanner

In light of the above, following periods needs to be covered in interim financial statements for the period ended and as at 31st December, 20X1:

Balance Sheet	as of the end of the current interim period and a comparative balance sheet as of the end of the immediately preceding financial year (As at 31 December 20X1 and 31 March 20X1).
Statements of Profit and Loss	for the current interim period and cumulatively for the current financial year to date, with comparative statements of profit and loss for the comparable interim periods (current and year-to-date) of the immediately preceding financial year. (for 3 months and 9 months i.e., year to date ended 31 December 20X1 and same for 31 December 20X0 being comparative period).
Cash Flow Statement	cumulatively for the current financial year to date, with a comparative statement for the comparable year-to-date period of the immediately preceding financial year. (year to date i.e., 1 April 20X1 to 31 December 20X1 and 1 April 20X0 to 31 December 20X0).

QUESTION 151

Antarbarti Limited reported a Profit Before Tax (PBT) of ₹ 4 lakhs for the third quarter ending 30-09-20X1. On enquiry you observe the following. Give the treatment required under AS 25:

(i) Dividend income of ₹ 4 lakhs received during the quarter has been recognized to the extent of ₹ 1 lakh only.

(ii) 80% of sales promotion expenses ₹ 15 lakhs incurred in the third quarter has been deferred to the fourth quarter as the sales in the last quarter is high.

(iii) In the third quarter, the company changed depreciation method from WDV to SLM, which resulted in excess depreciation of ₹ 12 lakhs. The entire amount has been debited in the third quarter, though the share of the third quarter is only ₹ 3 lakhs.

(iv) ₹ 2 lakhs extra-ordinary gain received in third quarter was allocated equally to the third and fourth quarter.

(v) Cumulative loss resulting from change in method of inventory valuation was recognized in the third quarter of ₹ 3 lakhs. Out of this loss ₹ 1 lakh relates to previous quarters.

(vi) Sale of investment in the first quarter resulted in a gain of ₹ 20 lakhs. The company had apportioned this equally to the four quarters.

Prepare the adjusted profit before tax for the third quarter.

Solution

As per para 36 of AS 25 “Interim Financial Reporting”, seasonal or occasional revenue and cost within a financial year should not be deferred as of interim date until it is appropriate to defer at the end of the enterprise’s financial year. Therefore, dividend income, extra-ordinary gain, and gain on sale of investment received during 3rd quarter should be recognised in the 3rd quarter only. Similarly, sales promotion expenses incurred in the 3rd quarter should also be charged in the 3rd quarter only.

Further, as per AS 10, Property, Plant and Equipment, if there is change in the depreciation method, such a change should be accounted for as a change in accounting estimate in accordance with AS 5, Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies, and applied prospectively. Therefore, no adjustment would be required due to change in the method of depreciation.

Accordingly, the adjusted profit before tax for the 3rd quarter will be as follows:

Scanned with OKEN Scanner

Statement showing Adjusted Profit Before Tax for the third quarter

	(₹ in lakhs)
Profit before tax (as reported)	4
Add: Dividend income ₹ (4-1) lakhs	3
Excess depreciation charged in the 3rd quarter, due to change in the method	-
Extra ordinary gain ₹ (2-1) lakhs	1
Cumulative loss due to change in the method of inventory valuation should be applied retrospectively ₹ (3-2) lakhs	1
	9
Less: Sales promotion expenses (80% of ₹ 15 lakhs)	(12)
Gain on sale of investment (occasional gain should not be deferred)	(5)
Adjusted Profit before tax for the third quarter	**(8)**

Scanned with OKEN Scanner

28. AS 4 - CONTINGENCIES & EVENTS OCCURRING AFTER THE BALANCE SHEET DATE

QUESTION 152:

A company has filled a legal suit against the debtor from whom Rs. 15 lakh is recoverable as on 31.03.2019. The chances of recovery by way of legal suit are not good as per the legal opinion by the counsel in April, 2019. Can the company provide for full amount of Rs. 15 lakh as provision for doubtful debts? Discuss in brief.

ANSWER:

As per AS 4 (Revised) "Contingencies and Events Occurring After the Balance Sheet Date", assets and liabilities should be adjusted for events occurring after the balance sheet date that provide additional evidence to assist the estimation of amounts relating to conditions existing at the balance sheet date.

In the given case, company should make the provision for doubtful debts, as legal suit has been filed on 31st March, 2019 and the chances of recovery from the suit are not good. Though, the actual result of legal suit will be known in future yet situation of non-recovery from the debtors exists before finalisation of financial statements. Therefore, provision for doubtful debts should be made for the year ended on 31st March, 2019.

QUESTION 153:

A Limited Company closed its accounting year on 30.6.20X1 and the accounts for that period were considered and approved by the board of directors on 20th August, 20X1. The company was engaged in laying pipe line for an oil company deep beneath the earth. While doing the boring work on 1.9.20X1 it had met a rocky surface for which it was estimated that there would be an extra cost to the tune of Rs.80 lakhs. You are required to state with reasons, how the event would be dealt with in the financial statements for the year ended 30.6.20X1.

ANSWER

AS 4 (Revised) on Contingencies and Events Occurring after the Balance Sheet Date defines 'events occurring after the balance sheet date' as 'significant events, both favourable and unfavourable, that occur between the balance sheet date and the date on which financial statements are approved by the Board of Directors in the case of a company'. The given case is discussed in the light of the above mentioned definition and requirements given in AS 4 (Revised).

In this case the incidence, which was expected to push up cost, became evident after the date of approval of the accounts. So it is not an 'event occurring after the balance sheet date'. However, this may be mentioned in the Report of Approving Authority.

QUESTION 154:

During the year 20X1-20X2, Raj Ltd. was sued by a competitor for Rs. 15 lakhs for infringement of a trademark. Based on the advice of the company's legal counsel, Raj Ltd. provided for a sum of Rs. 10 lakhs in its financial statements for the year ended 31st March, 20X2. On 18th May, 20X2, the Court decided in favour of the party alleging infringement of the trademark and ordered Raj Ltd. to pay the aggrieved party a sum of Rs.14 lakhs. The financial statements were prepared by the company's management on 30th April, 20X2, and approved by the board on 30th May, 20X2.

ANSWER:

As per AS 4 (Revised), adjustments to assets and liabilities are required for events occurring after the balance sheet date that provide additional information materially affecting the determination of the amounts relating to conditions existing at the balance sheet date.

In the given case, since Raj Ltd. was sued by a competitor for infringement of a trademark during the year 20X1-X2 for which the provision was also made by it, the decision of the Court on 18th May, 20X2, for payment of the penalty will constitute as an adjusting event because it is an event occurred before approval of the financial statements. Therefore,

Scanned with OKEN Scanner

Raj Ltd. should adjust the provision upward by Rs. 4 lakhs to reflect the award decreed by the Court to be paid by them to its competitor.

Had the judgment of the Court been delivered on 1st June, 20X2, it would be considered as an event occurring after the approval of the financial statements which is not covered by AS 4 (Revised). In that case, no adjustment in the financial statements of 20X1-X2 would have been required.

QUESTION 155

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

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

SOLUTION:

As per AS 4 (Revised) "Contingencies and Events occurring after the Balance Sheet Date", an event occurring after the balance sheet date should be an adjusting event even if it does not reflect any condition existing on the balance sheet date, if the event is such as to indicate that the fundamental accounting assumption of going concern is no longer appropriate.

The fire occurred in the factory and office premises of an enterprise after 31 March, 2018 but before approval of financial statement of 30.4.18. The loss by fire is of such a magnitude that it is not reasonable to expect the Dee Ltd. to start operations again, i.e., the going concern assumption is not valid. Since the fire occurred after 31/03/18, the loss on fire is not a result of any condition existing on 31/03/18. But the loss due to fire is an adjusting event the entire accounts need to be prepared on a liquidation basis with adequate disclosures by the company by way of note in its financial statements in the following manner:

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

QUESTION 156

Neel Limited has its corporate office in Mumbai and sells its products to its stockists all over India. On 31st March, 20X1, the company wants to recognize receipts of cheques bearing date 31st March, 20X1 or before, as "Cheques in Hand" by reducing "Trade Receivables". The Cheques in Hand is shown in the Balance sheet as an item of Cash and Cash Equivalents. All the cheques are presented to the bank in the month of April 20X1 and are also realized in the same month in normal course. State with reasons, whether each of the following is an adjusting event and how this fact is to be disclosed by the company, with reference to the relevant accounting standard:

(a) Cheques collected by marketing personnel of the company from stockists on or before 31st March, 20X1.

(b) Cheques sent by the stockists through courier on or before 31st March, 20X1.

SOLUTION:

(a) Cheques collected by the marketing personnel of the company is an adjusting event as the marketing personnels are employees of the company and therefore, are representatives of the company. Handing over of cheques by the stockist to the marketing employees discharges the liability of the stockist. Therefore, cheques collected by the marketing personnel of the company on or before 31st March, 20X1 require adjustment from the stockists' accounts i.e. from 'Trade Receivables A/c' even though these cheques (dated on or before 31st March, 20X1) are presented in the bank in the month of April, 20X1 in the normal course. Hence, collection of cheques by the marketing personnel is an adjusting event as per AS 4 'Contingencies and Events Occurring after the Balance Sheet Date'. Such 'cheques in hand' will be shown in the Balance Sheet as 'Cash and Cash equivalents' with a disclosure in the Notes to accounts about the accounting policy followed by the company for such cheques.

(b) Even if the cheques bear the date 31st March or before and are sent by the stockists through courier on or before 31st March, 20X1, it is presumed that the cheques will be received after 31st March. Collection of cheques after 31st March, 20X1 does not represent any condition existing on the balance sheet date i.e. 31st March. Thus, the

Scanned with OKEN Scanner

collection of cheques after balance sheet date is not an adjusting event. Cheques that are received after the balance sheet date should be accounted for in the period in which they are received even though the same may be dated 31st March or before as per AS 4. Moreover, the collection of cheques after balance sheet date does not represent any material change affecting financial position of the enterprise, so no disclosure in the Director's Report is necessary.

QUESTION 157

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

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

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

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

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

SOLUTION:

Events occurring after the balance sheet date are those significant events, both favourable and unfavourable, that occur between the balance sheet date and the date on which the financial statements are approved by the Board of Directors in the case of a company, and, by the corresponding approving authority in the case of any other entity. Assets and liabilities should be adjusted for events occurring after the balance sheet date that provide additional evidence to assist the estimation of amounts relating to conditions existing at the balance sheet date or that indicate that the fundamental accounting assumption of going concern is not appropriate. In the given case, financial statements are approved by the approving authority on 30 June 2020. On the basis of above principles, following will be the accounting treatment in the financial statements for the year ended at 31 March 2020:

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

(ii) A fire took place after the balance sheet date i.e., during 2020-2021 financial year. Hence, the financial statements for the year 2019-2020 should not be adjusted for loss occurred due to fire. However, in this circumstance, the going concern assumption will be evaluated. In case the going concern, assumption is considered to be appropriate even after the occurrence of fire, no disclosure of the same is required in the financial statements.

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

QUESTION 158

State with reasons, how the following events would be dealt with in the financial statements of Hari Ltd. for the year ended 31st March, 2022 (accounts were approved on 25th July, 2022):

(1) Negotiations with another company for acquisition of its business was started on 21st January, 2022. Hari Ltd. invested Rs. 40 lakh on 22nd April, 2022.

(2) The company made a provision for bad debts @ 4% of its total debtors (as per trend followed from the previous years). In the second week of March 2022, a debtor for Rs. 2,50,000 had suffered heavy loss due to an earthquake;

Scanned with OKEN Scanner

the loss was not covered by any insurance policy. In May, 2022 the debtor became bankrupt.

(3) During the year 2021-22, Hari Ltd. was sued by a competitor for Rs. 13 lakhs for infringement of a trademark. Based on the advice of the company's legal counsel, Hari Ltd. provided for a sum of Rs. 8 lakhs in its financial statements for the year ended 31st March, 2022. On 26th May, 2022, the Court decided in favour of the party alleging infringement of the trademark and ordered Hari Ltd. to pay the aggrieved party a sum of Rs. 12 lakhs.

(4) Cashier of Hari Ltd. embezzled cash amounting to Rs. 3,00,000 during March, 2022. However, the same comes to the notice of Company management during August, 2022.

(5) Cheques dated 31st March, 2022 collected in the month of April, 2022. All cheques are presented to the bank in the month of April, 2022 and are also realized in the same month in the normal course after deposit in the bank.

SOLUTION:

(i) As per AS 4'Contingencies and Events Occurring After the Balance Sheet Date', disclosure should be made in the report of the approving authority of those events occurring after the balance sheet date that represent material changes and commitments affecting the financial position of the enterprise, the investment of Rs. 40 lakhs in April, 2022 in the acquisition of another company should be disclosed in the report of the Board of Directors to enable users of financial statements to make proper evaluations and decisions.

(ii) As per AS 4, adjustment to assets and liabilities are required for events occurring after the balance sheet date that provide additional information materially affecting the determination of the amounts relating to conditions existing at the Balance Sheet date. A debtor for Rs. 2,50,000 suffered heavy loss due to earthquake in the second week of March, 2022 which was not covered by insurance. This information with its implications was already known to the company. The fact that he became bankrupt in May, 2022 (after the balance sheet date) is only an additional information related to the existing condition on the balance sheet date. Accordingly, full provision for bad debts amounting Rs. 2,50,000 should be made, to cover the loss arising due to the insolvency of a debtor, in the final accounts for the year ended 31st March 2022.

(iii) As per AS 4, adjustments to assets and liabilities are required for events occurring after the balance sheet date that provide additional information materially affecting the determination of the amounts relating to conditions existing at the balance sheet date. In the given case, since Hari Ltd. was sued by a competitor for infringement of a trademark during the year 2021- 22 for which the provision was also made by it, the decision of the Court on 26 th May, 2022, for payment of the penalty will constitute as an adjusting event because it is an event occurred before approval of the financial statements. Therefore, Hari Ltd. should adjust the provision upward by Rs. 4 lakhs to reflect the award decreed by the Court to be paid by them to its competitor.

(iv) As the embezzlement of cash comes to the notice of company management only after approval of financial statements by board of directors of the company, then the treatment will be done as per the provisions of AS 5 "Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies" and the same will not be adjusted in the financial statements for the year ended 31st March, 2022. This being an extra-ordinary item should be disclosed in the statement of profit and loss as a part of loss for the year ending March, 2023, in a manner, that its impact on current profit or loss can be perceived.

Collection of cheques after balance sheet date is not an adjusting event even if the cheques bear the date of 31st March. Recognition of cheques in hand is therefore not consistent with requirements of AS 4. Moreover, the collection of cheques after balance sheet date does not represent any material change or commitments affecting financial position of the enterprise and no disclosure of such collections in the Directors' Report is necessary

Scanned with OKEN Scanner

29. AS 5 - "NET PROFIT OR LOSS FOR THE PERIOD, PRIOR PERIOD ITEMS & CHANGE IN ACCOUNTING POLICIES"

QUESTION 159:

(i) During the year 20X1-20X2, a medium size manufacturing company wrote down its inventories to net realisable value by ` 5,00,000. Is a separate disclosure necessary?

(ii) A company signed an agreement with the Employees Union on 1.9.20X2 for revision of wages with retrospective effect from 30.9.20X1. This would cost the company an additional liability of ` 5,00,000 per annum. Is a disclosure necessary for the amount paid in 20X2-X3?

ANSWER:

(i) Although the case under consideration does not relate to extraordinary item, but the nature and amount of such item may be relevant to users of financial statements in understanding the financial position and performance of an enterprise and in making projections about financial position and performance. AS 5 on 'Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies' states that:

"When items of income and expense within profit or loss from ordinary activities are of such size, nature or incidence that their disclosure is relevant to explain the performance of the enterprise for the period, the nature and amount of such items should be disclosed separately."

Circumstances which may require separate disclosure of items of income and expense in accordance with AS 5 include the write-down of inventories to net realisable value as well as the reversal of such write-downs.

(ii) It is given that revision of wages took place on 1st September, 20X2 with retrospective effect from 30.9.20X1. Therefore wages payable for the half year from 1.10.20X1 to 31.3.20X2 cannot be taken as an error or omission in the preparation of financial statements and hence this expenditure cannot be taken as a prior period item. Additional wages liability of ` 7,50,000 (for 1½ years @ ` 5,00,000 per annum) should be included in current year's wages.

It may be mentioned that additional wages is an expense arising from the ordinary activities of the company. Such an expense does not qualify as an extraordinary item. However, as per AS 5, when items of income and expense within profit or loss from ordinary activities are of such size, nature or incidence that their disclosure is relevant to explain the performance of the enterprise for the period, the nature and amount of such items should be disclosed separately.

QUESTION 160

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

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

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

ANSWER:

As per AS 5 'Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies', the adoption of an accounting policy for events or transactions that differ in substance from previously occurring events or transactions, will not be considered as a change in accounting policy.

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

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

Scanned with OKEN Scanner

QUESTION 161

In the current year, A Ltd. changed the depreciation method from the Straight Line Method (SLM) to Written Down Value (WDV) method. When A Ltd. recomputed depreciation retrospectively as per the new method, deficiency arose in depreciation in respect of past years. Therefore, it reduced the carrying amount of the asset by the amount of deficiency and such change in carrying amount (deficiency amount) has been debited to the statement of profit and loss as an extraordinary expense.

Whether the change in the carrying amount of assets due to the change in depreciation method should be treated as an extraordinary item?

Solution

As per AS 5, "Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies" extraordinary items are income or expenses that arise from events or transactions that are clearly distinct from the ordinary activities of the enterprise and, therefore, are not expected to recur frequently or regularly.

A change in the method of charging depreciation is not an event that is clearly distinct from the ordinary activities of the entity. In the instant case, A Ltd. has changed the depreciation method and treated the reduction in carrying amount (or amount of deficiency in depreciation) of the asset as an extraordinary expense. This is not correct. Such deficiency should be treated as a normal expense.

A change in the estimated useful life of a depreciable asset (i.e. change in depreciation method) affects the depreciation in the current period and in each period during the remaining useful life of the asset. In both cases, the effect of the change relating to the current period is recognised as income or expense in the current period. The effect, if any, on future periods, is recognised in future periods.

The change in depreciation method is considered as a change in accounting estimate as per the provisions of AS 5.

QUESTION 162:

A limited company created a provision for bad and doubtful debts at 2.5% on debtors in preparing the financial statements for the year 20X1-X2.

Subsequently on a review of the credit period allowed and financial capacity of customers, the company decided to increase the provision to 8% on debtors as on 31.3.20X2. The accounts of the company were not approved by the Board of Directors till the date of decision. While applying the relevant accounting standard can this revision be considered as an extraordinary item or Prior Period Item?

ANSWER:

As per para 21 of AS 5 'Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies', the preparation of financial statements involves making estimates which are based on the circumstances existing at the time when the financial statements are prepared. It may be necessary to revise an estimate in a subsequent period if there is a change in the circumstances on which the estimate was based. Revision of an estimate, by its nature, does not bring the adjustment within the definitions of a prior period item or an extraordinary item [para 21 of AS 5 (Revised) on Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies].

In the given case, a limited company created 2.5% provision for doubtful debts for the year 20X1-20X2. Subsequently in 20X2 the company revised the estimates based on the changed circumstances and wants to create 8% provision. As per AS-5 (Revised), this change in estimate is neither a prior period item nor an extraordinary item.

However, as per para 27 of AS 5 (Revised), a change in accounting estimate which has material effect in the current period, should be disclosed and quantified. Any change in the accounting estimate which is expected to have a material effect in later periods should also be disclosed and quantified.

QUESTION 163

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

Scanned with OKEN Scanner

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

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

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

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

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

SOLUTION

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

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

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

(iv) Adoption of a new accounting policy for events or transactions which did not occur previously should not be treated as a change in an accounting policy. Hence the introduction of new pension scheme is not a change in accounting policy.

(v) Change in cost formula used in measurement of cost of inventories is a change in accounting policy.

QUESTION 164

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

b. Management decided to pay pension to those employees who have retired after completing 5 years of service in the organisation. Such employees will get pension of Rs. 20,000 per month. Earlier there was no such scheme of pension in the organization. Explain whether this will constitute a change in accounting policy or not as per AS 5.

SOLUTION

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

(b) As per AS 5 'Net Profit or Loss for the Period, Prior Period Items and Changes in Accounting Policies', the adoption of an accounting policy for events or transactions that differ in substance from previously occurring events or transactions, will not be considered as a change in accounting policy. Accordingly, the adoption of a new accounting

Scanned with OKEN Scanner

policy of paying pension to retired employees is a policy for events or transactions which did not occur previously. Hence, it will not be treated as a change in an accounting policy.

QUESTION 165

State whether the following items are an example of Change in Accounting policy / Change in Accounting Estimates / Extra-Ordinary Items / Prior Period Items / Ordinary Activity.

i) Actual Bad Debts turning out to be more than provisions.

ii) Change from Cost model to Revaluation model for Measurement of carrying amount of PPE.

iii) Government grant receivable as compensation for expenses incurred in previous accounting period.

iv) Treating Operating Lease as Finance Lease.

v) Capitalisation of borrowing cost on working capital.

vi) Legislative changes having long-term retrospective application.

vii) Change in method of depreciation from straight line to WDV.

viii) Government grant becoming refundable.

ix) Applying 10% depreciation instead of 15% on furniture.

x) Change in useful life of fixed asset.

SOLUTION

Classification of given items is as follows:

Sr. No.	Particulars	Remarks
(i)	Actual bad debts turning out to be more than provisions	Change in Accounting Estimates
(ii)	Change from Cost model to Revaluation model for measurement of carrying amount of PPE	Change in Accounting Policy
(iii)	Government grant receivable as compensation for expenses incurred in previous accounting period	Item of Ordinary Activity
(iv)	Treating operating lease as finance lease.	Prior- period Items
(v)	Capitalisation of borrowing cost on working capital	Prior-period Items (as interest on working capital loans is not eligible for capitalization)
(vi)	Legislative changes having long term retrospective application	Ordinary Activity
(vii)	Change in the method of depreciation from straight line to WDV	Change in Accounting Estimates
(viii)	Government grant becoming refundable	Extra -ordinary Items
(ix)	Applying 10% depreciation instead of 15% on furniture	Prior- period Items
(x)	Change in useful life of fixed assets	Change in Accounting Estimates

Scanned with OKEN Scanner

30. AS 18 - RELATED PARTY DISCLOSURES

QUESTION 166:

Narmada Ltd. sold goods for Rs 90 lakhs to Ganga Ltd. during financial year ended 31-3-20X1. The Managing Director of Narmada Ltd. own 100% of Ganga Ltd. The sales were made to Ganga Ltd. at normal selling prices followed by Narmada Ltd. The Chief accountant of Narmada Ltd contends that these sales need not require a different treatment from the other sales made by the company and hence no disclosure is necessary as per the accounting standard. Is the Chief Accountant correct?

Solution

As per AS 18 'Related Party Disclosures', Enterprises over which a key management personnel is able to exercise significant influence are related parties. This includes enterprises owned by directors or major shareholders of the reporting enterprise and enterprise that have a member of key management in common with the reporting enterprise.

In the given case, Narmada Ltd. and Ganga Ltd are related parties and hence disclosure of transaction between them is required irrespective of whether the transaction was done at normal selling price.

Hence the contention of Chief Accountant of Narmada Ltd is wrong.

QUESTION 167:

X Ltd. sold goods to its associate Company for the 1st quarter ending 30.6.20X1. After that, the related party relationship ceased to exist. However, goods were supplied as was supplied to any other ordinary customer. Decide whether transactions of the entire year have to be disclosed as related party transaction.

Answer

As per AS 18, transactions of X Ltd. with its associate company for the first quarter ending 30.06.20X1 only are required to be disclosed as related party transactions. The transactions for the period in which related party relationship did not exist need not be reported.

QUESTION 168:

Arohi Ltd. sold goods for Rs. 90 lakhs to Anya Ltd. during financial year ended 31-3-20X1. The Managing Director of Arohi Ltd. own 100% of Anya Ltd. The sales were made to Anya Ltd. at normal selling prices followed by Arohi Ltd. The Chief accountant of Arohi Ltd contends that these sales need not require a different treatment from the other sales made by the company and hence no disclosure is necessary as per the accounting standard. Is the Chief Accountant correct? Comment in accordance with AS 18.

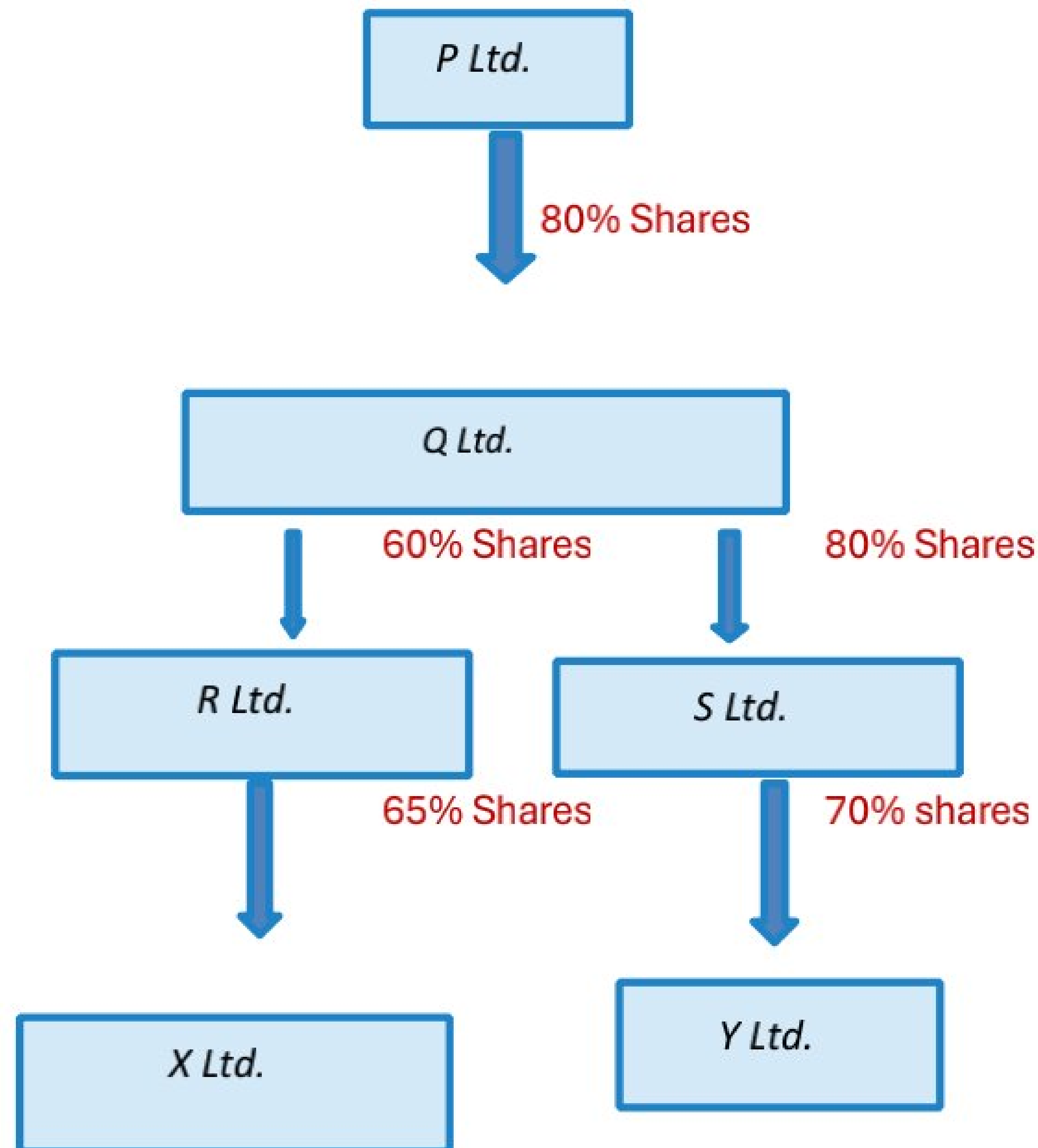
Solution:

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

Scanned with OKEN Scanner

QUESTION 169

Consider the following organization structure related to P Ltd.



Given the above structure: Identify related party relationships, if R Ltd. is the reporting enterprise

Solution

The following table identifies the related party relationships for R Ltd. (being the reporting enterprise):

Party Name	Relationship under AS-18
P Ltd.	♦ P Ltd. has indirect control on R Ltd. (through Q Ltd.) ♦ Hence R Ltd. is related to P Ltd.
Q Ltd.	♦ Q Ltd. has direct control of R Ltd. ♦ Hence R Ltd. is related to Q Ltd.
S Ltd.	♦ R Ltd. and S Ltd. are under common control of Q Ltd. ♦ Hence R Ltd. is related to S Ltd.
X Ltd.	♦ X Ltd. is controlled by R Ltd. ♦ Hence R Ltd. is related to X Ltd.
Y Ltd.	♦ Y Ltd. is the sub-subsidiary of Q Ltd. ♦ Both R Ltd. and Y Ltd. are under common control of Q Ltd. ♦ Hence R Ltd. is related to Y Ltd.

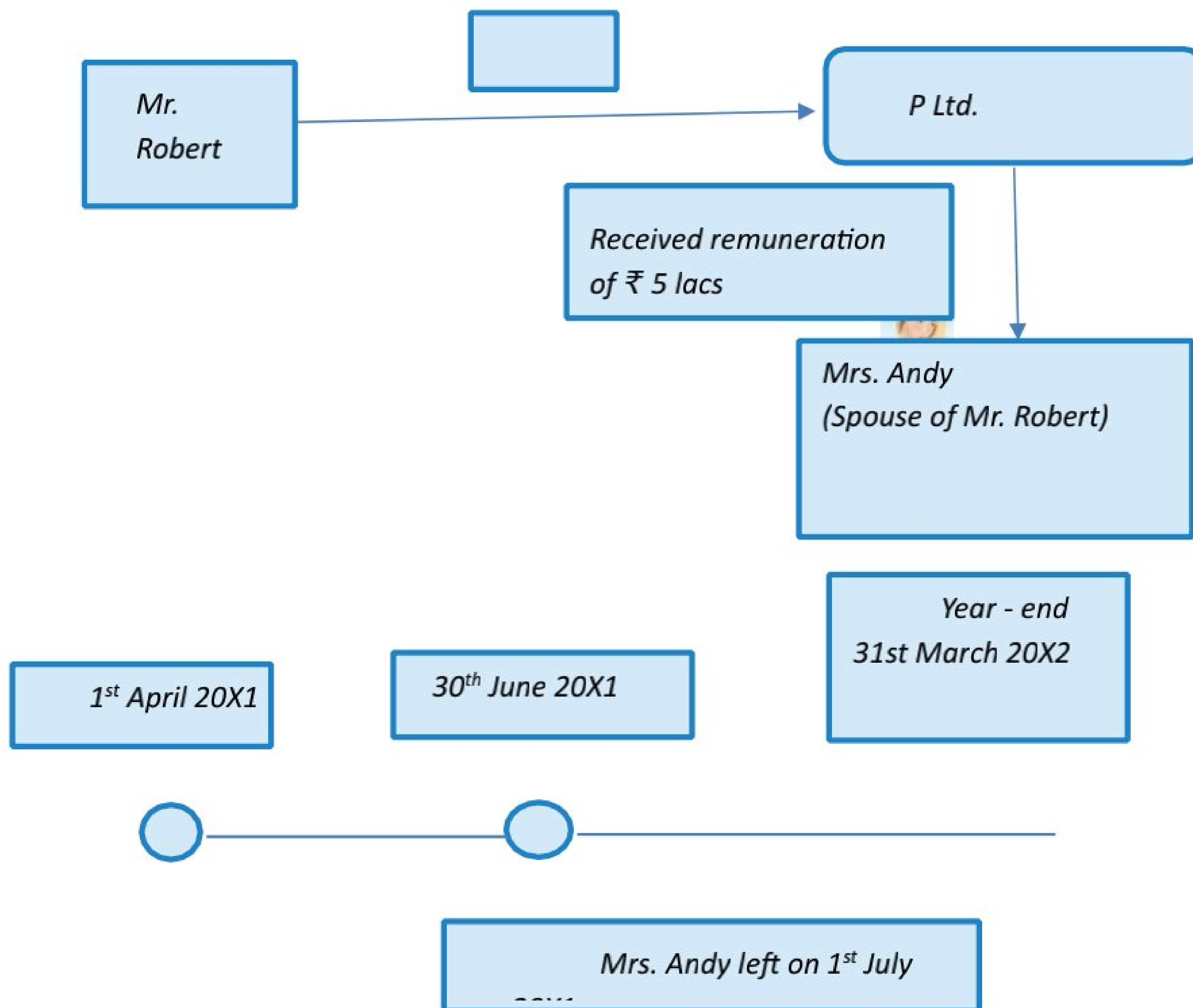
QUESTION 170

Consider a scenario wherein:

- Mr. Robert is a Managing Director of P Ltd.
- Andy (spouse of Robert) received a remuneration of Rs 5 lacs from P Ltd. – for the services she rendered to P Ltd. for the period 1st April 20X1 through 30th June 20X1
- Andy left the services of P Ltd. on 1st July 20X1

Scanned with OKEN Scanner

- Consider 31st March 20X2 as the year-end date for P Ltd.



Whether Andy is to be identified as related party at the year-end date (31st March 20X2) for the purposes of AS-18?

Solution

Yes – This is because as per AS-18, parties are considered to be related if at any time during the reporting period one party has the ability to control the other party or exercise significant influence over the other party in making financial and/or operating decisions.

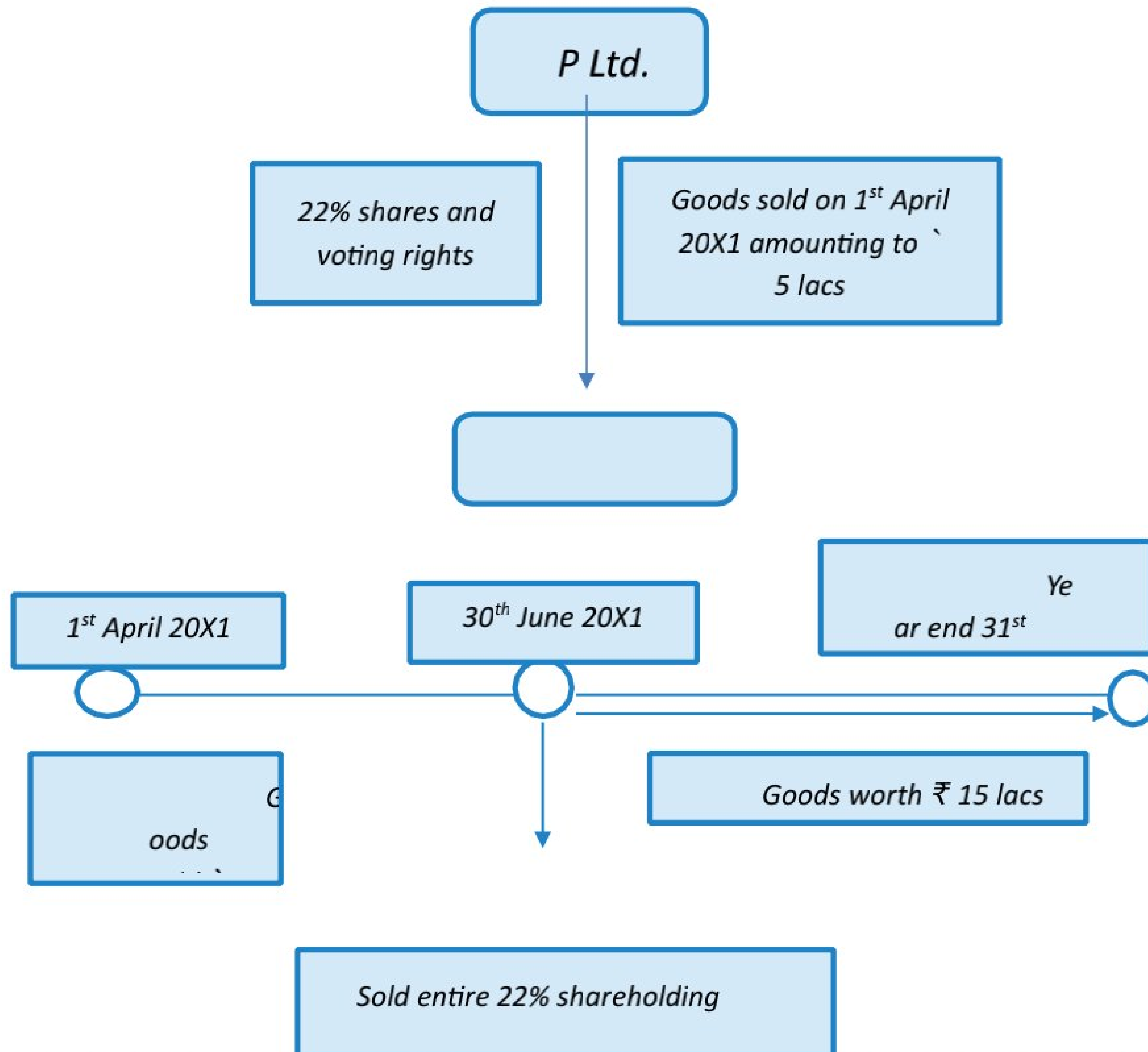
Hence Andy (being the spouse and relative of the KMP of P Ltd.) **needs to be reported** as related party at the year-end date (i.e., 31st March 20X2). This is because the remuneration Andy received from P Ltd. (for the period April 20X1 to 30 June 20X1) falls within the reporting year April 20X1 to March 20X2.

QUESTION 171

Consider a scenario wherein:

- P Ltd. hold 22% shares and voting rights in Q Ltd. (and hence Q Ltd. is an associate of P Ltd.)
- On 1st April 20X1, P Ltd. sold certain goods to Q Ltd. amounting to Rs. 5 lacs
- On 30th June 20X1, P Ltd. sold its entire 22% stake in Q Ltd. (and hence the related party relationship ceased to exist after 30th June 20X1)
- However, P Ltd. continued supply goods to Q Ltd. subsequent to 30th June 20X1 (just like any other customer) and sold goods worth Rs. 15 lacs during 9-month period ended 31st March 20X2
- Consider 31st March 20X2 as the year-end date for P Ltd.

Scanned with OKEN Scanner



Determine whether the transaction for the entire year (ending on 31st March 20X2) is required to be disclosed under AS-18 as related party transaction.

Solution

No – This is because as per AS-18, the disclosure requirements under the Standard relate only to the period **during related party relationship existed.**

Accordingly, only transactions between P Ltd and Q Ltd till 30th June 20X1 (being sale of goods worth Rs. 5 lacs) are required to be reported / disclosed under AS- 18.

Transactions entered into after 30th June 20X1 are **NOT required** to be disclosed under AS-18.

QUESTION 172

SP hotels Limited enters into an agreement with Mr. A for running its hotel for a fixed return payable to the later every year. The contract involves the day-to-day management of the hotel, while all financial and operating policy decisions are taken by the Board of Directors of the company. Mr. A does not own any voting power in SP Hotels Limited. Would he be considered as a related party of SP Hotels Limited"?

SOLUTION

Mr. A will not be considered as a related party of SP Hotels Limited in view of paragraph 3(c) of AS 18 which states, "individuals owning, directly or indirectly, an interest in the voting power of the reporting enterprise that gives them control or significant influence over the enterprise, and relatives of any such individual". In the above example, in the absence of share ownership, Mr. A would not be considered to exercise significant influence on SP Hotels Limited, even though there is an agreement giving him the power to manage the company. Further, the fact that Mr. A does not have the ability to direct or instruct the board of directors does not qualify him as a key management personnel.

Scanned with OKEN Scanner

QUESTION 173

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

1. Maya Ltd. holds 61 % shares of Sheetal Ltd.
   Sheetal Ltd. holds 51 % shares of Fair Ltd.
   Care Ltd. holds 49% shares of Fair Ltd.

(Give your answer - Reporting Entity wise for Maya Ltd., Sheetal Ltd., Care Ltd. and Fair Ltd.)

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

SOLUTION

(i)

(a) Reporting entity- Maya Ltd.

- Sheetal Ltd. (subsidiary) is a related party
- Fair Ltd.(subsidiary) is a related party

(b) Reporting entity- Sheetal Ltd.

- Maya Ltd. (holding company) is a related party
- Fair Ltd. (subsidiary) is a related party

(c) Reporting entity- Fair Ltd.

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

(d) Reporting entity- Care Ltd.

- Fair Ltd. (associate) is a related party

(ii)

Mr. Subhash Kumar is Key management personnel as he has the authority for planning, directing and controlling the activities of A Ltd. He also holds substantial interest in B Ltd. as he holds 72% capital of B Ltd. Thus, Mr. Subhash is related party for both A Ltd. and B Ltd. Moreover, as per the definition of related party relationship described in para 3 of AS 18, enterprises over which Subhash is able to exercise significant influence are also related parties. Thus, a Ltd. and B Ltd. will also be construed as related to each other.

QUESTION 174

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

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

SOLUTION

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

Scanned with OKEN Scanner

it could be clearly demonstrated otherwise. In the given example, Omega Bank Limited exercises significant influence over B Limited by virtue of ownership of 25 per cent of the voting power.
Omega Bank Limited is also a provider of finance for B Limited (as it has provided a loan to B Limited), and as per the standard, a provider of finance is deemed not to be a related party during its normal dealings with the enterprise by virtue only of those dealing. However, in this case, the exemption would not be available to Omega Bank Limited as the exercise of significant influence of Omega Bank Limited over B Limited has been demonstrated on account of ownership of more than 20 per cent of voting power. Accordingly, Omega Bank Limited would be construed to be a related party in the financial statements of B Limited and consequently, the latter would be required to disclose the transactions with Omega Bank Limited in its financial statements.

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

Scanned with OKEN Scanner

32. AS 29 - "PROVISIONS, CONTINGENT LIABILITIES AND CONTINGENT ASSETS"

QUESTION 177

At the end of the financial year ending on 31st March, 2022, a company finds that there are twenty law suits outstanding which have not been settled till the date of approval of accounts by the Board of Directors. The possible outcome as estimated by the Board is as follows:

particulars	probability	Loss (Rs.)
In respect of five cases (Win)	100%	-
Next ten cases (Win)	50%	-
Lose (Low damages)	40%	12,00,000
Lose (High damages)	10%	20,00,000
Remaining five cases		
Win	50%	-
Lose (Low damages)	30%	10,00,000
Lose (High damages)	20%	21,00,000

Outcome of each case is to be taken separate entity. Ascertain the amount of contingent loss and the accounting treatment in respect thereof as per AS – 29.

SOLUTION

According to AS 29 (Revised) 'Provisions, Contingent Liabilities and Contingent Assets', contingent liability should be disclosed in the financial statements if following conditions are satisfied:

(i) There is a present obligation arising out of past events but not recognized as provision.

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

(iii) The possibility of an outflow of resources embodying economic benefits is not remote.

(iv) The amount of the obligation cannot be measured with sufficient reliability to be recognized as provision.

In this case, the probability of winning of first five cases is 100% and hence, question of providing for contingent loss does not arise. The probability of winning of next ten cases is 50% and for remaining five cases is 50%. As per AS 29 (Revised), we make a provision if the loss is probable. As the loss does not appear to be probable and the possibility of an outflow of resources embodying economic benefits is remote, therefore disclosure by way of note should be made. For the purpose of the disclosure of contingent liability by way of note, amount may be calculated as under:

Expected loss in next ten cases = 40% of ₹ 12,00,000 + 10% of ₹ 20,00,000
= ₹ 4,80,000 + ₹ 2,00,000
= 6,80,000

Expected loss in remaining five cases = 30% of ₹ 10,00,000 + 20% of ₹ 21,00,000
= ₹ 3,00,000 + ₹ 4,20,000
= ₹ 7,20,000

To disclose contingent liability on the basis of maximum loss will be highly unrealistic. Therefore, the better approach will be to disclose the overall expected loss of 1,04,00,000 (₹ 6,80,000 x 10 + ₹ 7,20,000 x 5) as contingent liability.

QUESTION 178:

An engineering goods company provides after sales warranty for 2 years to its customers. Based on past experience, the company has the following policy for making provision for warranties on the invoice amount, on the remaining balance warranty period:

Less than 1 year: 2% provision

More than 1 year: 3% provision

The company has raised invoices as under:

Scanned with OKEN Scanner

Invoice Date	Amount
19th Jan, 20X1	40,000
29th Jan, 20X2	25,000
15th Oct, 20X2	90,000

Calculate the provision to be made for warranty under AS – 29 as at 31st March, 20X2 and 31st March, 20X3. Also compute the amount to be debited to Profit and Loss a/c for the year ended 31st March, 20X3.

(Answer: (i) 2012 – 1,550/-; 2013 – 3,200/- (ii) Amount debited to P&L - 1,650/-)

QUESTION 179

M/s. XYZ Ltd. is in a dispute with a competitor company. The dispute is regarding alleged infringement of Copyrights. The competitor has filed a suit in the court of law seeking damages of Rs 200 lakhs.
The Directors are of the view that the claim can be successfully resisted by the Company.
How would the matter be dealt in the annual accounts of the Company in the light of AS 29? You are required to explain in brief giving reasons for your answer.

ANSWER:

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

- An enterprise has a present obligation as a result of a past event;
- Tt is probable that an outflow of resources embodying economic benefits will be required to settle the obligation; and
- A reliable estimate can be made of the amount of the obligation.

If these conditions are not met, no provision should be recognized.
In the given situation, since, the directors of the company are of the opinion that the claim can be successfully resisted by the company; therefore there will be no outflow of the resources. Hence, no provision is required. The company will disclose the same as contingent liability by way of the following note: "Litigation is in process against the company relating to a dispute with a competitor who alleges that the company has infringed copyrights and is seeking damages of Rs 200 lakhs. However, the directors are of the opinion that the claim can be successfully resisted by the company."

QUESTION 180

The company has not made provision for warrantee in respect of certain goods considering that the company can claim the warranty cost from the original supplier.
You are required to **examine** in line with the provisions of AS 29.

ANSWER:

As per provisions of AS 29 "Provisions, Contingent Liabilities and Contingent Assets", where some or all of the expenditure required to settle a provision is expected to be reimbursed by another party, the reimbursement should be recognized when, and only when, it is virtually certain that reimbursement will be received if the enterprise settles the obligation. The reimbursement should be treated as a separate asset. The amount recognized for the reimbursement should not exceed the amount of the provision.
It is apparent from the question that the company had not made provision for warranty in respect of certain goods considering that the company can claim the warranty cost from the original supplier. However, the provision for warranty should have been made as per AS 29 and the amount claimable as reimbursement should be treated as a separate asset in the financial statements of the company rather than omitting the disclosure of such liability. Accordingly, it can be said that the accounting treatment adopted by the company with respect to warranty is not correct.

QUESTION 181

Chaos Limited is in the process of finalizing its accounts for the year ended 31st March, 2020. It seeks your advice in the following cases:

(i) Chaos Limited has filed a court case in 2014-2015 against its competitors. It became evident to its lawyers during the year ended 31st March, 2020 that Chaos Limited may lose the case and would have to pay Rs. 3,00,000 being

Scanned with OKEN Scanner

the cost of litigation. No entries/provisions have been made in the books.

(ii) A new regulation has been passed in 2019-2020 by the healthcare ministry to upgrade facilities. Deadline set by the government is 31.03.2021. The company estimates an expenditure of Rs. 10,00,000 for the said upgrade.

(iii) The company gives one year warranty for its healthcare equipment under the contract of sale that it will make good any manufacturing defect by repair or replacement. As per past experience, it is probable that there will be 1% such cases and estimated cost of repair / replacement is estimated at 10% of such sale value. During the year, the company has made a sale of Rs. 5 crores.

Kindly give your answer for each of above with proper reasoning according to the relevant Accounting Standard. Also state the principles for recognition of provision, as per AS 29.

SOLUTION

Principles for recognition of provisions: As per AS 29, "a provision shall be recognised when:

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

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

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

Accounting treatment under the given scenarios:

(i) On 31st March, 2020, since it is evident to the lawyer that Chaos Limited may lose the case and also a reliable estimate of the outflow can be made as Rs. 3,00,000, there is a present obligation. Hence, provision should be recognised for Rs. 3,00,000 for the amount which may be required to settle the obligation.

(ii) Under new regulation, an entity is required to upgrade its facilities by 31 st March, 2021. However, on 31st March, 2020, i.e. at the end of the reporting period, there is no obligation because there is no obligating event either for the costs of upgrading the facilities or for fines under the regulations. Hence, no provision should be recognized on 31st March, 2020 for upgrading the facilities by 31st March, 2021.

(iii) The obligating event is the sale of health care equipment with a warranty, which gives rise to a legal obligation. Here, an outflow of resources embodying economic benefits in settlement is probable for the warranties as a whole. Hence, a provision is recognized for the best estimate of the costs of making good under the warranty products sold before the end of the reporting period as follows:

Probability of warranty cases for the entity where repair/replacement may be required as per past experience

= 1% of Rs. 5,00,00,000 = Rs. 5,00,000

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

QUESTION 182

An airline is required by law to overhaul its aircraft once in every five years. The pacific Airlines which operate aircrafts does not provide any provision of as required by law in its final accounts. Discuss with reference to relevant Accounting Standard 29.

SOLUTION:

A provision should be recognized only when an enterprise has a present obligation arising from a past event or obligation. In the given case, there is no present obligation but a future one, therefore no provision is recognized as per AS 29.

The cost of overhauling aircraft is not recognized as a provision because it is a future obligation and the incurring of the expenditure depends on the company's decision to continue operating the aircrafts. Even a legal requirement to overhaul does not require the company to make a provision for the cost of overhaul because there is no present obligation to overhaul the aircrafts. Further, the enterprise can avoid the future expenditure by its future action, for example by selling the aircraft. However, an obligation might arise to pay fines or penalties under the legislation after completion of five years. Assessment of probability of incurring fines and penalties depends upon the provisions of the legislation and the stringency of the enforcement regime. A provision should be recognized for the best estimate of any fines and penalties if airline continues to operate aircrafts for more than five years.

Scanned with OKEN Scanner

QUESTION 183

Saharsh Ltd. is engaged in manufacturing of electric home appliances. The company is in the process of finalizing its accounts for the year ended 31.3.2020 and needs your expert advice on the following issues in line with the provisions of AS 29:

A case has been filed against the company in the consumer court and a notice for levy of a penalty of Rs. 20 lakhs has been received. The company has appointed a lawyer to defend the case for a fee of Rs. 2 lakhs. 50% of the fees has been paid and balance 50% will be paid after finalisation of the case. There are 75% chances that the penalty may not be levied.

The company had committed to supply a consignment worth Rs. 1 crore to one of its dealers by the year-end. As per the contract, if delivery is not made on time, a compensation of 15% is to be paid on the value of delayed/lost consignment. While the consignment was in transit, one of the trucks carrying goods worth Rs. 30 lakhs met with an accident. It was however covered by Insurance. According to the surveyor's report, the policy amount is collectable, subject to 10% deduction. Before closing the books of accounts, the company has received the information that the policy amount has been processed and the dealer has also claimed the compensation for the consignment of goods worth Rs. 30 lakhs which was in transit.

SOLUTION

(i) As per AS 29, an obligation is a present obligation if, based on the evidence available, its existence at the balance sheet date is considered probable, i.e., more likely than not.

Liability is a present obligation of the enterprise arising from past events, the settlement of which is expected to result in an outflow from the enterprise of resources embodying economic benefits.

In the given case, there are 75% chances that the penalty may not be levied. Accordingly, Saharsh Ltd. should not make the provision for penalty.

However, a provision should be made for remaining 50% fees of the lawyer in the financial statements of financial year 2019-2020.

(ii)

Loss due to accident	Rs. 30,00,000
Insurance claim receivable by company = Rs. 30,00,000 x 90%	Rs. 27,00,000
Loss to be recognised in the books for 2019-2020	Rs. 3,00,000
Insurance claim receivable to be recorded in the books	Rs. 27,00,000
Compensation claim by dealer against company to be provided for in the books = Rs. 30,00,000 x 15%	Rs. 4,50,000

Scanned with OKEN Scanner