CA-INTERMEDIATE

ADVANCED ACCOUNTING

GROUP-1

MODULE-1

NEW COURSE

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Dedicated to

BABA VISHAN PURI JI MAHARAJ

BABA LAKSHMAN PURI JI MAHARAJ

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ACCOUNTING STANDARD: 20
EARNING PER SHARE

UNIT I : BASIC EPS

CONCEPT 1: ADJUSTMENT OF NEW ISSUE & BUY BACK OF SHARES

QUESTION NO 1

Calculate the weighted average number of shares on the basis of following table:-

		No of shares issued	No of shares bought back	No of shares outstanding
1st January 99	Opening balance	1800	-	1800
31.5.99	Issue of shares for cash	600	-	2400
1.11.99	Buy back of shares		300	2100
31.12.99	Balance at the end of year			2100

QUESTION NO 2

Given below are the details of equity share capital of ABC Limited for the year 2001:

Particulars	No of shares in lacs	Face value: amount (₹ in lacs)
Balance if fully paid up equity as on 1.1.2001	100	1000
Convertible debentures converted into fully paid up equity shares on 1.7.2001	50	500
Equity shares bought back on 1.11.2001	30	300

Net profit after tax ₹ 240 Lacs.

QUESTION NO 3 (HOMEWORK)

For the year 2013-2014 Tuts Limited earns ₹ 3 Lakhs before tax. Other details are as follows:

Opening Equity Share Capital ₹ 500,000

5,000 Shares issued on 01.11.2013 (₹ 10/-)

ON 1.3.2014 1,000 Shares were buy backed.

Corporate Tax 33.33% Compute Basic EPS.

SOLUTION:

Basic EPS = Net Profit/WANES = 2,00,000/52,000 = ₹ 3.85

Net Profit = 3,00,000 – 1,00,000 = ₹ 2,00,000

WANES = 50000 + 5000 x 5/12 -1000 x 1/12 = 50000 + 2083.33 - 83.33 = 52,000

CONCEPT 2: ADJUSTMENT OF DIFFERENT FACE VALUES

QUESTION NO 4 (EQUAL DIVIDEND RIGHTS)

	No. of Shares
Of ₹10 each fully paid up	2,00,00,000
Of ₹25 each fully paid up	1,00,00,000
Of ₹5 each fully paid up	6,00,00,000

Compute the EPS if PAT is 15,00,00,000.

QUESTION NO 5 (DIFFERENT DIVIDEND RIGHTS)

No. of outstanding shares	
Of ₹10 each fully paid up- Class A	2,00,00,000
Of ₹25 each fully paid up- Class B	1,00,00,000
Of ₹5 each fully paid up – Class C	6,00,00,000
Profit after tax (₹ In lakhs)	15,00,00,000
Dividend %	
-Class A	Normal as declared
-Class B	1% above normal
-Class C	2% above normal

QUESTION NO 6

XYZ Limited has the following different classes of equity shares, outstanding as at March 31, 2002 having different face values as follows:

Number of shares	Rights as to share in net profit to the extent of capital
1,00,000 "A" class equity shares	**Proportionate to capital**
30,000 "B" class equity shares	In the proportion of 3:2 with respect to "A" class shares
30,000 "C" class equity shares	In the proportion of 5:2 with respect to "A" class share.
40,000 "D." class equity shares	In the proportion of 3:1 with respect to "A" class shares.

Profit for the year ended March 31, 2002 was ₹8,00,000. AS paragraph 8 of the statement requires an enterprise to present basic and diluted earnings per share on the face of the statement of Profit and Loss account for each class of equity shares that has a different right to share in the net profit for the period, the company calculates and discloses Basic EPS as follows:

The company believes that net profits is to be shared in the ratio of 2:3:5:6 as derived from their rights to share net profit.

Class	Calculations	Net profits	No of shares	Basic EPS
A	₹8,00,000*2/16	100,000	100,000	1.00
B	₹8,00,000*3/16	150,000	30,000	5.00
C	₹8,00,000*5/16	250,000	30,000	8.33
D.	₹8,00,000*6/16	300,000	40,000	7.50

Is the calculation of EPS by the company correct?

CONCEPT 3: ADJUSTMENT OF DIFFERENT PAID UP VALUES

QUESTION NO 7

Particulars	No.	Amount
Equity shares of ₹10 each fully paid up on 1.4.2000	10,00,000	99,00,000
Calls in arrears on 1.4.2000		1,00,000
Calls in arrears received on 1.6.2000		50,000
New issue amount paid up on 1.10.2000 ₹7.5	10,00,000	75,00,000
Calls in arrears received on 1.3.2001		50,000

PBIT before extraordinary items for the year ended on 31.3.200: ₹2,62,00,000, Extraordinary items(-) ₹2,00,000, Tax provision: ₹30,00,000. 10% preference share capital issued on 1.7.2000: ₹20,00,000.

QUESTION NO 8

		No of shares issued	Nominal value of shares	Amount paid
1st January 2001	Balance at beginning of year	1800	₹10	₹10
31st October 2001	Issue of shares	600	₹10	₹5

QUESTION NO 9

CD Limited makes a public issue of equity shares during the year ended March 31,2002 of 1,00,000 shares of ₹10 each. The issue was fully subscribed and the calls were made as given below:

₹5 on application and allotment made on July 1, 2001

₹2 on first call made on September 30, 2001

₹3 on second and final call made on January 1, 2002

Partly paid shares are entitled to participate in the dividend to the extent of amount paid. CD Limited had 5,00,000 shares outstanding at the beginning of the year and apart from the public issue of shares made above, there were no other additions to or reductions from share capital.

CONCEPT 4: ADJUSTMENT OF BONUS SHARES

QUESTION NO 10

Net profit for the year 2000	₹18,00,000
Net profit for the year 2001	₹60,00,000
No of equity shares outstanding until 30.9.2001	20,00,000
Bonus issue 1.10.2001	2 equity shares for each equity share outstanding at 30.9.2001

QUESTION NO 11

Given below equity shares capital details of XYZ Limited for the year 2000 and 2001:

Details	No of shares	Amount
Equity shares of ₹10 each fully paid up on 1.6.2000	10,00,000	1,00,00,000
Bonus issue on 1.6.2001	10,00,000	1,00,00,000

Net profit 2000 - ₹ 45,00,000, Net profit 2001 - ₹ 60,00,000.

QUESTION NO 12

As a statutory auditor for the year ended 31.3.2002 how would you deal with the following: As on 31.3.2001 the equity share capital of Q Ltd. is ₹10crores divided into shares of ₹10 each. During the financial year 2001-2002, it has issued bonus shares in the ratio of 1:1. The net profit after tax for the years 31.3.2001 and 31.3.2002 is ₹8.50crores and ₹11.50crores respectively. The EPS disclosed in the accounts for two years is ₹8.50 and 5.75 respectively.

QUESTION NO 13 (HW)

Financial information of X Limited is extracted s follows:

Opening Equity Shares on 01.01.2006	1, 00,000
Shares issued as Bonus as on 01.05.2006	20,000
Profits for the year ended 31.12.2006	(₹) 40, 00,000
Profits for the year ended 31.12.2.005	(₹) 55, 00,000

Calculate Basic EPS for 2006 and adjusted EPS for 2005.

SOLUTION:

Basic EPS 2006 (Reported) = Net Profit/WANES = 40, 00,000/1, 20,000 = ₹ 33.33

Basic EPS 2005 (Reported) = 55, 00,000/1, 00,000 = ₹ 55

Basic EPS 2005 (Restated) = 55, 00,000/1, 20,000 = ₹45.83

Assume Opening shares are numbers.

Note: One should compare Restated EPs with Reported EPS i.e. ₹44.83 with ₹ 33.33

CONCEPT 5: ADJUSTMENT OF RIGHT SHARES

QUESTION NO 14

Accounting Year is Calendar year

Net profit	Year 2000: ₹11,00,000 Year 2001: ₹15,00,000
No of shares outstanding prior to right issue	5,00,000 shares
Right issue	One new share for each five outstanding (i.e., 1,00,000 new shares) Right issue price: ₹15 last date to exercise rights: 1st March 2001
Fair value of one equity share immediately prior to exercise of rights on 1st March 2001	₹21

QUESTION NO 15

Given below are the details of equity shares of MN Limited during 2000 and 2001:

Details	No of shares (in lacs)	Amount (₹ in lacs)
Equity shares fully paid up on 1.1.2000	1,000	10,000
Right issue on 1.7.2001	1,000	2,000

- Closing market price on 30.6.2001 : ₹ 35
- Price of right : ₹ 20
- Net profit after tax (₹ in lacs) for the year ended 31.12.2000 :2200
- Reported basic EPS for the year ended 31.12.2000 : ₹ 2.20
- Net profit after tax (₹in lacs) for the year ended 31.12.2001 :2400

QUESTION NO 16

X Ltd. supplied the following information. You are required to compute the Basic EPS. (Accounting year 1.1.2002-31.12.2002)

Net profit for the accounting years 2002 and 2003: ₹ 20,00,000 and 30,00,000

No of shares outstanding prior to Right issue 10,00,000 shares

Right issue= one new share for each four shares outstanding (that is 2,50,000)

Term right issue Price = ₹ 20; last date for exercise of rights is 31.3.2003

Fair rate of one equity share immediately prior to exercise of right on 31.03.2003 ₹25

QUESTION NO 17 (HW)

Platinum Ltd. had 1200,000 equity shares of ₹ 10 each fully paid up outstanding prior to right issue. The details of rights issues are as follows:

(k) One new share for every two shares outstanding.

(l) Right issue price – ₹ 18

(m) Last date of exercise rights to 31st December, 2010

(n) Fair value of each equity share prior to exercise of rights – ₹ 24

The details of net profit earned by the company as follows:

Year ended 31.3.2010	₹ 40,00,000
Year ended 31.3.2011	₹ 54,00,000

Calculate EPS.

SOLUTION: For 2011 – ₹ 3,77, EPS for 2010 – ₹ 3.33, adjusted EPS for 2010- ₹ 3.05

QUESTION NO 18 (HW)

As on 01.01.2006 Pistons Limited had 5,00,000 shares. It issued 1 right share for every 5 shares held at Rs 15/- on 01.03.2006. Market price per share just before the right issue is ₹ 21. Net profit for 2005 was ₹ 11,00,000 and for 2006 ₹ 15,00, 000.

Calculate EPS for 2006 and restated EPS for 2005.

SOLUTION:

$$\text{Theoretical Ex-right MP} = \frac{\text{OS x MP + RI x Subscription Price}}{\text{Total Shares}}$$

$$= \frac{5,00,000 \times 21 + 1,00,000 \times 15}{6,00,000} = \text{Rs } 20$$

Irrespective of any method Theoretical Ex-right MP is required to be calculated as a first step.

Formula Method:

WANES = 5,00,000 +Right Shares x 9/12 x Adjusting Factor (A.F.)

= 5,00,000 + 1,00,000 x 10/12 x 1.05 = 500000+87500

Calculation of A.F.:

Adjusting Factor = MP before rights = 21/20 = 1.05

MP ex-right

Basic EPS 2006 (Reported) = Net Profit/WANES = 15,00,000/(5,00,000+87500) = ₹2.55

Basic EPS 2005 (Reported) = 1100,000/5,00,000 = ₹ 2.20

Basic EPS 2005 (Restated) = 1100000/500000 x 1.05 = ₹ 2.10

QUESTION NO 19 (HW)

Calculate from the following information:

- Theoretical ex-right fair value.
- Right Factor:
  - — Number of equity shares outstanding 5 Lakhs.
  - — Right issue 2 shares for each 5 shares
  - — Fair value per share before right ₹ 34.00

— Right issue price Rs 20.00

Ans. ₹ 30; ₹ 1.13

CONCEPT 6: ADJUSTMENT OF SHARES ISSUED IN AMALGAMATION OF COMPANIES

QUESTION NO 20

Given below information relating to equity shares of A Limited and B Limited. Two companies amalgamated w.e.f. 1-10-2001. A Limited issued the required No. of shares on the basis of the agreed valuation.

	A Limited	B Limited
No of outstanding equity shares as on 1.4.2001		
(No. in lakhs)	500	200
Agreed value per share for acquisition	120	30
Date of acquisition 1-10-2001		
Profit after tax (₹ In lakhs)	1200	350

Profit after tax during 1-10-2001—31-3-2001 (₹ In lakhs) 1500

QUESTION NO 21

On June 30, 2001, B Limited merged into A Limited. The Amalgamation was accounted for in accordance with the pooling interest method described in Accounting Standard 14 on “accounting for Amalgamation”.

The following is the relevant information for the year ended 31st March 2002:

Particulars	A Limited	B Limited
Net profit (₹)		
Until merger	5,00,000	2,00,000
After merger to year end	8,00,000	
(March 31, 2002)		
Number of shares (₹10 each)		
At the start of the year	6,000	4,000
On the date of merger	6,000	4,000
At year end (March 31, 2002)	10,000	

Compute the E.P.S of A Limited at the year end, i.e., March 31, 2002

QUESTION 22 (HW)

Max Ltd. takes over Zee Ltd. as on 01.04.2005.

	Max Ltd.	Zee Ltd.
Original Shares	200,000	1,00,000
Face Value	100	100
Share Value for P.C.	210	105
Profits (01.01.2005 – 31.03.2005)	1,00,000	70,000
Profits (01.04.2005 – 31.12.2005)	4,30,000	--

Compute EPS assuming:

(a) Amalgamation in the nature of Purchase

(b) Amalgamation in the nature of Merger

SOLUTION:

Calculation of PC = 100000 x 105 = 1,05,00,000

Number of shares issued = 10500000/210 = 50,000

Amalgamation in the nature of Purchase	Amalgamation in the nature of Merger
Net Profit = 530000	Net Profit = 600000
WANES = 237500 (200000 + 50000x9/12)	WANES=250000 (2000000+50000)
Basic EPS = ₹ 2.23	Basic EPS= ₹ 2.40

UNIT II : DILUTED EPS

CONCEPT 1 : ADJUSTMENT OF SINGLE POTENTIAL SHARE

QUESTION NO 23

Net profit for the year	₹1,00,00,000
No. of equity shares outstanding	50,00,000
Basic earnings per share	₹2.00
No. of 12% convertible debentures of ₹100 each	1,00,000
Each debenture is convertible in to 10 equity shares	
Interest expense for the current year	₹12,00,000
Tax relating to the interest expense	3,60,000

QUESTION NO 24

Net profit for the year 2001	₹12,00,000
Weighted average number of equity shares outstanding during the 2001	5,00,000
Average fair value of one equity share during the year 2001	₹20
Weighted average number of shares under option during the year 2001	1,00,000
Exercise price for shares under option during the year 2001	₹15

QUESTION 25 (C.A.FINAL NOV. 2006)

(Similar Problem Nov. 2009) (NS)

Mohur Limited has equity capital of ₹ 40,00,000 consisting of fully paid up shares of ₹ 10 each. Net Profit after tax for 2004-2005 was ₹/ 60,00,000. It has also issued 36,000. 10% Convertible Debentures of ₹ 50 each. Each debenture is convertible into 5 equity shares. Tax rate 30%. Compute diluted EPS.

SOLUTIONS:

1. Basic EPS = $\frac{\text{PAT}}{\text{No. of Share}} = \frac{6000000}{400000}$ x 15

2. Diluted EPS = $\frac{\text{PAT}}{\text{New No. of Share}} = \frac{6126000}{580000}$ x 10.56

Note – Adjust PAT

Net Profit before conv. debenture in to share =	60,00,000
Interest saving on debenture	
(36000*50*10%*70%(100-30) =	1,26,000
Adj. PAT	61,26,000
New No. share for dilution:	
Old Shares =	4,00,000
Convertible debentures (36000*5) =	1,80,000
	5,80,000

CONCEPT 2 : ADJUSTMENT OF MULTIPLE POTENTIAL SHARES

QUESTION NO 26

Net profits attributable to equity shareholders	₹1,00,00,000
No of equity shares outstanding	20,00,000
Average fair value of the one equity share during the year	₹75
Potential equity shares:	
Options	1,00,000 with exercise price of 60
Convertible preference shares	8,00,000 shares entitled to a cumulative dividend of ₹ 8 per share, each preference share is convertible into 2 equity shares.
12% convertible debentures of ₹100 each	Nominal amount ₹ 10,00,00,00. each debenture is convertible into 4 equity shares.
tax rate	30%.

QUESTION NO 27

Particulars	No. in lacs	Amount in lacs.
Equity shares outstanding on 1.1.2001	1,000	10,000
10% convertible each to converted into 8 equity shares	200	20,000
Net profits after tax		1,000
Basic EPS(₹)	=1000/1000	1

Assume tax rate is 38.5%.

UNIT 3 : MISC. CONCEPTS

QUESTION NO 28 (DILUTED EPS FOR LOSS MAKING COMPANY)

How would Diluted EPS be calculated for a loss making enterprise? To illustrate, at December 31, 20X2, a company has 2,000 shares of face value of ₹10 each. The stock options outstanding at December 31,20X2 were for 400 shares of face value ₹10 each. The net loss for the year 20X2 was ₹1,200,000. The fair value of the shares on the date of grant and the exercise price were ₹100 and ₹60 per share, respectively.

QUESTION NO 29 (SHARE SPLIT/SHARE CONSOLIDATION)

COSY COMFORTS Limited earns a Net Profit for the year 2006-2007 ₹ 20, 00,000 after tax. The corresponding figure for the last year was ₹ 16,00,000. Its Capital Structure contains 80,000 Shares of ₹ 10 each. On 07.11.2006 it has decided to consolidate the shares from ₹ 10 each to ₹ 100 each. Calculate Basic EPS and Restated EPS.

SOLUTION:

Basic EPS 2006-07 (Reported) = Net Profit/WANES = 20,00,000/8,000 = ₹250

Basic EPS 2005-06 (Reported) = 1600000/80000 = ₹ 20

Basic EPS 2005-06 (Restated) = 1600000/8000 = ₹ 200

QUESTION NO 30 (DISCONTINUED OPERATIONS)

Undivided Ltd. having a net profit of ₹40,000 from continuing operations and net loss of ₹ 30,000 from discontinuing operations. The company has 20,000 equity shares and 500 Potential equity shares.

Compute Basic EPS & Dilutive EPS of Undivided Ltd.

SOLUTION:

Profit/Loss position is as follows:

Net Profit from continuing operations	40,000
Net Loss from discontinuing operations	(30,000)
Net Profit to the company as a whole	10,000

Retail Potential Equity Shares are considered dilutive only when their conversion would lead to decrease in net profit per share from 'continuing operations'.

For checking purpose whether the PES are dilutive/anti-dilutive consider results of continuing operations only. In other words results from dis-continuing operations is to be ignored.

But for the final reporting purpose consider both Continuing as well as Discontinuing operations for computing Basic as well as Dilutive EPS.

Therefore, for dilutive EPS profits of ₹ 40,000 is the control figure which is from continuing operations.

Accordingly 500 Potential equity shares are dilutive as it decreases the net profit per share from 'continuing ordinary operations' from ₹ 2.00 to ₹ 1.95.

Reporting and Disclosures:

Basic EPS = (10,000/20,000) = 0.50

Dilutive EPS = (10,000/20,500) = 0.49

UNIT 4: PAST EXAMINATION QUESTIONS

QUESTION 31 (NOV 2019:5 MARKS)

Following information is supplied by K Ltd.:

Number of shares outstanding prior to right issue - 2,50,000 shares.

Right issue - two new share for each 5 outstanding shares (i.e. 1,00,000 new shares) Right issue price - ₹ 98

Last date of exercising rights - 30-06-2018.

Fair value of one equity share immediately prior to exercise of right on 30-06-2018 is ₹ 102.

Net Profit to equity shareholders:

2017-2018 - ₹ 50,00,000

2018-2019 - ₹ 75,00,000

You are required to calculate the basic earnings per share as per AS-20 Earnings per Share.

SOLUTION:

$$\frac{\text{Fair value of shares immediately prior to exercise of rights} + \text{Total amount received from exercise}}{\text{Number of shares outstanding prior to exercise} + \text{Number of shares issued in the exercise}}$$

$$= \frac{102 \times 2{,}50{,}000 \text{ Shares} + ₹\ 98 \times 1{,}00{,}000 \text{ shares}}{3{,}50{,}000 \text{ shares}}$$

Theoretical ex-rights fair value per share = ₹ 100.86

Computation of adjustment factor:

$$\frac{\text{Fair value per share prior to exercise of rights}}{\text{Theoretical ex - rights value per share}} = \frac{102}{100.86} = 1.01$$

Computation of earnings per share:

EPS for the year 2017-18 as originally reported: ₹ 50,00,000/2,50,000 shares = ₹ 20

EPS for the year 2017-18 restated for rights issue:

=₹ 50,00,000/ (2,50,000 shares x 1.01)

= ₹ 19.80

EPS for the year 2018-19 including effects of rights issue:

EPS = 75,00,000/3,25,625* = ₹ 23.03

*[(2,50,000 x 1.01 x 3/12) + (3,50,000 x 9/12)] =63,125 + 2,62,500 = 3,25,625 shares

Note: Financial year (ended 31st March) is considered as accounting year while giving the above SOLUTION.

QUESTION 32 (NOV 2018 :5 MARKS)

From the following information given by Sampark Ltd., Calculate Basis EPS and Diluted EPS as per AS 20 :

	₹
Net Profit for the current year	2,50,00,000
No. of Equity Shares Outstanding	50,00,000
No. of 12% convertible debentures of ₹100 each	50,000
Each debenture is convertible into 8 Equity Shares	
Interest expense for the current year	6,00,000
Tax saving relating to interest expense (30%)	1,80,000

SOLUTION :

Calculation of Basic Earning Per Share

$$\textbf{Basic EPS} = \frac{\text{Net Profit for the current year}}{\text{No. of Equity Shares}}$$

$$= \frac{2,50,00,000}{50,00,000}$$

Basic EPS = ₹ 5

Calculation of Diluted Earning Per Share

$$\textbf{Diluted EPS} = \frac{\text{Adjusted net profit for the current year}}{\text{Weighted average no. of Equity Shares}}$$

	₹
Adjusted net profit for the current year	2,50,00,000
Net profit for the current year	6,00,000

Add: Interest expenses for the current year	(1,80,000)
Less: Tax saving relating to Tax Expenses	2,54,20,000

No. of equity shares resulting from conversion of debentures: 4,00,000 Shares

Weighted average no. of equity shares used to compute diluted EPS:

(50,00,000 + 4,00,000) = 54,00,000 Equity Shares

Diluted earnings per share: (2,54,20,000/54,00,000) = ₹ 4.71 (Approx.)

QUESETION 33 (CA INTER DEC. 2021 EXAMS : 5 MARKS)

"At the time calculating diluted earnings per share, effect is given to all dilutive potential equity shares that are outstanding during the period". Comment and also calculate the basic and diluted earnings per share for the year 2020-21 from the following information:

(i)	Net profit after tax for the year	₹ 64,12,500
(ii)	No. of equity shares outstanding	15,00,000
(iii)	No. of 9% convertible debentures of ₹ 100 issued on 1st July,2020	75,000
(iv)	Each debenture is convertible into 8 Equity Shares	
(v)	Tax relating to interest expenses	35%

SOLUTION :

In calculating diluted earnings per share, effect is given to all dilutive potential equity shares that were outstanding during the period." As per AS 20 'Earnings per Share', the net profit or loss for the period attributable to equity shareholders and the weighted average number of shares outstanding* during the period should be adjusted for the effects of all dilutive potential equity shares for the purpose of calculation of diluted earnings per share.

Basic EPS for the year 2020-21= 64,12,500/15,00,000 = ₹ 4.275 or ₹ 4.28

Computation of diluted earnings per share for year 2020-21

$$\frac{\text{(Adjusted net profit for the current year)}}{\text{(Weighted average number of equity shares)}}$$

Adjusted net profit for the current year will be (64,12,500 + 5,06,250 – 1,77,188) = ₹ 67,41,562

No. of equity shares resulting from conversion of debentures:

6,00,000 Shares (75,000 × 8)

Weighted average no. of equity shares used to compute diluted EPS: (15,00,000 X12/12+ 6,00,000X9/12)

= 19,50,000 Shares

Diluted earnings per share: (67,41,562/19,50,000) = ₹ 3.46

Working Note:

Interest expense for 9 months = 75,00,000×9%×9/12 =₹ 5,06,250

Tax expense 35 % on interest is ₹1,77,188 (5,06,250 x 35%)

QUESTION 34 (CA INTER MAY 2022 EXAMS : 5 MARKS)

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

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

During the year 2021-2022, the company had profit after tax of ₹ 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 ₹ 1 each at their full market price of ₹ 7.60 per share.

NAT's shares were trading at ₹ 8.05 per share on 31st March,2022.

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

= ₹ 62.30 x 10,00,000 equity shares

= ₹ 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

= ₹ 6,23,00,000 / (10,00,000+ 5,00,000)

= ₹ 6,23,00,000 / 15,00,000

= ₹ 41.53 per share

(c) 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)

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

= ₹ 82,00,000 / 15,50,000 shares

= ₹ 5.29 per share

(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 35 (CA INTER NOV. 2022 EXAMS : 5 MARKS)

The following information is provided to you:

Net profit for the year 2022	₹ 72,00,000
Weighted average number of equity shares outstanding during the year 2022:	30,00,000 shares
Average Fair value of one equity share during the year 2022:	₹ 25.00
Weighted average number of shares under option during the year 2022:	6,00,000 shares
Exercise price for shares under option during the year 2022:	₹ 20.00

You are required to compute Basic and Diluted Earnings Per Share as per AS 20.

SOLUTION :

Computation of Basic earnings per share

	Earnings ₹	Shares	Earnings/ Share ₹
Net profit for the year 2022	72,00,000		
Weighted average no. of shares during year 2022		30,00,000	
Basic earnings per share (72,00,000/30,00,000)			2.40

Computation of Diluted earnings per share

	Earnings	Shares	Earnings/Share
	₹		₹
Net profit for the year 2022	72,00,000		
Weighted average no. of shares during year 2022		30,00,000	
Number of shares under option		6,00,000	
Number of shares that would have been issued at fair value (6,00,000 x 20.00)/25.00		(4,80,000)	
Diluted earnings per share	72,00,000	31,20,000	2.31
			(rounded-off)

Note: The earnings have not been increased as the total number of shares has been increased only by the number of shares (1,20,000) deemed for the purpose of the computation to have been issued for no consideration.

To the extent that partly paid shares are not entitled to participate in dividends during the reporting period they are considered the equivalent of options.

AS 20 (EPS)

EXTRA QUESTIONS FOR SELF STUDY

QUESTION 1

The following information relates to M/s. XYZ Limited for the year ended 31st March, 2017:

Net Profit for the year after tax: ₹ 75,00,000

Number of Equity Shares of ₹ 10 each outstanding: ₹ 10,00,000

Convertible Debentures Issued by the Company (at the beginning of the year)

Particulars	Nos.
8% Convertible Debentures of ₹ 100 each	1,00,000
Equity Shares to be issued on conversion	1,10,000

The Rate of Income Tax: 30%.

You are required to calculate Basic and Diluted Earnings Per Share (EPS)

SOLUTION

Computation of basic earnings per share

Net profit for the current year / Weighted average number of equity shares outstanding during the year

₹ 75,00,000 / 10,00,000 = ₹ 7.50 per share

$$\text{Computation of diluted earnings per share} = \frac{\text{Adjusted net profit for the current year}}{\text{Weighted average number of equity shares}}$$

Adjusted net profit for the current year

	₹
Net profit for the current year	75,00,000
Add: Interest expense for the current year	8,00,000
Less: Tax relating to interest expense (30% of ₹ 8,00,000)	(2,40,000)
Adjusted net profit for the current year	80,60,000

Number of equity shares resulting from conversion of debentures

= 1,10,000 Equity shares (given in the question)

Weighted average number of equity shares used to compute diluted earnings per share

= 11,10,000 shares (10,00,000 + 1,10,000)

Diluted earnings per share

= 80,60,000/ 11,10,000 = ₹ 7.26 per share

Note: Conversion of convertible debentures into Equity Share will be dilutive potential equity shares. Hence, to compute the adjusted profit the interest paid on such debentures will be added back as the same would not be payable in case these are converted into equity shares.

QUESTION 2

A-One Limited supplied the following information. You are required to compute the basic earnings per share as per AS 20 'Earnings per Share':

Net profit attributable to equity shareholders	Year 2017-18:	₹ 1,00,00,000
	Year 2018-19:	₹ 1,50,00,000

Number of shares outstanding prior to

Right Issue	50,00,000 shares
Right Issue	One new share for each four outstanding shares i.e., 12,50,000 shares Right Issue Price - ₹ 96 Last date of exercising rights - 30-06-2018
Fair value of one equity share immediately prior to exercise of rights on 30-06-2018	₹ 101

SOLUTION

Computation of Basic earnings per share

	2017-18 ₹	2018-19 ₹
EPS for the year 2017-18 as originally reported: (₹ 1,00,00,000 / 50,00,000 shares)	2.00	
EPS for the year 2017-18 restated for rights issue: ₹1,00,00,000 / (50,00,000 shares x 1.01)*	1.98	
EPS for the year 2018-19 including effects of rights issue $\frac{₹\ 1,50,00,000}{(50,00,000 \times 1.01 \times 3/12) + (62,50,000 \times 9/12)}$		2.52

* Computation of Basic Earnings per share in case of Rights Issue requires computation of adjustment factor which is given as working note.

Working Notes:

1. **Computation of theoretical ex-rights fair value per share**

$$= \frac{\text{Fair value of all outstanding shares immediately prior to exercise of rights+total amount received from exercise}}{\text{Number of shares outstanding prior to exercise + Number of shares issued in the exercise}}$$

$$= \frac{(₹\ 101 \times 50,00,000 \text{ shares}) + (₹\ 96 \times 12,50,000 \text{ shares})}{50,00,000 \text{ shares} + 12,50,000 \text{ shares}}$$

= ₹ 62,50,00,000 / 62,50,000 = ₹100

Therefore, theoretical ex-rights fair value per share is = ₹ 100

2. **Computation of adjustment factor**

$$= \frac{\text{Fair value per share prior to exercise of rights}}{\text{Theoretical ex-rights value per share}}$$

$$= \frac{₹\ (101)}{₹\ (100)} = 1.01$$

QUESTION 3

AB Limited is a company engaged in manufacturing industrial packaging equipment. As per the terms of an agreement entered with its debenture holders, the company is required to appropriate adequate portion of its profits to a specific reserve over the period of maturity of the debentures such that, at the redemption date, the reserve constitutes at least half the value of such debentures. As such appropriations are not available for distribution to the equity shareholders, AB Limited has excluded this from the numerator in the computation of Basic EPS. Is this treatment correct as per provisions of AS 20?

SOLUTION

The appropriation made to such a mandatory reserve created for the redemption of debentures would be included in the net profit attributable to equity shareholders for the computation of Basic EPS. AS 20 states that "For the purpose of calculating basic earnings per share, the net profit or loss for the period attributable to equity shareholders should be the net profit or loss for the period after deducting preference dividends and any attributable tax thereto for the period". With an emphasis on the phrase attributable to equity shareholders, it may be construed that such amounts appropriated to mandatory reserves, though not available for distribution as dividend, are still attributable to equity shareholders. Accordingly, these amounts should be included in the computation of Basic EPS. In view of this, the treatment made by the company is not correct.

QUESTION 4

(a) Stock options have been granted by AB Limited to its employees and they vest equally over 5 years, i.e., 20 per cent at the end of each year from the date of grant. The options will vest only if the employee is still employed with the company at the end of the year. If the employee leaves the company during the vesting period, the options that have vested can be exercised, while the others would lapse. Currently, AB Limited includes only the vested options for calculating Diluted EPS. Should only completely vested options be included for computation of Diluted EPS? Is this in accordance with the provisions of AS 20? Explain.

(b) X Limited, as at March 31, 2021, has income from continuing ordinary operations of ₹ 2,40,000, a loss from discontinuing operations of ₹ 3,60,000 and accordingly a net loss of ₹ 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

(a) The current method of calculating Diluted EPS adopted by AB limited is not in accordance with AS 20. The calculation of Diluted EPS should include all potential equity shares, i.e., all the stock options granted at the balance sheet date, which are dilutive in nature, irrespective of the vesting pattern. The options that have lapsed during the year should be included for the portion of the period the same were outstanding, pursuant to the requirement of the standard.

AS 20 states that "A potential equity share is a financial instrument or other contract that entitles, or may entitle, its holder to equity shares". Options including employee stock option plans under which employees of an enterprise are entitled to receive equity shares as part of their remuneration and other similar plans are examples of potential equity shares. Further, for the purpose of calculating diluted earnings per share, the net profit or loss for the period attributable to equity shareholders and the weighted average number of shares outstanding during the period should be adjusted for the effects of all dilutive potential equity shares.

(b) As per AS 20 "Potential equity shares should be treated as dilutive when, and only when, their conversion to equity shares would decrease net profit per share from continuing ordinary operations". As income from continuing ordinary operations, ₹ 2,40,000 would be considered and not ₹ (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 ₹ 240 to ₹ 200. Thus the basic E.P.S would be ₹ (120) and diluted E.P.S. would be ₹ (100).

QUESTION 5

The following information relates to XYZ Limited for the year ended 31st March, 2022:

Net Profit for the year after tax:	₹ 37,50,000
Number of Equity Shares of ₹ 10 each outstanding:	₹ 5,00,000

Convertible Debentures Issued by the Company (at the beginning of the year)

Particulars	Nos.
8% Convertible Debentures of ₹ 100 each	50,000
Equity Shares to be issued on conversion	55,000

The Rate of Income Tax: 30%.

You are required to calculate Basic and Diluted Earnings Per Share (EPS).

SOLUTION

Computation of basic earnings per share

Net profit for the current year / Weighted average number of equity shares outstanding during the year

₹ 37,50,000 / 5,00,000 = ₹ 7.50 per share

Computation of diluted earnings per share = $\frac{\text{Adjusted net profit for the current year}}{\text{Weighted average number of equity shares}}$

Adjusted net profit for the current year

	₹
Net profit for the current year	37,50,000
Add: Interest expense for the current year	4,00,000
Less: Tax relating to interest expense (30% of ₹ 4,00,000)	(1,20,000)
Adjusted net profit for the current year	40,30,000

Number of equity shares resulting from conversion of debentures

= 55,000 Equity shares (given in the question)

Weighted average number of equity shares used to compute diluted earnings per share

= 5,55,000 shares (5,00,000 + 55,000)

Diluted earnings per share

= 40,30,000/ 5,55,000 = ₹ 7.26 per share

Note: Conversion of convertible debentures into Equity Share will be dilutive potential equity shares. Hence, to compute the adjusted profit the interest paid on such debentures will be added back as the same would not be payable in case these are converted into equity shares.

QUESTION 6

On 1st April, 2019 a company had 6,00,000 equity shares of ₹ 10 each (₹ 5 paid up by all shareholders). On 1st September, 2019 the remaining ₹ 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, 2020 was ₹ 21,96,000 after considering dividend ₹ 3,40,000 on preference shares.

You are required to compute Basic EPS for the year ended 31st March, 2020 as per Accounting Standard 20 "Earnings Per Share".

SOLUTION

Basic Earnings per share (EPS)

$$= \frac{\text{Net profit attributable to equity shareholders}}{\text{Weighted average number of equity shares outstanding during the year}}$$

$$= \frac{21{,}96{,}000}{4{,}57{,}500 \text{ Shares (as per working note)}} = ₹\ 4.80 \text{ per share}$$

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
	₹	₹	₹
1.4.2020	6,00,000	5	6,00,000 x 5/10 x 5/12 = 1,25,000
1.9.2020	5,40,000	10	5,40,000 x 7/12 = 3,15,000
1.9.2020	60,000	5	60,000 x 5/10 x 7/12 = 17,500
Total weighted average equity shares			4,57,500

QUESTION 7 (IMPORTANT QUESTION ON CALLS IN ARREAR)

On 1st April, 2019 a company had 6,00,000 equity shares of ₹ 10 each (₹ 5 paid up by all shareholders). On 1st September, 2019 the remaining ₹ 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, 2020 was ₹ 21,96,000 after considering dividend on preference shares and dividend distribution tax on such dividend totalling to ₹ 3,40,000.

You are required to compute Basic EPS for the year ended 31 st March, 2020 as per Accounting Standard 20 "Earnings Per Share".

SOLUTION

Basic Earnings per share (EPS)

$$= \frac{\text{Net profit attributable to equity shareholders}}{\text{Weighted average number of equity shares outstanding during the year}}$$

$$= \frac{21{,}96{,}000}{4{,}57{,}500 \text{ Shares (as per working note)}} = ₹\ 4.80 \text{ per share}$$

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
	₹	₹	₹
1.4.2020	6,00,000	5	6,00,000 x 5/10 x 5/12 = 1,25,000
1.9.2020	5,40,000	10	5,40,000 x 7/12 = 3,15,000
1.9.2020	60,000	5	60,000 x 5/10 x 7/12 = 17,500
Total weighted average equity shares			4,57,500

NOTES

ACCOUNTING STANDARD:13
INVESTMENT ACCOUNT
(EXAM RATING: 5 STARS)

UNIT 1: THEORY QUESTIONS

QUESTION NO 1

Define investment as per Accounting *Standard-13*. How investments are classified by AS-13? What are the items not dealt with by AS-13?

SOLUTION:

Meaning of Investments: AS-13 defines investments as assets held by an enterprise for:

Earning income by way of dividends, interest, and rentals, e.g., investment in building let out

Capital appreciation, e.g., increase in the value of land,

Other benefits to the investing enterprise, e.g., to control the investee,

Not held as stock-in-trade, e.g., held by investment company not investment

AS-13 does not deal with:

Bases for recognition of interest, dividends and rentals earned covered by AS-9;

Operating or finance leases;

Investments of retirement benefit plans and life insurance enterprises; and

Mutual funds, banks and public financial institutions

Classification of investments: An enterprise should disclose current investments and long-term investments distinctly in its financial statements.

Current investment: A current investment is an investment that is-

By its nature readily realizable, e.g., land & building are not readily realizable, and

Intended to be held for not more than one year from the date of making such investment (Evidence that held for not more than one year could be management representation)

Therefore,' ready marketability is not the only criteria for classifying the investment in to current or long term. To be classified as current investment, an investment must be made for a period not more than one year.

Long-term investment: A long-term investment is an investment other than a current investment, e.g., investment in property such as land and building should be accounted for as long term investment.

Further classification of current and long-term investments should be as specified in the statute governing the enterprise. In the absence of a statutory requirement, such further classification should disclose, where applicable, investments in:

Government or Trust securities

Shares, debentures or bonds

Investment properties

Others—specifying nature

QUESTION NO 2

Briefly indicate, how would you determine the cost of investment?

SOLUTION:

Cost of Investments: AS-13 lays down following with regard to determination of cost:

Acquisition against monetary consideration: The cost of an investment should include purchase price and acquisition charges such as brokerage, fees and duties.

It is also possible that an investment has been purchased on cum-interest or cum-dividend basis, the subsequent receipt of interest/dividend is allocated between pre-acquisition and post-acquisition periods; the pre-acquisition portion is deducted from cost as it represents recovery of cost.

Acquisition of right shares: When right shares are acquired, the cost of the right shares is added to the carrying amount of the original holding. If rights are not acquired but sold in the market, the sale proceeds are taken to the profit and loss account. However, where the investments are acquired on cum-right basis and the market value of investments immediately after their becoming ex-right is lower than the cost for which they were acquired, it may be appropriate to apply the sale proceeds of rights to reduce the carrying amount of such investments to the market value.

QUESTION NO 3

Summarize the provision contained in the Accounting Standard-13 in respect of valuation of investments in the financial statements.

SOLUTION:

Valuation of Investments: Valuation depends upon classification of investments:

Current investments:

Present in the financial statements at the lower of cost and fair value.

Cost or fair value should be determined either on an individual investment basis (i.e., cost and fair value of each investment should be compared separately) or by category of investment (all types preference shares constitute a category), but not on an overall/global basis.

Long-term investments:

Present at cost

Provision for diminution (reduction) in the value of the investments, shall be made to recognise a decline, other than temporary,

Such reduction being determined on individual investment basis

Changes in Carrying Amounts of Investments:

Any reduction in the carrying amount and any reversals of such reductions should be charged or credited to the profit and loss account.

Disposal of Investments: On disposal of an investment, the difference between the carrying amount and net disposal proceeds should be charged or credited to the profit and loss account.

When disposing of a part of the holding of an individual investment, the carrying amount to be allocated to that part is to be determined on the basis of the average carrying amount of the total holding of the investment.

QUESTION NO 4

Briefly summarize the discloser requirements of Accounting Standard-13.

SOLUTION:

Disclosure: The following information should be disclosed in the financial statements:

Accounting policies for valuation of investments;

Classification of investments;

Amounts included in profit and loss account for interest, dividends from subsidiary companies, other dividends and rentals separately from long term and current investments.

Gross income should be stated, the TDS being included under Advance Taxes Paid;

Profits and losses on disposal of current and long term investments and changes in the earning amount of such investments;

Significant restrictions on the right of ownership, realisability of investments **or** the remittance of income and proceeds of disposal;

Aggregate amount of quoted and unquoted investments along with market value;

Other disclosures as specifically required by the relevant statute.

UNIT 2: ACCOUNTING FOR SHARES

QUESTION NO 5

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

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

(2) Right shares are to be issued to the existing shareholders on 1st September 2009. The company will issue one right share for every 6 shares at 20% premium. No dividend was payable on these shares.

(3) Dividend for the year ended 31.3.2009 were declared by ABC Ltd. @ 20% which was received by XY Ltd. on 31st October 2009.

XY Ltd.

(i) Took up half the right issue

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

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

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

SOLUTION :

In the books of XY Ltd.

Investment in equity shares of ABC Ltd.

For the year ended 31st March, 2010

Date	Particulars	No	Dividend (₹)	Amount (₹)	Date	Particular	No	Dividend (₹)	Amount (₹)
2009 April 1	To balance b/d	15,000	-	2,25,000	2009 Oct. 31	By Bank A/c(W.N.5)	-	30,000	10,000
June 1	To bank A/c	5,000	-	1,00,000	2010 Jan. 1	By Bank A/c(W.N4)	13,000	-	2,12,355
July 1	To bonus issue (W.N1)	4,000	-	-	March 31	By Balance c/d (W.N.6)	13,000	-	1,69,500
Sep. 1	To Bank A/c (W.N.2)	2,000	-	24,000					
2010 March 31	To P&L A/c (W.N.4)	-	-	42,855					
	To P&L A/c	-	30,000	-					
		26,000	**30,000**	**3,91,855**			**25,000**	**30,000**	**3,91,855**

Working Notes:

1. **Calculation of no. of bonus shares issued**

$$\text{Bonus Shares} = \frac{15{,}000 \text{ shares} + 5{,}000 \text{ shares}}{5} \times 1 = 4{,}000 \text{ shares}$$

2. **Calculation of rights shares subscribed**

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

$$\text{Shares subscribed by XY Ltd.} = \frac{4{,}000}{2} = 2{,}000 \text{ shares}$$

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

3. **Calculation of sale of right entitlement**

2,000 shares x ₹8 per share = ₹ 16,000

Amount received from sale of tights will be credited to P&L A/c as per Para 13 of AS 13 'Accounting for investment'.

4. **Calculation of profit on sale of shares**

Total holding =	15,000 shares	original
	5,000 shares	purchased
	4,000 shares	bonus
	2,000 shares	right shares
	26,000 shares	

50% of the holding were sold

i.e. 13,000 shares (26,000 shares (on average basis)

= ₹2,25,000 + ₹1,00,000 + ₹24,000 - ₹10,000

= ₹3,39,000

Average cost of 13,000 shares would be

$$= \frac{3,39,000}{26,000} \times 13,000 = ₹1,69,500$$

Sale proceeds of 13,000 shares (13,000xx₹16.50)	2,14,500
Less: 1% Brokerage	(2,145)
	2,12,355
Less: cost of 13,000 shares	(1,69,500)
Profit on sale	42,855

5. **Dividend received on investment held as on 1st April,2009**

= 15,000 shares x ₹10x20%

= ₹30,000 will be transferred to profit and loss A/c

Dividend received on shares purchased on 1st June 2009

= 5,000 shares x ₹10 x 20% = ₹10,000 will be adjusted to investment A/c

Note: it is presumed that no dividend is received on bonus shares as bonus shares are declared on 1st July 2009 and dividend pertains to the year ended 31.3.2009.

6. **Calculation of closing value of shares (on average basis) as on 31st March, 2010**

$$13,000 \times \frac{3,39,000}{26,000} = ₹1,69,500.$$

QUESTION NO 6

On 1st April, 2011, Rajat has 50,000 equity shares of P Ltd. at a book value of ₹15 per share (face value rs.10 each). He provides you the further information:

(1) on 20th June, 2011 he purchased another 10,000 shares of P Ltd. at ₹16 per share

(2) on 1st August, 2011, P Ltd. issued one equity bonus share for every six shares held by the shareholders/

(3) on 31st October, 2011, the directors of P Ltd. announced a right issue which entitles the holders to subscribe three shares for every seven shares at ₹15 per share. Shareholders can transfer their rights in full or in part.

Rajat sold 1/3rd of entitlement to Umang for a consideration of ₹2 per share and subscribed the rest on 5th November, 2011.

You are required to prepare investment A/c in the books of Rajat for the year ending 31st March, 2012.

SOLUTION :

In the books of Rajat

Investment Account

(equity shares in P Ltd.)

Date	Particulars	No. of shares	Amount (₹)	Date	Particulars	No. of shares	Amount (₹)
1.4.11	To balance b/d	50,000	7,50,000	31.3.12	By balance c/d (bal. fig)	90,000	12,10,000
	To bank A/c	10,000	1,60,000				
	To bonus issue (W.N.1)	10,000					
	To bank A/c (right shares) (W.N.4)	20,000	3,00,000				
		90,000	**12,10,000**			**90,000**	**12,10,000**

Working Notes:

(1) Bonus shares = $\frac{50,000 + 10,000}{6}$ =10,000 shares

(2) Right shares = $\frac{50,000 + 10,000 + 10,000}{7} \times 3$ = 30,000 shares

(3) Sale of Rights = 30,000 shares x $\frac{1}{3}$ x ₹15 = ₹3,00,000

QUESTION NO 7

On 01-04-2011, Mr. T. Shekharan purchased 5,000 equity shares of ₹100 each in V Ltd. @ ₹120 each from a broker who charged 2% brokerage. He incurred 50 paisa per ₹100 as cost of shares transfer stamps. On 31-01-2012 bonus was declared in the ratio of 1:2. Before and after the record date of bonus shares, the shares were quoted at ₹175 per share and ₹90 per share respectively. On 3103-2012, Mr. T. shekharan sold bonus shares to a broker, who charged 2% brokerage.

Shoe the investment account in the books of T. Shekharan, who held the shares as current Assets and closing value of investment shall be made at cost or market value whichever is lower.

SOLUTION :

In the books of T. Shekharan

Investment Account

For the year ended 31st March, 2012

(Script : Equity Shares of V Ltd.)

Date	Particulars	Nominal Value (₹)	Cost (₹)	Date	Particulars	Nominal Value (₹)	Cost (₹)
1.4.2011	To Bank A/c (W.N.1)	5,00,000	6,15,000	31.3.2012	By Bank A/c (W.N.2)	2,50,000	2,20,500
	To bonus shares	2,50,000	-	31.3.2012	By Balance c/d (W.N.4)	5,00,000	4,10,000
	To profit and Loss A/c (W.N.3)		15,500				
		7,50,000	**6,3,500**			**7,50,000**	**6,30,500**

Working Notes:

1. **Cost of equity shares purchased on 1st April, 2011**

= cost +Brokerage+ cost of transfer stamps

=5,000x ₹120+2% of ₹6,00,000 + ½ % of ₹6,00,000

=₹6,15,000

2. **sale proceeds of equity shares sold on 31st March, 2012**

   = sale price – Brokerage

   =2,500 x ₹90 – 2%of ₹2,25,000

   =₹2,20,000.

3. **profit on sale of bonus shares on 31st March, 2012**

   = sales proceeds – Average cost

   Sales proceeds = ₹2,20,500

   Average cost = ₹ [6,15,000 x 2,50,00/7,50,000]

   = ₹ 2,05,000

   Profit = ₹ 2,20,500 - ₹ 2,05,000 = ₹15,500.

4. **Valuation of equity shares on 31st March 2012**

   Cost = ₹[6,15,000 x 5,00,000/7,50,000] = ₹4,10,000 i.e. ₹ 82 per share

   Market Value= 5,000 Shares x ₹90 = ₹4,50,000

Closing stock of equity shares has been valued at ₹4,10,000 i.e. cost being lower than the market value.

QUESTION NO 8

A limited purchased 5,000 equity shares (face value ₹100 each) of Allianz limited for ₹105 each on 1st April, 2014. The shares were quoted cum dividend. On 15th may, 2014, Allianz Limited declared & paid dividend of 2% for year ended 31st March, 2014. On 30th June, 2014 Allianz limited issued bonus shares in ratio of 1:5 on 1st October, 2014 Allianz Limited issued rights share in the ratio of 1:2 @ 45 per share. A Limited subscribed to half of the rights issue and the balance was sold at ₹5 per right entitlement. The company declared interim dividend of 1% on 30th November, 2014. Right shares were not entitled to dividend. The company sold 3,000 shares on 31st December, 2014 at ₹ 95 per share. The company A Ltd. incurred 2% as brokerage while buying and selling shares.

You are required to prepare investment account in books of A Ltd.

QUESTION NO 9

On 1.4.2014, sundar had 25,000 equity shares of 'X' Ltd. at a book valu of ₹15 per share (face value Rs 10). On 20.6.2014, 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 16.8.2014).

Rights basis 3:7 (date 31.8.2014) price ₹15 per share.

Due date for payment 30.9.2014.

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: dividend for the year ended 31.3.2014 at the rate of 20% were declared by X Ltd. and received by sundar on 31.10.2014. dividends for shares acquired by him on 20.6.2014 are to be adjusted against the cost of purchase.

On 15.11.2014. 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 31.12.2014 and shares are valued at average cost.

QUESTION NO 10

On 1.4.2014, Mr Krishna murty purchased 1,000 equity shares of ₹100 each in TELCO Ltd. @ ₹120 each from a broker, who charged 2% brokerage. He incurred 50 paise per ₹100 as cost of shares transfer stamps. On 31.3.2015 bonus was declared in the ratio of 1 : 2 Before and after the record date of bonus shares the shares were quoted at ₹175 per share and ₹90 per share respectively. On 31.3.2015 Mr. Krishna Murty sold bonus shares to a broker, who charged 2% brokerage.

Show the investment Account in the books of Mr. Krishna Murty. Who held the shares as Current assets and closing value of investments shall be made at cost of Market value which ever is lower.

QUESTION NO 11

Mr. X purchased 500 equity shares of ₹100 each in omega Co. Ltd. for ₹ 62,500 inclusive of brokerage and stamp duty. Some years later the company resolved to capitalize its profits and to issue to the holders of equity shares, one equity bonus share for every share held by them. Prior to capitalization, the shares of omega co. Ltd. were quoted at ₹175 per share. After the capitalization, the shares were quoted at ₹92.50 per share. Mr. X. sold the bonus shares and received at ₹90 per share.

Prepare the investment account in X's books on average cost basis.

QUESTION NO 12

On 1st January 2014, singh had 20,000 equity shares in X Ltd. face value of the shares was on ₹10 each but their book value was ₹ 16 per share. On 1st June 2014, Singh purchased 5,000 more equity shares in the company at a premium of ₹ 4 per share.

On 30th June, 2014, the directors of X Ltd. announced a bonus and rights issue. Bonus was declared at the rate of one equity share for every five shares held and these were received on 2nd august, 2014.

The terms of the rights issue were:

(a) rights shares to be issued to the existing holders on 10th august, 2014.

(b) rights issue would entitle the holders on 10 august, 2014.

(c) rights issue would entitle the holders to subscribe to additional equity shares in the company at the rate of one share per every held at ₹ 15 per share the whole sum being payable by 30th September, 2014.

(d) existing share holders were entitled to transfer their rights to outsiders, either wholly or in part.

(e) Singh exercised his option under the issue for 50% of his entitlements and the balance of rights he sold to ananth for a consideration of ₹1.50 per share.

(f) dividends for the year ended 31st March, 2014, at the rate of 15% were declared by the company and received by singh on 20th October, 2014.

(g) on 1st November, 2014, Singh sold 20,000 equity shares at a premium of ₹ 3 per share. The market price of share on 31-12-2014 was ₹14. Show the investment Account as it would appear is Singh's books on 31-12-2014 and the value of shares held on that date.

QUESTION NO 13

Y Limited purchases 25,000 shares of ₹ 10 each of X Limited on 15.4.1999 @ 120 per share(cum-right cum dividend). The company paid brokerage 1.5% and stamp duties 1%. It acquires another 30,000 shares of X Limited on 25.5.1999 @ ₹ 140 pr share(cum right cum dividend). And paid for brokerage and stamp duties. The company offered 1:1 right @ 80 per share on 30.5.99. Y Limited acquired 35,000 shares exercising the right and sold the right for 20,000 shares @ ₹ 30 per right. The company received dividend @ 40% on paid up value of shares for 1999-2000. It sold 15,000 shares @ ₹ 110 less brokerage 1.5% on 15.11.1999. Please calculate the cost of investment sold, carrying amount of unsold investments and profit on sale of investments.

QUESTION NO 14

A Limited purchases 10000 shares of X Limited @ ₹ 80 and paid brokerage @ 1.5% and stamp duties ₹ 8000 on 15.12.1999. The company purchases another 15000 shares of X Limited @ 96 and paid brokerage @ 1.5% and stamp duties ₹ 14400 on 25.12.1999. It sold 12000 shares @ 105 and brokerage @ 1.5% on 15.2.2000.

Show the cost of investment balance In account in the balance sheet and amount of profit or loss on the sale?

QUESTION NO 15

Continuing with the example above if X Limited issues one bonus share for every two shares held on 2.1.2000 and X Limited sold 12000 shares on 15.2.2000.

Calculate the carrying amount of investments

QUESTION NO 16

Mr. Lal purchased 500 equity shares of ₹ 100 each in omega co Ltd. for ₹ 62500 inclusive of brokerage and stamp duty on cum right basis. Later the company announced right issue @ one equity share for every share held by them. X accepted 50% of right shares and sold 50% right. The shares of Omega co Ltd. were quoted at ₹ 110 per share pre right and the shares were quoted at Rs92.50 per share after right issue. Mr. Lal sold the right @10 per right share and paid at ₹ 80 per share as subscription charges for his 50% shares.

Prepare investment account on average cost basis valuation.

QUESTION NO 17

Sharma purchased 1000 equity shares of X Ltd. as ₹ 35 each on 1st April 2003. He further purchased 300 equity shares @32 each on 1 july 2003. On 30 Sep, he received dividend @ ₹ 2 per share for the year 2002-03. He sold 500 shares @38 per share on 1 Nov 2003. Market value of share on 31st March 2004 was ₹ 33, prepare investment account(assume permanent investment).

QUESTION NO 18

MY Ltd. Had acquired 200 equity shares of YZ Ltd. At ₹ 105 per share on 1.1.2009 and paid ₹ 200 towards brokerage, stamp duty and STT. On 31st March, 2009 Share of YZ Ltd. Were traded at ₹ 110 per share. At what value investment is to be shown in the Balance Sheet of MY Ltd. As at 31st March, 2009.

QUESTION NO 19

Rose Ltd. Had made an investment of ₹ 500 lakhs in the equity shares of Nose Ltd on 10.01.2009. The realizable value of such investment on 31.03.2009 became

₹ 200 laksh as Nose Ltd. Lost a case of patent rights. Rose Ltd. Follows financial years as accounting year. How will you recognize this reduction in Financial Statements for the year 2008-09.

QUESTION NO 20

On 01-05-2012, Mr. Mishra purchased 800 equity shares of ₹ 10 each in Fillco Ltd. @ ₹50 each from a broker who charged 5%. He incurred 20 paisa per ₹ 100 as cost of shares transfer stamps. On 31-10-2012, bonus was declared in the ratio 1:4 The shares were quoted at ₹ 110 and ₹ 60 per share before and after the record date of bonus shares respectively. On 30-11-2012, Mr. Mishra sold the bonus shares to a broker who charged 5%. You are required to prepare Investment Account in the books of Mr. Mishra for the year ending 31-12-2012 and closing value of Investment shall be made at cost or market value whichever is lower.

SOLUTION:

In the books of Mr. MISHRA Investment Account for the year ended 31.12.2012

Date	Particular	No. of shars (₹)	Amount (₹)	Date	Particular	No. of shares (₹)	Amount (₹)
1.5.2012	To bank A/c	800	42,080	30.11.2012	By bank A/c	200	11,400
31.10.2012	To Bonus Shares	200	-	31.12.2012	By Bal. c/d	800	33,664
31.12.2012	To profit on sale		2,984				
		1,000	**45,064**			**1,000**	**45,064**

W.N#1

CALCULATION OF COST OF INVESTMENTS PURCHASED ON 1.5.2012

Particulars	Amount
Purchase price (800*50)	40,000
Brokerage @ 5%	2,000
Stamp duty (40000*.20/100)	80
Total acquisition cost	42,080

W.N#2

CALCULATION OF PROFIT OR LOSS ON SALE OF INVESTMENTS ON 30.11.2012

Particulars	Amount
Selling price (200*60)	12,000
Brokerage @ 5%	(600)
Net selling price	11,400
Cost for sold portion on weighted average cost basis	8,416
(42080/1000shares x 200shares)	
Profit on sale	2,984

W.N#3

VALUATION OF INVESTMENTS

Particulars	Amount
Cost Of Investments (42080/1000 X 800)	33664
Or	
Market Value on Balance Sheet Date	48000
(800*60)	
Whichever Is Lower	33664

classes

UNIT 3: ACCOUNTING FOR DEBENTURES

QUESTION NO 21

Mr. T purchased 1,000 nos. 10% debentures of ₹ 100 each on 1st April, 2009 at ₹ 96 com interest, the previous interest date being 31st December, 2008. Computer cost of investment.

QUESTION NO 22

In 2011, M/s wye Ltd. issued 12% fully paid debenture of ₹100 each, interest being payable half yearly on 30th September and 31st March of every accounting year.

On 1st December, 2012 M/s Bull & bear purchased 10,000 of these Debentures at ₹101 cum-interest price, also paying brokerage @ 1% of cum-interest amount of the purchase. On 1st March, 2013 the firm sold all of these debentures at ₹106 cum interest price, again paying brokerage @ 1% of cum-interest amount. Prepare investment account in the books of M/s. Bull & Bear for the period 1st December, 2012 to 1st March, 2013.

SOLUTION :

In the books of M/s Bull & Bear
Investment account
For the period from 1st December 2012 to 1st March, 2013
(Scrip : 12% Debentures of M/s. Wye Ltd.)

Date	Particular	Nominal value (Rs)	Interest	Cost (₹)	Date	Particular	Nominal Value (₹)	Interest	Cost (₹)
1.12.2012	To bank A/c (W.N.1)	10,00,000	20,000	10,00,100	1.03.2013	By bank A/c (W.N.2)	10,00,000	50,000	9,99,400
1.3.2013	To Profit & loss A/c		30,000		1.3.2013	By profit & Loss A/c			700
		10,00,000	50,000	10,00,100			10,00,000	50,000	10,00 ,100

Working Notes:

1. **Cost of 12% debentures purchased on 1.12.2012**

	₹
Cost Value (10,000x₹101) =	10, 10,000
Add: Brokerage (1% of ₹10,10,000) =	10,100

Less : Cum interest (10,000x100x12%x2/12) =	(20,000)
Total =	10, 00,100

2. Sale proceeds of 12% Debentures sold on 31st March, 2013 ₹

Sales Price (10,000x₹106) =	10,60,000
Less: Brokerage (1% of ₹ 10,60,000) =	(10,600)
Less: Cum interest (10,000x100x12%x5/12) =	(50,000)
Total =	9,99,4000

QUESTION NO 23

The following information is presented by Mr. Z, relating to his holding in 9% Central Government bonds.

Opening balance (face value) ₹1,20,000 cost ₹1,18,000(face value of each unit is ₹100).

1.3.2008	Purchased 200 units, ex-interest at ₹ 98.
1.7.2008	Sold 500 units, ex-interest out of original holding at ₹100.
1.10.2008	Purchased 150 units at ₹98, cum interest.
1.11.2008	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 as it would in this books. Mr. Z follows FIFO method.

SOLUTION :

In the books of Mr. Z

9% Central Government bonds (investment) account

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

Working Note:

Calculation of closing balance:	**Units**		₹
Bonds In hand remained in hand at 31st 2008	40,000	$\frac{1,18,000}{1,20,000}$ = x 40,000=	39,333
From original holding (1,20,000-50,000-30,000)=			19.600
Purchased on 1st March	20,000		14.700
Purchased on 1st October	15,000		
TOTAL	**75,000**		**73,633**

QUESTION NO 24

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

1.4.2009	Opening balance- face Value ₹1,20,000, cost ₹1,18,000
1.7.2009	100 debentures purchased ex-interest at ₹98
1.10.2009	Sold 200 Debentures ex-interest at ₹100
1.1.2010	Purchased 50 Debentures at ₹98 cum-interest
1.2.2010	Sold 200 Debentures ex-interest at ₹99

Due dates for interest are 30th September and 31st march.

Mr. Purohit closes his books on 31.03.20x2. Brokerage is to be paid @ 1% for each transaction. Prepare investment account in the books of investor assuming FIFO method for accounting. Market value of debentures on balance sheet date is 99 per debenture.

SOLUTION:

Investment A/c of Mr. Prohit

For the year ending on 31-3-2010

(Scrip: 8% Debentures of P Limited_

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

Date	Particulars	Nominal Value	Interest	Cost	Date	Particulars	Nominal Value	Interest	Cost
			(₹)	(₹)				(₹)	(₹)
1.4.09	To balance b/d	1,20,000	-	1,18,000	30.9.09	By Bank	-	5,200	-
1.7.09	To bank (ex-interest)	10,000	200	9,898	1.10.09	By Bank	20,000	-	19,800
1.10.09	To profit & Loss A/c			133	1.12.10	By Bank (ex interest	20,000	533	19,602
1.1.10	To bank (cum-interest)	5,000	100	4,849					
					1.2.10	By profit & Loss A/c	-	3,800	64
31.3.10	To profit & Loss A/c(Bal. fig.)	-	9,233						
					31.3.10	By Bank	95,000	-	-
					31.3.10	By Balance c/d			93,414
		1,35,000	**9.533**	**1,32,880**			**1,35,000**	**9,533**	**1,32,880**

Working Notes:

1. Valuation of closing balance as on 31.3.2010:

Market value of 950 Debentures at ₹99 =	₹94,050
Cost Price of	
800 Debentures cost = ($\frac{1,18,000}{1,20,000}$ x 80,000) =	78,667
100 Debentures cost =	9,898
50 Debentures cost- =	4,849
	93,414

Value at the end = ₹93,414 i.e. whichever is less

2. Profit on sale of debentures as on 1.10.2009

	₹
Sales price of Debentures (200x100)	20,000
Less: Brokerage @ 1%	(200)
	19,800
Less: cost price of Debentures ($\frac{1,18,000}{1,20,000}$ x 20,000) =	(19,667)
Profit on sale	133

3. Loss on sale of debentures as on 1.2.2010

	₹
Sale price of debentures (200x99)	19,800
Less: Broerage @ 1%	(198)
	19,602
Less: cost price of Debentures ($\frac{1,18,000}{1,20,000}$ x 20,000) =	(19,666)
Loss on sale	64

QUESTION NO 25

Mr. Chatur had 12% Debentures of face value ₹ 100 of M/s Unnati Ltd. as current investments. He provides the following details relating to the investments.

1-4-2014	Opening balance 4,000 debentures costing ₹98 each
1-6-2014	Purchased 2,000 debentures @ ₹120 cum interest
1-9-2014	Sold 3,000 debentures @ ₹110 cum interest
1-12-2014	Sold 2,000 debentures @ ₹105 ex-interest
31-1-2015	Purchased 3,000 debentures @ ₹100 ex-interest
31-1-2015	Market value of the investment ₹105 each

Interest due date are 30th June and 31st December.

Mr. Chatur closes his books on 31-3-2015. He incurred 2% brokerage for all his transactions show investment account in the books of Mr. Chatur assuming FIFO method is followed

SOLUTION :

Investment A/c of Mr. Chatur

For the year ending on 31.3.2015

(scrip : 12% Debenture of Unnati limited

(interest Payable on 30th June and 31st December)

Date	Particulars	Nominal Value	Interest	Cost	Date	Particulars	Nominal Value	Interest	Cost
1.4.2014	To balance b/d	4,00,000	12,000	3,92,000	30.6.2014	By bank (6,00,000 x 6%)	-	36,000	-
1.6.2014	To bank	2,00,000	10,000	2,34,800					
					1.9.2014	By bank	3,00,000	6,000	3,17,400
1.9.2014	To profit & Loss A/c			23,400	1.12.2014	By Bank	2,00,000	10,000	2,05,800
31.1.2015	To bank	3,00,000	3,000	3,06,000	1.12.2014	By Profit & Loss A/c	-	-	9,600
31.3.2015	To profit & Loss A/c (Bal. fig.)		45,000		31.12.14	By Bank (1,00,000 x 6%)	-	6,000	-
					31.3.2015	By Profit & Loss A/c	-	-	3,400
					31.3.2015	By Balance c/d	4,00,000	12,000	4,20,000
		9,00,000	**70,000**	**9,56,200**			**9,00,000**	**70,000**	**9,56,200**

Working Notes:

1. **Valuation of closing balance as on 31.3.2015:**	
Market Value of 4,000 Debentures at ₹105+	₹ 4,00,000
Cost price of 1,000 Debentures at	1,17,400
3,000 debentures at	3,06,000
	4,23,400

Value at the end = ₹4,20,000 i.e. whichever is less

2. Profit on sale of debentures as on 1.9.2014

	₹
Sales price of Debentures (3,000x₹110)	3,30,000
Less: Brokerage @2%	(6,600)
	3,23,400
Less : interest for 2 months	(6,000)
Less: cost price of Debentures (3,92,000 x $\frac{3,000}{4,000}$)	(2,94,000)
Profit on sale	23,400

3. Loss on sale of debentures as on 1..12.2014

	₹
Sales price of Debentures (2,000x₹105)	2,10,000
Less: Brokerage @ 2%	(4,200)
	2,05,800
Less: cost price of Debentures (98,000 + 1,17,400)	(2,15,400)
Loss on sale	9,600

4. Purchase Cost of 2,000 debentures on 1.6.2014

	₹
2,000 Debentures @ ₹120 cum interest	2,40,000
Add: Brokerage @ 2%	4,800
	2,44,800
Less: Interest for 5 Months	(10,000)
Purchase cost of 2,000 debentures	2,34,800

5. Sale Value for 3,000 debentures on 1.9.2014

	₹
Sales price of Debentures cum interest (3,000 x ₹110)	3,30,000
Less: Brokerage @2%	(6,600)
	3,23,400
Less: interest for 2 months	(6,000)
Sale value for 3,000 debentures	3,17,400

QUESTION NO 26

The following transaction of Nidhi took place during the year ended 31st March 2014:

1st April	Purchased ₹12,000,00, 8% bonds at ₹80.50 cum-interest. Interest is payable on 1st November and 1st May.
12th April	Purchased 1,00,000 equity shares of ₹10 each in X Ltd. for ₹40,00,000
1st May	Received half-year's interest on 8% bonds.
15th May	X Ltd. made a bonus issue of three equity shares for every two held. Nidhi sold 1,25,000 bonus shares for ₹ 20 each.
1st October	Sold ₹ 3,00,000 8% bonds at ₹81 ex-interest.
1st November	Received half years bond interest.
1st December	Received 18% dividend on equity shares in X Ltd.

Prepare the relevant investment account in the books of Nidhi for the year ended 31st March 2014.

QUESTION NO 27

Bonanzaa Limited held on 1st April 1993 ₹ 2,00,000 of 9% Government loan (2003) at ₹ 1,90,000. (Face value of loan ₹ 100 each). Three month's interest accrued on the above date. On 31st May 1993 the company purchased the same government loan of the face value of ₹ 80,000 at ₹ 95 (net) cum-interest. On 1st June 1993

60,000 face value of the loan was sold at ₹ 94 (net) ex-interest. Interest on the loan was paid each year on 30th June and 31st December and was credited by the bank on the same date. On 30th November 1993 ₹ 40,000 face value of the loan was sold at ₹ 97 (net) cum-interest. On 1st December 1993 the company purchased the same loan ₹ 10,000 at per ex-interest. On 1st March 1994 the company sold

10,000 face value of the loan at ₹ 95 ex-interest. The market price of the loan on 31st March 1994 was ₹ 96. Draw up the 9% government loan (2003) account in the books of the company. First in first out method shall be followed and the balance of the loan held by the company shall be valued at total average cost or market price whichever is lower. Calculation shall be made to the nearest rupee or multiple thereof.

QUESTION NO 28

A purchased on 1st March, ₹ 24,000 5% Bharat Debenture stock at 90 cum-interest interest being payable on 31st March and 30th September each year, stamp and expenses on purchase amounted to ₹ 20 and brokerage at 2% was charged on cost; interest for the half-year was received on the due date. On 1st September ₹ 10,000 of the stock was sold at 92 ex-interest less brokerage at 2%. On 30th September ₹ 8,000 stock was purchased at 91 ex-interest plus brokerage at 2% and charges ₹ 10. On 1st December ₹ 6,000 stock was sold at 94 cum-interest less brokerage at 2%. The market price of stock on 31st December was 91%. Show the investment account for the year ended 31st December, marking all calculations in months.

QUESTION NO 29

Tee Limited purchased on 1st May 1997 13.5% Convertible Debentures in Dee Limited of face value of ₹ 5,00,000 @ 105; Interest on the debentures is payable each year on 31st March and 30th September. The accounting year adopted by Tee Limited is the calendar year. The following other transactions were entered into in 1997 by Tee Limited in regard to these debentures:

August 1 Purchased ₹ 2,50,000 debentures @ 107 cum interest. October 1 Sale of ₹ 2,00,000 debentures @ 103

December 31 Receipt of 10,000 equity shares in Dee Limited of ₹ 10 each in conversion of 20% of the debentures held.

The market value of the debentures and equity shares in Dee Limited at the end of 1997 was 106 and ₹ 15 respectively.

Prepare the debenture investment account in the books of Tee Limited on average cost basis.

QUESTION NO 30

Gamma Investment Company hold 1,000, 15% debentures of ₹ 100 each in Beta Industries Ltd. As on April 1,2009 at a cost of ₹ 1,05,000. Interest is payable on June, 30 and December, 31 each year.

On may 1,2009, 500 debentures are purchased cum-interest at ₹ 53,500. On November, 1,2009, 600 debentures are sold ex-interest at ₹ 57,300. on November 30, 2009, 400 debentures are purchased ex-interest at ₹ 38,400. On December 31, 2009 400 debentures are sold cum-interest for ₹ 55,000.

Prepare the investment account showing value of holdings on March 31, 2010 at cost, using FIFO method.

UNIT 4: ACCOUNTING FOR MULTIPLE INVESTMENTS IN SINGLE QUESTION

QUESTION NO 31

Mr. Brown has made following transaction during the financial year 2011-12:

Date	Particulars
01.05.2011	Purchased 24,000 12% bonds of ₹100 each at ₹ 84 cum-interest. Interest is payable on 30th September and 31st March every year.
15.06.2011	Purchased 1,50,000 equity shares of ₹10 each in Alpha limited for ₹25 each through a broker, who changed brokerage @2%
10.07.2011	Purchased 60,000 equity shares of ₹ 10 each in Beeta Limited for Rs44 each through a broker, who changed brokerage @ 2%
14.10.2011	Alpha limited made a bonus issue of two shares for every three shares held.
31.10.2011	Sold 80,000 shares in alpha Limited for ₹22 each.
01.01.2012	Received 15% interim dividend on equity shares of Alpha Limited.
15.01.2012	Beeta Limited a right issue of One equity share for every four shares held at ₹5 per share. Mr. Brown exercised his option for 40% his entitlement and sold the balance rights in the market at ₹2.25 per share.
01.03.2012	Sold 15,000 12% bonds at ₹90 ex-interest.
15.03.2012	Received 18% interim dividend on equity shares of Beeta Limited.

Interest on 12% bonds was duly received on due dates

Prepare separate investment account for 12% Bonds. Equity shares of Alpha Limited and Equity shares of Beeta Limited in the books of Mr. Brown for the year ended on 31st March,2012

SOLUTION :

In the books of Mr. Brown

12% bonds for the year ended 31st March, 2012

Date	Particulars	No.	Interest (₹)	Amount (₹)	Date	Particulars	No.	Interest (₹)	Amount (₹)
2011 May 1	To Bank A/c	24,000	24,000	19,92,000	2011 Sept 30	By bank interest	-	1,44,000	
2012 March 31	To P&L A/c (W.N.1)	-	-	1,05,000	2012 Mar 1	By bank A/c	15,000	75,000	13,50,000
	To P&L A/c		2,49,000						
					2012 Mar. 1	By Bank interest		54,000	
						By Balance c/d (W.N.2)	9,000	-	7,47,000
		24,000	**2,73,000**	**20,97,000**			**24,000**	**2,73,000**	**20,97,000**

Investment in Equity shares of Alpha Ltd. for the year ended 31st March, 2012

Date	Particulars	No.	Dividend (₹)	Amount (₹)	Date	Particulars	No.	Dividend (₹)	Amount (₹)
2011 June 15	To Bank A/c	1,50,000	-	38,25,000	2011 Oct. 31	By bank A/c	80,000	-	17,60,000
Oct. 14	To bonus issue (1,50,000/ 3x2)	1,00,000	-	-	2012 Jan. 1	By Bank A/c dividend		2,55,000	
2012 Mar. 31	To P&L A/c (W.N.3)		2,55,000	5,36,000	March 31	By Balance c/d (W.N.4)	1,70,000	-	26,01,000
		2,50,000	**2,55,000**	**43,61,000**			**2,50,000**	**2,55,000**	**43,61,000**

Date	Particulars	No.	Dividend ₹	Amount ₹	Date	Particulars	No.	Dividend ₹	Amount ₹
2011 July 10	To bank A/c	60,000	-	26,92,800	2012 Mar.15	By Bank dividend	-	1,18,800	
2012 Jan. 15	To Bank A/c (W.N.5)	6,000	-	30,000	March 31	By Balance c/d (bal. fig.)	66,000		27,22,800
							66,000	**1,18,000**	**27,22,800**
March 31	To P&L A/c	-	1,18,800	-					
		66,000	**1,18,800**	**27,22,800**					

Working Notes:

1. **Profit on sale of 12% Bond**

Sales Price	₹13,50,000
Less: Cost of Bond sold = $\frac{19,92,000}{24,000} \times 15,000$	(₹12,45,000)
Profit on sale	₹1,05,000

2. **Closing balance as on 31.3.2012 of 12% Bond**

$\frac{19,92,000}{24,000} \times 9,000 =$ ₹7,47,000

3. **Profit on sale of equity shares of Alpha Ltd.**

Sales price	₹17,60,000
Less cost of bond sold = $\frac{38,25,000}{2,50,000} \times 80,000$	₹(12,24,000)
Profit on sale	₹5,36,000

4. **closing Balance as on 31.3.2012 of equity shares of Alpha Ltd.**

$\frac{38,25,000}{2,50,000} \times 1,70,000 =$ ₹26,01,000

5. **Calculation of right subscribed by Beeta. Ltd.**

Right shares= $\frac{60,000 \text{ shares}}{4} \times 1 = 15,000$ shares

Shares subscribed by Mr. Brown = 15,000x40% = 6,000 shares

Value of right shares subscribed = 6,000 shares @ ₹5 per share = ₹30,000

6. **calculation of sale of right entitlement by Beeta Ltd.**

No. of right shares sold = 15,000-6,000 = 9,000 shares

Sale value of right = 9,000 shares x ₹2.25 per share =₹20,250

Note: As per Para 13 of AS 13, sale proceeds of rights is to be credited to P&L A/c.

QUESTION NO 32

Smart investment made the following investment in the year 2013-14

12% state Govermment bonds having face value ₹100

Date	Particulars
01.04.2013	Opening balance (1200 bonds) book value of ₹1,26,000
02.05.2013	Purchased 2,000 bonds @ ₹100 cum interest
30.09.2013	Sold 1,500 bonds at ₹105 ex interest

Interest on the bonds is received on 30th June and 31st Dec. each year.

Equity Shares of X Ltd.	
15.04.2013	Purchased 5,000 equity shares @ ₹200 on cum right basis Brokerage of 1% was paid in addition (face value of shares ₹10)
03.06.2013	The company announced a bonus issue of 2 shares for every 5 share held.
16.08.2013	The company made a rights issue of 1 share for every 7 shares held. At ₹250 per share.
22.08.2013	The entire money was payable by 31.08.2013.
02.09.2013	Rights to the exlent of 20% was sold @ ₹60. the remaining rights were subscribed.
15.12.2013	Dividend @ 15% for the year ended 31.03.2013 was received on 16.09.2013
15.01.2014	Sold 3,000 shares @ ₹300. Brokerage of 1% was incurred extra.
31.03.2014	Received interim dividend @ 10% for the year 2013-14 The shares were quoted in the stock exchange @ ₹220

Prepare investment Accounts in the books of Smart Investments. Assume that the average cost method is followed.

SELF PRACTICE QUESTIONS

QUESTION 33 (CA INTER NOV 2019) (10 MARKS)

Mr. Harsh provides the following details relating to his holding in 10% debentures (face value of ₹ 100 each) of Exe Ltd. held as current assets:

1.4.2018	opening balance - 12,500 debentures, cost ₹ 12,25,000
1.6.2018	purchased 9,000 debentures@ ₹ 98 each ex-interest
1.11.2018	purchased 12,000 debentures @ ₹ 115 each cum interest
31.1.2019	sold 13,500 debentures@ ₹ 110 each cum-interest
31.3.2019	Market value of debentures @ ₹ 115 each

Due dates of interest are 30th June and 31st December.

Brokerage at 1% is to be paid for each transaction. Mr. Harsh closes his books on 31.3.2019. Show investment account as it would appear in his books assuming FIFO method is followed.

SOLUTION:

Investment Account of Mr. Harsh for the year ending on 31-3-2019

(Scrip: 10% Debentures of Exe Limited)

(Interest Payable on 30th June and 31st December)

Date	Particulars	Nominal Value ₹	Interest ₹	Cost ₹	Date	Particulars	Nominal Value ₹	Interest ₹	Cost ₹
1.4.18	To Balance b/d	12,50,000	31,250	12,25,000	30.6.18	By Bank 21,500 x 100 X 10% x 1/2	-	1,07,500	-
1.6.18	To Bank (ex-Interest) (W.N.1)	9,00,000	37,500	8,90,820	31.12.19	By Bank 33,500 x 100x10% x 1/2		1,67,500	

1.11.18	To Bank (cum-Interest) (W.N.2)	12,00,000	40,000	13,53,800	31.1.19	By Bank (W.N.3)	13,50,000	11,250	14,58,900
31.1.19	To Profit & Loss A/c (W.N.3)			1,34,920	31.3.19	By Balance c/d (W.N.4)	20,00,000	50,000 -	21,45,640
31.3.19	To Profit & Loss A/c (Bal. fig.)		2,27,500						
		33,50,000	**3,36,250**	**36,04,540**			**33,50,000**	**3,36,250**	**36,04,540**

Working Notes:

1. **Purchase of debentures on 1.6.18**

   Interest element = 9,000 x 100 x 10% x 5/12 = ₹ 37,500

   Investment element = (9,000 x 98) + [1%(9,000 x 98)] = ₹ 8,90,820

2. **Purchase of debentures on 1.11.2018**

   Interest element = 12,000 x 100 x 10% x 4/12 = ₹ 40,000

   Investment element = 12,000 X 115 X 101% less 40,000 = ₹ 13,53,800

3. **Profit on sale of debentures as on 31.1.19**

	₹
Sales price of debentures (13,500 x ₹ 110)	14,85,000
Less: Brokerage @ 1%	(14,850)
	14,70,150
Less: Interest (1,35,000/ 12)	(11,250)
	14,58,900
Less: Cost of Debentures [(12,25,000 + (890820 X 1,00,000/9,00,000)]	(13,23,980)
Profit on sale	1,34,920

4. **Valuation of closing balance as on 31.3.2019:**

Market value of 20,000 Debentures at ₹ 115 = ₹ 23,00,000

Cost of

8,000 Debentures	=	8,90,820 / 9,000 X 8,000 =	7,91,840
12,000 Debentures	=	13,53,800	
Total			21,45,640

Value at the end is ₹ 21,45,640, i.e., which is less than market value of ₹ 23,00,000.

QUESTION 34 (CA INTER NOV 2020) (5MARKS)

A Limited invested in the shares of XYZ Ltd. on 1st December, 2019 at a cost of ₹50,000. Out of these shares, ₹ 25,000 shares were purchased with an intention to hold for 6 months and ₹ 25,000 shares were purchased with an intention to hold as long-term Investment.

A Limited also earlier purchased Gold of ₹ 1,00,000 and Silver of ₹ 30,00,000 on 1st April, 2019. Market value as on 31st March, 2020 of above investments are as follows:

Shares	₹ 47,500 (Decline in the value of shares is temporary.)
Gold	₹ 1,80,000
Silver	₹ 30,55,000

How above investments will be shown in the books of accounts of M/s A Limited for the year ended 31st March, 2020 as per the provisions of AS 13 (Revised)?

SOLUTION:

As per AS 13 (Revised) 'Accounting for Investments, for investment in shares - if the investment is purchased with an intention to hold for short-term period (less than one year), then it will be classified as current investment and to be carried at lower of cost and fair value.

In the given case ₹ 25,000 shares held as current investment will be carried in the books at ₹ 23,750 (₹ 47,500/2).

If equity shares are acquired with an intention to hold for long term period (more than one year), then should be considered as long-term investment to be shown at cost in the Balance Sheet of the company. However, provision for diminution should be made to recognize a decline, if other than temporary, in the value of the investments. Hence, ₹ 25,000 shares held as long-term investment will be carried in the books at ₹ 25,000.

Gold and silver are generally purchased with an intention to hold them for long term period (more than one year) until and unless given otherwise.

Hence, the investment in Gold and Silver (purchased on 1st March, 2019) should continue to be shown at cost (since there is no 'other than temporary' diminution) as on 31st March, 2020. Thus Gold at ₹ 1,00,000 and Silver at ₹ 30,00,000 respectively will be shown in the books.

QUESTION 35 (CA INTER NOV 2020) (10 MARKS)

On 1st April, 2019 Mr. H had 30,000 equity shares of ABC Ltd. at book value of ₹ 18 per share (Nominal value 10 per share). On 10th June, 2019, H purchased another 10,000 equity shares of the ABC ltd. at ₹ 16 per share through a broker who charged 1.5% brokerage.

The directors of ABC Ltd. announced a bonus and a right issue. The terms of the issues were as follows:

(i) Bonus shares were declared at the rate of one equity share for every four shares held on 15th July, 2019.

(ii) Right shares were to be issued to the existing equity shareholders on 31st August, 2019. The company decides to issue one right share for every five equity share s held at 20% premium and the due date for payment will be 30th September, 2019. Shareholders were entitled to transfer their rights in full or in part.

(iii) No dividend was payable on these issues.

Mr. H subscribed 60% of the rights entitlements and sold the remaining rights for consideration of ₹ 5 per share.

Dividends for the year ending 31st March, 2019 was declared by ABC Ltd. at the rate of 20% and received by Mr. H on 31st October, 2019.

On 15th January, 2020 Mr. H sold half of his shareholdings at ₹ 17.50 per share and brokerage was charged @1 %.

You are required to prepare Investment account in the books of Mr. H for the year ending 31st March, 2020, assuming the shares are valued at average cost.

SOLUTION:

In the books of Mr. H

Investment in equity shares of ABC Ltd. for the year ended 31st March, 2020

Date	Particulars	No.	Income ₹	Amount ₹	Date	Particulars	No.	Income ₹	Amount ₹
2019 April 1	To Balance b/d	30,000	-	5,40,000	2019 Oct.	By Bank A/c (W.N. 5)	-	60,000	20,000
June	To Bank A/c	10,000	-	1,62,400	20X2 Jan.	By Bank A/c (W.N.4)	28,000	-	4,85,100
July	To Bonus Issue (W.N. 1)	10,000	-	-	March 31	By Balance c/d (W.N. 6)	28,000	-	3,77,200
Sept.	To Bank A/c (W.N. 2)	6,000	-	72,000					
2020 Jan.	To P&L A/c (W.N. 4)	-	-	1,07,900					
March 31	To P&L A/c	-	60,000	-					
		56,000	**60,000**	**8,82,300**			**56,000**	**60,000**	**8,82,300**

Working Notes:

1. **Calculation of no. of bonus shares issued**

   Bonus Shares = (30,000 + 10,000) divided by 4= 10,000 shares

2. **Calculation of right shares subscribed**

   $$\text{Right Shares} = \frac{30{,}000 \text{ shares} + 10{,}000 \text{ shares} + 10{,}000 \text{ shares}}{3}$$

   = 10,000 shares

   Shares subscribed 10,000 x 60% = 6,000 shares

   Value of right shares subscribed = 6,000 shares @ ₹ 12 per share = ₹ 72,000

3. **Calculation of sale of right entitlement**

   Amount received from sale of rights will be 4,000 shares x ₹ 5 per share = ₹ 20,000 and it will be credited to statement of profit and loss.

4. **Calculation of profit/loss on sale of shares-**

Total holding	=	30,000 shares original
		10,000 shares purchased
		10,000 shares bonus
		6,000 shares right shares
		56,000

50% of the holdings were sold i.e. 28,000 shares (56,000 x1/2) were sold.

Cost of total holdings of 56,000 shares

= ₹ 5,40,000 + ₹ 1,62,400 + ₹ 72,000– ₹ 20,000 = ₹ 7,54,400

Average cost of shares sold would be:

$$= \frac{7{,}54{,}400}{56{,}000} \times 28{,}000 = \text{₹}\ 3{,}77{,}200$$

Sale proceeds of 28,000 shares (28,000 x ₹17.50)	4,90,000
Less: 1% Brokerage	(4,900)
	4,85,100
Less: Cost of 28,000 shares sold	(3,77,200)
Profit on sale	1,07,900

5. **Dividend received on investment held as on 1st April, 2019**

= 30,000 shares x ₹ 10 x 20%

= ₹ 60,000 will be transferred to Profit and Loss A/c and

Dividend received on shares purchased on 10th June, 2019

= 10,000 shares x ₹ 10 x 20% = ₹20,000 will be adjusted to Investment A/c

6. **Calculation of closing value of shares (on average basis) as on 31st March, 2020**

$$= \frac{7{,}54{,}400}{56{,}000} \times 28{,}000 = \text{₹}\ 3{,}77{,}200$$

QUESTION 36 (CA INTER JAN 21) (5MARKS)

Kunal Securities Ltd. wants to reclassify its investments in accordance with AS -13 (Revised). State the values, at which the investments have to be reclassified in the following cases:

(i) Long term investment in Company A, costing ₹ 10.5 lakhs is to be re-classified as current investment. The company had reduced the value of these investments to ₹ 9 lakhs to recognize a permanent decline in value. The fair value on the date of reclassification is ₹ 9.3 lakhs.

(ii) Long term investment in Company B, costing ₹ 14 lakhs is to be re-classified as current investment The fair value on the date of reclassification is ₹ 16 lakhs and book value is ₹ 14 lakhs.

(iii) Current investment in Company C, costing ₹12 lakhs is to be re-classified as long term investment as the company wants to retain them. The market value on the date of reclassification is ₹ 13.5 lakhs.

(iv) Current investment in Company D, costing ₹ 18 lakhs is to be re-classified as long term investment. The market value on the date of reclassification is ₹ 16.5 lakhs.

SOLUTION:

As per AS 13 (Revised) 'Accounting for Investments', where long-term investments are reclassified as current investments, transfers are made at the lower of cost and carrying amount at the date of transfer. And where investments are reclassified from current to long term, transfers are made at lower of cost and fair value on the date of transfer.

Accordingly, the re-classification will be done on the following basis:

(i) In this case, carrying amount of investment on the date of transfer is less than the cost; hence this re-classified current investment should be carried at ₹ 9 lakhs in the books.

(ii) The carrying / book value of the long-term investment is same as cost i.e., ₹ 14 lakhs. Hence this long-term investment will be reclassified as current investment at book value of ₹ 14 lakhs only.

(iii) In this case, reclassification of current investment into long-term investments will be made at ₹ 12 lakhs as cost are less than its market value of ₹ 13.5 lakhs.

(iv) Market value of the investment is ₹ 16.5 lakhs, which is lower than its cost i.e., ₹ 18 lakhs. Therefore, the transfer to long term investments should be done in the books at the market value i.e., ₹ 16.5 lakhs.

QUESTION 37 (CA INTER JAN 21) (10 MARKS)

P Ltd. had 8,000 equity shares of K Ltd., at a book value of ₹ 15 per share (face value of ₹ 10 each) on 1st April,2019. On 1st September, 2019, P Ltd. acquired another 2,000 equity shares of K Ltd. at a premium of ₹ 4 per share. K Ltd. announced a bonus and right issue for existing shareholders.

The term of bonus and right issue were:

(i) Bonus was declared at the rate for two equity shares for every five shares held on 30th September, 2019.

(ii) Right shares are to be issued to the existing shareholders on 1st December, 219. The Company had issued two right shares for every seven shares held at 25% premium on face value. No dividend was payable on these shares. The whole sum being payable by 31st December, 2019.

(iii) Existing shareholders were entitled to transfer their right to outsiders either wholly or in part.

(iv) P Ltd. exercised its option under the issue for 50% of its entitlements and sold the remaining rights for ₹8 per share.

(v) Dividend for the year ended 31st March,2019 at the rate of 20% was declared by K Ltd. and received by P Ltd. on 20th January, 2020.

(vi) On 1st February, 2020, P Ltd. sold half of its shareholdings at a premium of ₹ 4 per share.

(vii) The market price of share on 31st March,2020 was ₹13 per share.

You are required to prepare the Investment account of P Ltd. for the year ended 31st March,2020 and determine the value of shares held on that date, assuming the investment as current investment. Consider average cost basis for ascertainment fo r cost for equity shares sold.

SOLUTION

Investment Account-Equity Shares in K Ltd.

Date		No. of shares	Dividend	Amount	Date		No. of shares	Dividend	Amount
			₹	₹				₹	₹
1.4.19	To Bal. b/d	8,000	-	1,20,000	20.1.20	By Bank (dividend) [8,000 x 10 x 20%] and [2,000 x 10 x 20%]		16,000	4,000
1.9.19	To Bank	2,000	-	28,000	1.2.20	By Bank	8,000		1,12,000
30.9.19	To Bonus Issue	4,000		—					
31.12.19	To Bank (Right) (W.N.1)	2,000	-	25,000	31.3.20	By Balance c/d (W.N. 3)	8,000		84,500
20.1.20	To Profit & Loss A/c (Dividend income)		16,000						
1.2.20	To P& L A/c (profit on sale)			27,500					
		16,000	16,000	2,00,500			16,000	16,000	2,00,500

Working Notes:

1. **Right shares**

   No. of right shares issued = (8,000 + 2,000 + 4,000)/ 7 X 2= 4,000

   No. of right shares subscribed = 4,000 x 50% = 2,000 shares

   Value of right shares issued = 2,000 x ₹12.50 = ₹ 25,000

   No. of right shares sold = 2,000 shares

   Sale of right shares = 2,000 x ₹ 8 = ₹ 16,000 to be credited to statement of profit and loss

2. **Cost of shares sold — Amount paid for 16,000 shares**

	₹
(₹1,20,000 + ₹ 28,000 + ₹ 25,000)	1,73,000
Less: Dividend on shares purchased on Sept.1 (since the dividend pertains to the year ended 31st March, 2019, i.e., the pre-acquisition period)	(4,000)
Cost of 16,000 shares	1,69,000
Cost of 8,000 shares (Average cost basis)	84,500
Sale proceeds (8,000 X ₹14)	1,12,000
Profit on sale	27,500

3. **Value of investment at the end of the year**

   Assuming investment as current investment, closing balance will be valued based on lower of cost or net realizable value.

Here, Net realizable value is ₹13 per share i.e., 8,000 shares x ₹ 13 = ₹ 1,04,000 and cost = 84,500. Therefore, value of investment at the end of the year will be ₹ 84,500.

QUESTION 38 (CA INTER JULY 21 EXAM)(20 MARKS)

Mr. Z has made following transactions during the financial year 2020-21:

Investment 1: 8% Corporate Bonds having face value ₹ 100.

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

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

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

Date	Particulars
01-04-2020	Opening balance 8,000 equity shares at a book value of ₹ 190 per share
01-05-2020	Purchased 7,000 equity shares@ ₹ 230 on cum right basis; Brokerage of 1% was paid in addition.

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

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

You are required to:

(i) Prepare Investment Accounts in the books of Mr. Z for the year 2020-21, assuming that the average cost method is followed.

(ii) Profit and loss Account for the year 2020-21, based on the above information.

(iii) Suggest values at which investment in equity shares should be reclassified in accordance with AS 13.

SOLUTION:

(i) In the books of Mr. Z

Investment in 8% Corporate Bonds Account
For the period 01 April 2020 to 31 March 2021

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

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

Investment in Equity Shares of G Ltd

For the period 1st April 2020 to 31 March 2021

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

Working Notes

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

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

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

No of Bonds sold	24,000
Face value per bond	₹ 100
Face value of the bonds sold	₹ 24,00,000
Interest Rate	8%
Interest Amount	₹ 24,00,000 x 8% x 4.5/12
	= ₹ 722,000

3. Computation of Profit on Sale of Bonds on 15 Feb 2021

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

4. Valuation of Bonds as on 31 March 2021

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

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

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

6. Right Shares

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

7. Computation of Dividend Received on 16 Sept 2020

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

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

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

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

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

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

10. Computation of Amount of Interim Dividend

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

11. Valuation of Shares as on 31 March 2021

Cost of Shares	(15,20,000 + 16,26,100 + 4,83,000 – 42,000) / 23,100 x 16,100
	= 25,00,100
Market Value of Shares	₹ 260 x 16,100 = ₹ 41,86,000
Closing stock of equity shares has been value at ₹ 25,00,100 i.e. cost being lower than its market value.	

(ii)

Profit & Loss Account (Extract)

For the period 01 April 2020 to 31 March 2021

Particulars	Amount (₹)	Particulars	Amount (₹)
To Balance c/d	12,70,600	By Investment in 8% Corporate Bonds Account (Profit on sale of bonds)	1,76,000
		By Investment in 8% 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 – ₹ 25,00,100/16,100 shares – ₹ 155.29

Market Price/Fair Value per share – ₹ 180

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

Note:

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, ₹ 22,500 (67,500X 7/21) will be applied to reduce the carrying amount of investment and ₹ 45,000 will be credited to profit and loss account.

QUESTION 39

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

SOLUTION:

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

QUESTION 40

On 1st April, 20X1, XY Ltd. has 15,000 equity shares of ABC Ltd. at a book value of ₹ 15 per share (nominal value ₹ 10 per share). On 1st June, 20X1, XY Ltd. acquired 5,000

equity shares of ABC Ltd. for ₹ 1,00,000. ABC Ltd. announced a bonus and right issue.

(1) Bonus was declared, at the rate of one equity share for every five shares held, on 1st July 20X1.

(2) Right shares are to be issued to the existing shareholders on 1st September 20X1. The company will issue one right share for every 6 shares at 20% premium. No dividend was payable on these shares.

(3) Dividend for the year ended 31.3.20X1 were declared by ABC Ltd. @ 20%, which was received by XY Ltd. on 31st October 20X1.

XY Ltd.

(i) Took up half the right issue.

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

(iii) Sold half of its shareholdings on 1st January 20X2 at ₹ 16.50 per share. Brokerage being 1%.

You are required to prepare Investment account of XY Ltd. for the year ended 31st March 20X2 assuming the shares are being valued at average cost.

SOLUTION

In the books of XY Ltd.

Investment in equity shares of ABC Ltd. for the year ended 31st March, 20X2

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

Working Notes:

1. **Calculation of no. of bonus shares issued**

$$\text{Bonus Shares} = \frac{15{,}000 \text{ shares} + 5{,}000 \text{ shares}}{5} \times 1 = 4{,}000 \text{ shares}$$

2. **Calculation of right shares subscribed**

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

$$\text{Shares subscribed by XY Ltd.} = \frac{4{,}000}{2} = 2{,}000 \text{ shares}$$

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

3. **Calculation of sale of right entitlement**

2,000 shares x ₹ 8 per share = ₹ 16,000

Amount received from sale of rights will be credited to statement of profit and loss.

4. **Calculation of profit on sale of shares**

Total holding =	15,000 shares original
	5,000 shares purchased
	4,000 shares bonus
	2,000 shares right shares
	26,000 shares

50% of the holdings were sold

i.e. 13,000 shares (26,000 x1/2) were sold.

Cost of total holdings of 26,000 shares (on average basis)

=₹ 2,25,000 + ₹ 1,00,000 + 24,000- ₹ 10,000 = ₹ 3,39,000

Average cost of 13,000 shares would be

$\frac{3,39,000}{26,000}$ = x 13,000 = ₹1,69,500

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

5. **Dividend received on investment held as on 1st April, 20X1**

= 15,000 shares x ₹ 10 x 20%

= ₹ 30,000 will be transferred to Profit and Loss A/c

Dividend received on shares purchased on 1st June, 20X1

= 5,000 shares x ₹ 10 x 20% = ₹ 10,000 will be adjusted to Investment A/c

Note: It is presumed that no dividend is received on bonus shares as bonus shares are declared on 1st July, 20X1 and dividend pertains to the year ended 31.3.20X1.

6. **Calculation of closing value of shares (on average basis) as on 31st March, 20X2**

13,000 × $\frac{3,39,000}{26,000}$ = ₹ 1,69,500

QUESTION 41

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).

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	To 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	To Bank A/c				July 1	By Bank A/c			
1	(W.N.2)	20,000	750	19,600		(W.N.4)	50,000	1,125	50,000
July 1	To 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.	To P&L A/c								
31	(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

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	$\frac{1,18,000}{1,20,000} \times 40,000$	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 42

On 1st April, 20X1, Mr. Vijay had 30,000 Equity shares in X Ltd. at a book value of ₹ 4,50,000 (Face Value ₹ 10 per share). On 22nd June, 20X1, he purchased another 5000 shares of the same company for ₹ 80,000.

The Directors of X Ltd. announced a bonus of equity shares in the ratio of one share for seven shares held on 10th August, 20X1.

On 31st August, 20X1 the Company made a right issue in the ratio of three shares for every eight shares held, on payment of ₹ 15 per share. Due date for the payment was 30th September, 20X1, Mr. Vijay subscribed to 2/3rd of the right shares and sold the remaining of his entitlement to Viru for a consideration of ₹ 2 per share.

On 31st October, 20X1, Vijay received dividends from X Ltd. @ 20% for the year ended 31st March, 20X1. Dividend for the shares acquired by him on 22nd June, 20X1 to be adjusted against the cost of purchase.

On 15th November, 20X1 Vijay sold 20,000 Equity shares at a premium of ₹ 5 per share.

You are required to prepare Investment Account in the books of Mr. Vijay for the year ended 31st March, 20X2 assuming the shares are being valued at average cost.

SOLUTION:

Investment Account in Books of Vijay
(Scrip: Equity Shares in X Ltd.)

		No.	Amount			No.	Amount
			₹				₹
1.4.20X1 22.6.20X1	To Bal b/d To Bank	30,000 5,000	4,50,000 80,000	31.10.20X1	By Bank (dividend on shares acquired on 22.6.20X1)	—	10,000
10.8.20X1	To Bonus	5,000	_				
30.9.20X1	To Bank (Rights Shares)	10,000	1,50,000				
15.11.20X1	To P&L A/c (Profit on sale of shares)		32,000	15.11.20X1	By Bank (Sale of shares)	20,000	3,00,000
				31.3.20X2	By Bal. c/d	30,000	4,02,000
		50,000	7,12,000			50,000	7,12,000

Working Notes:

(1) **Bonus Shares**

= (30,000 + 5,000) / 7 = 5,000 shares

(2) **Right Shares**

$$= \frac{(30{,}000 + 5{,}000 + 5{,}000)}{8} \text{ x } 3 = 15{,}000 \text{ shares}$$

(3) **Rights shares sold**

= 15,000×1/3 = 5,000 shares

(4) **Dividend received**

= 30,000×10×20% = ₹ 60,000 will be taken to P&L statement

(5) **Dividend on shares purchased on 22.6.20X1**

= 5,000×10×20% = ₹ 10,000 is adjusted to Investment A/c

(6) **Profit on sale of 20,000 shares**

= Sales proceeds – Average cost Sales proceeds = ₹ 3,00,000

Average cost = $\frac{(4,50,000 + 80,000 + 1,50,000 - 10,000)}{50,000}$ × 20,000 = ₹ 2,68,000

Profit = ₹ 3,00,000– ₹ 2,68,000= ₹ 32,000.

(7) **Cost of shares on 31.3.20X2**

$\frac{(4,50,000 + 80,000 + 1,50,000 - 10,000)}{50,000}$ × 30, 000 = ₹ 4,02,000

(8) Sale of rights amounting ₹ 10,000 (₹ 2 x 5,000 shares) will not be shown in investment A/c but will directly be taken to P & L statement.

QUESTION 43 (CA INTER DEC. 2021 EXAMS : 5 MARKS)

Mr. Mohan has invested some money in various Mutual funds. Following information in this regard is given:

Mutual Funds	Date of purchase	Purchase cost (₹)	Brokerage Cost (₹)	Stamp duty (₹)	Market value as on 31.03.2021 (₹)
A	01.05.2017	50,000	200	20	48,225
B	05.08.2020	25,000	150	25	24,220
C	01.01.2021	75,000	300	75	78,190
D	07.05.2020	70,000	275	50	65,880

You are required to:

1. Classify his investment in accordance with AS-13 (revised).
2. Value of Investment in mutual fund as on 31.03.2021

SOLUTION :

As per AS 13 "Accounting for Investments", a current investment is an investment that is by its nature readily realizable and is intended to be held for not more than one year from the date on which such investment is made. The carrying amount for current investments is the lower of cost and fair value.

A long-term investment is an investment other than a current investment. Long term investments are usually carried at cost. If there is a decline, other than temporary, in the value of a long-term investment; the carrying amount is reduced to recognize the decline.

Mutual Funds	Classification	Cost (₹)	Market value (₹)	Carrying value (₹)
A	Long-term Investment	50,220	48,225*	50,220
B	Current Investment	25,175	24,220	24,220
C	Current Investment	75,375	78,190	75,375
D	Current Investment	70,325	65,880	65,880
Total				2,15,695

Note: *The reduction in value of Mutual fund A is considered to be temporary. If reduction in Market value is assumed as other than temporary in nature, then the carrying value of ₹48,225 will be considered.

QUESTION 44 (CA INTER DEC. 2021 EXAMS : 10 MARKS)

During the year ended 31st March, 2021, Purple Ltd. entered into the following transactions:

1st April, 2020	Purchased ₹ 4,00,000, 10% Govt. loan 1(interest payable on 30th April and 31st October) at ₹ 70 cum interest.
1st April, 2020	Purchased 6,000 Equity shares of ₹ 5 each in XY Ltd. for ₹ 1,26,000.
1st October, 2020	Sold ₹ 80,000, 10% Govt. loan at ₹75 ex-interest.
15th January, 2021	XY Ltd. made a bonus issued of four equity shares for every three shares held. Purple Ltd. sold all of the bonus shares for ₹ 10 each.
1st March, 2021	Received dividend @ 22% on shares in XY Ltd. for the year ended 31st December, 2020.

Prepare Investment accounts in the books of Purple Ltd.

SOLUTION :

In the books of Purple Ltd.

10% Govt. Loan

[Interest Payable: 30th April & 31st October]

Date	Particulars	Nominal	Interest	Cost	Date	Particulars	Nominal	Interest	Cost
		Value(₹)	(₹)	(₹)			Value (₹)	(₹)	(₹)
1.4.20	To Bank A/c (W.N.1)	4,00,000	16,667	2,63,333	30.4.20	By Bank A/c (4,00,000 x 10% x 6/12)	-	20,000	-

1.10.20	To Profit & Loss A/c (W.N 5)			7,333	1.10.20	By Bank A/c (W.N.2)	80,000	3,333	60,000
					31.10.20	By Bank A/c	-	16,000	-
31.3.21	To Profit & Loss A/c		35,999		31.3.21	By Balance c/d (W.N.3)	3,20,000	13,333	2,10,666
		4,00,000	52,666	2,70,666			4,00,000	52,666	2,70,666

Investment in Equity Shares of XY Ltd. Account (of ₹ 5 each)

Date	Particulars	No.	Dividend	Cost	Date	Particulars	No.	Dividend	Cost
			(₹)	(₹)				(₹)	(₹)
1.4.20	To Bank A/c	6,000		1,26,000	15.1.21	By Bank A/c	8,000	4,950	80,000
15.1.21 15.1.21	To Bonus Issue To Profit & Loss A/c. (W.N.4)	8,000		8,000	1.3.21	By Bank A/c (W.N.6)			1,650
31.3.21	To Profit & Loss A/c		4,950		31.3.21	By Balance c/d	6,000		52,350
		14,000	4,950	1,34,000			14,000	4,950	1,34,000

Working Notes:

1. **Cost of investment purchased on 1st April, 2020**

   4,000, 10% Govt. loan were purchased @ ₹ 70 cum-interest. Total amount paid 4,000 bonds x ₹ 70 = 2,80,000 which includes accrued interest for 5 months, i.e., 1st November, 2020 to 31st March, 2021. Accrued interest will be ₹ 4,00,000 x 10% x 5/12 = ₹ 16,667. Therefore, cost of investment purchased = ₹ 2,80,000 – ₹ 16,667 = ₹ 2,63,333.

2. **Sale of 10% Govt. loan on 1st October, 2020**

   800, 10% Govt. loan were sold@ ₹ 75 ex-interest, i.e., Total amount received = 800 x 75 + accrued interest for 5 months = ₹ 60,000 + ₹ 3333

3. **Cost of 10% Govt. loan on 31.3.2021**

   Cost of 10% Govt. loan on 31.3.2021 will be ₹ 2,63,333 x 3,20,000/4,00,000 = ₹ 2,10,666.

   Interest accrued on 10% Government Loan on 31.3.2021 = ₹ 3,20,000 x 10% x 5/12 = ₹ 13,333

4. **Profit on sale of bonus shares**

   Cost per share after bonus = ₹ 1,26,000/ 14,000 = ₹ 9 (average cost method being followed)

   Profit per share sold (₹ 10 – ₹ 9) = ₹ 1.

Therefore, total profit on sale of 8,000 shares = 8,000 x ₹ 1 = ₹ 8,000.

5. **Profit on sale of 10% Govt. loan**		₹
Sale value	=	60,000
Cost of ₹ 80,000 10% Government Loan = 2,63,333 x 80,000/ 4,00,000	=	52,667
Profit	=	7,333

6. Dividend on equity shares = 6,000 x 5 x 22% = ₹ 6,600 out of which ₹ 1,650 will be treated as capital receipt as it has been received for the period of 3 months during which shares werVe not held.

Note: It has been considered that dividend received relates for the period of 12 months ended 31st Dec., 2020, strictly based on the information, given in the question. Hence, dividend received for the period of 3 months (1st January, 20 to 31st March, 20) has been treated as pre-acquisition.

QUESTION 45 (CA INTER MAY 2022 EXAMS : 5 MARKS)

On 1st April 2021 Ms. Jayshree has 5,000 equity shares of Rama Limited (a listed company) of face value of₹ 10 each. Ms. Jayshree has purchased the above shares at ₹ 15 per share and paid a brokerage of 2% and stamp duty of 1 %.

On 15th May,2021 Ms. Jayshree purchased another 5,000 shares of Rama Limited at ₹ 18 including brokerage and stamp duty.

On 26th August,2021 Rama Limited issued one bonus equity share for every 1 equity share held by the shareholders.

On 23rd October,2021 Rama Limited announced a Right Issue which entitles the holders to subscribe 1 equity share for every 2 equity shares held at ₹ 20 per share. Shareholders can exercise their rights in full or in part. Ms. Jayshree sold 1/4th of entitlement to Mr. Mike for a consideration of ₹ 10 per share and subscribed the rest on 1st November 2021.

Ms. Jayshree also sold 10,000 shares at ₹ 25 per share on 1st November,2021. The shares of Rama Limited were quoted at ₹ 11 per share on 31st March,2022.

You are required to prepare Investment account for Ms. Jayshree for the year ended 31st March 2022.

SOLUTION :

In the books of Ms. Jayshree
Investment Account
(Equity shares in Rama Ltd.)

Date	Particulars	No. of shares	Amount (₹)	Date	Particulars	No. of shares	Amount (₹)
1.4.21	To Balance b/d	5,000	77,250	1.11.21	By Bank A/c	10,000	2,50,000
15.5.21	To Bank A/c	5,000	90,000	31.3.22	By Balance c/d	17,500	1,92,500
26.8.21	To Bonus issue	10,000	---	31.3.22	By Profit & Loss		
1.11.21	To Bank A/c (right shares)	7,500	1,50,000		A/c (loss on valuation)		9,386
1.11.21	To Profit & Loss A/c		1,34,636				
		27,500	4,51,886			27,500	4,51,886

Working Notes:

(1) Profit on sale of shares (average cost basis) on 1.11.21

10,000 shares @ ₹ 25 per share = 2,50,000

Cost of shares sold = [(77,250 + 90,000 + 1,50,000)/27,500 x 10,000]

= ₹ 1,15,364

Profit on sale of shares = ₹ 1,34,636

(2) Value of shares on 31.3.22 [(77,250 + 90,000 + 1,50,000)/27,500 x 17,500]

= ₹ 2,01,886 or ₹ 1,92,500 (17,500 shares at ₹ 11)

Shares will be valued at ₹, 1,92,500 as market value is less than cost.

Note: Average cost basis has been considered for valuation of shares at the year end and for calculation of cost of shares sold in the given answer.

QUESETION 46 (CA INTER NOV. 2022 EXAMS : 5 MARKS)

(i) An unquoted long term investment made in the shares of Rachel Limited is carried in the books of Ziva Limited at a cost of ₹ 1,00,000. The audited financial statements of Rachel Limited received in May,2021 showed that the company had been incurring cash losses with declining market share and the long term investment may not fetch more than ₹ 55,000.

(ii) On 1st December, 2021 Ziva Limited had made an investment of ₹ 5,00,000 in 4,000 Equity Shares of Garry Limited at a price of ₹ 125 per share with an intention to hold it for not more than six months. In the first week of March, 2022, Garry Limited suffered heavy loss due to an earthquake; the loss was not covered by an insurance policy. On 31st March,2022, the shares of Garry Ltd. were traded at a price of ₹ 80 per share on the Stock Exchange.

How would you deal with the above investments in the books of Ziva Limited for the year ended 31st March,2022 as per the provisions of Accounting Standard 13 'Accounting for Investments'?

SOLUTION :

(i) Investments classified as long -term investments should be carried in the financial statements at cost. However, provision for diminution should be made to recognize a decline, other than temporary, in the value of the investments, such reduction being determined and made for each investment individually.

On this basis, the facts of the given case, it would be appropriate to reduce the carrying value of Long-term investments to ₹ 55,000 in the financial statements for the year ended 31st March, 2022.Thus the unquoted investment in the shares of Rachel Ltd. will be valued at ₹ 55,000

The provision for diminution amounting ₹ 45,000 should be made to reduce the carrying amount of the investments.

(ii) Equity Shares in Garry Ltd. will be considered as current investment as intended to hold for not more than six months. As per AS 13, "Accounting for Investments", carrying amount for current investments is the lower of cost and fair value. In respect of current Investments for which as active market exists, market value generally provides the best evidence of fair value.

Since on 31st March,2022, the shares of Garry Limited were trading at a price of ₹ 80 per share on the stock exchange, the equity shares of Garry Ltd. should be carried in the financial statements at realizable value i.e. at ₹ 3,20,000 (4,000 shares @ ₹ 80 per share).The reduction of ₹ 1,80,000 in carrying value of current investment will be charged to the statement of profit and loss for the year ended 31 st March,2022.

QUESTION 47 (CA INTER NOV. 2022 EXAMS : 10 MARKS)

Mr. Saurabh held 10,000 equity shares of BT Limited on 1st April,2021. Nominal value of the shares is ₹ 2 each and their book value is ₹ 7 per share.

- On 4th July,2021 he purchased another 7,500 shares at ₹ 10 each.
- On 31st July 2021 the company announced a Bonus and Right issue.
- Bonus was declared of one share for every five shares held and was received on 5th August,2021.
- Right issue to be issued on 12th September,2021, which entitled the holders to sub-

scribe to additional 2 shares for every 7 shares held at ₹ 2 per share. Shareholders were entitled to transfer their rights in full or part. Mr. Saurabh sold whole of his entitlements to Mr. Nihal at ₹ 1.50 per share.

- Dividend was declared for the year ended 31st March,2021 @ 25% and received by Mr. Saurabh on 19th September 2021.
- On 11th December 2021 Mr. Saurabh sold 7,500 shares at ₹ 8 per share.
- The market price of the shares on 31st March,2022 was ₹ 7 per share.

You are required to prepare the Investment Account of Mr. Saurabh on 31st March,2022 considering the above mentioned points, also state the value of shares held on that date. (Assume investment as current investment)

SOLUTION :

Investment Account in Books of Saurabh

(Script: Equity Shares in BT Ltd.)

		No.	Dividend	Amount			No.	Dividend	Amount
				₹					₹
1.4.21	To Bal b/d	10,000		70,000	19.9.2021	By Bank (dividend on shares acquired on 4.7. 2021)		5,000	3,750
4.7.21	To Bank	7,500		75,000					
5.8.21	To Bonus	3,500		0					
11.12.21	To P&L A / c (Profit on sale of shares)			9,554	11.12.2021	By Bank (Sale of shares)	7,500		60,000
31.3.22	To P&L A/c		5,000		31.3.2022	By Bal. c/d	13,500		90,804
		21,000	5,000	1,54,554			21,000	5,000	1,54,554

Working Notes:

(1) Right Shares = $\frac{((10,000+7,500+3,500))}{7A} \times 2 = 6,000$

Sale of rights amounting ₹ 9,000 (₹ 1.5 x 6,000 shares)

It will not be shown in investment A/c but will directly be taken to P & L statement.

(2) Profit on sale of 7,500 shares

= Sales proceeds – Average cost

Sales proceeds = ₹ 60,000

Average cost = (70,000 + 75,000 – 3,750) /21,000 x 7,500 = ₹ 50,446

Profit = ₹ 60,000 – ₹ 50,446 = ₹ 9,554.

(3) **Value of investments**

Current investments are valued at lower of cost or net realizable value.

Here, cost= (70,000 + 75,000 – 3,750)/ 21,000 X 13,500 = ₹ 90,804

Net realizable value of the shares = ₹ 94,500

Therefore, value of investments will be taken lower of above i.e.₹ 90,804

Note: As question is silent, Average cost basis has been considered for calculation of cost of shares in above solution. Alternatively, FIFO method can also be considered for calculation of cost of shares. An alternative solution is given below based on FIFO method-

Alternative Solution

Investment Account in Books of Saurabh

(Script: Equity Shares in BT Ltd.)

		No.	Dividend	Amount			No.	Dividend	Amount
				₹					₹
1.4.21	To Bal b/d	10,000		70,000	19.9.21	By Bank (dividend on shares acquired on 4.7. 2021)		5,000	3,750
4.7.21	To Bank	7,500		75,000					
5.8.21	To Bonus	3,500		0					
11.12.21	To P&L A/c (Profit on sale of shares)			7,500	11.12.21	By Bank (Sale of shares)	7,500		60,000
31.3.22	To P&L A/c		5,000		31.3.22	By Bal. c/d	13,500		88,750
		21,000		1,52,500			21,000		1,52,500

Working Notes:

(1) Right Shares = $\frac{((10,000+7,500+3,500))}{7A} \times 2 = 6,000$

Sale of rights amounting ₹ 9,000 (₹ 1.5 x 6,000 shares)

It will not be shown in investment A/c but will directly be taken to P & L statement.

(2) **Profit on sale of 7,500 shares**

= Sales proceeds – Cost Sales proceeds = ₹ 60,000

Cost = 7,500 X ₹ 7= ₹ 52,500

Profit = ₹ 60,000 – ₹ 52,500 = ₹ 7,500.

(3) **Value of investments**

Current investments are valued at lower of cost or net realizable value

Here, cost= (2500 X₹7) + (7500 X₹10) -₹3750 = ₹ 88,750

Net realizable value of the shares = ₹ 94,500

Therefore, value of investments will be taken lower of above i.e.₹ 88,750

ACCOUNTING STANDARD 9: Revenue Recognition

QUESTION 1

Sale of goods costing ₹ 54,000 with a profit margin of 10% on selling price is included in the inventory as delivery of goods was postponed at buyer's request.

Advise the company on changes to be effected in the draft financial statements. Give reasons in support of your advice. There is no necessity to discuss disclosure requirements in this regard.

SOLUTION:

AS-9 on "Revenue Recognition", states when to recognize revenue from a transaction involving the sale of goods is that the seller has transferred the property in the goods to the buyer for a consideration". The transfer of property in goods on buyer's request is not in accordance with AS-9. Thus, ₹ 54,000 should not be considered as a part of inventory and it would be considered as sales. So the amount of ₹ 59,400 should be included in sales with correspondence increase in Debtor's balances.

QUESTION 2 (GOOD QUESTION)

The bank has recognized on accrual basis income from dividends on securities and Units of Mutual Funds help by it as at the end of financial year. The dividends on securities and Units of Mutual Funds were declared after the end of financial year.

SOLUTION:

It is not a prudent practice to treat dividend on shares of corporate bodies and unites of mutual funds as income unless these are actually received. Accordingly, income from dividend on shares of corporate bodies and units of mutual funds should be booked on cash basis.

In respect of income from Government securities and bonds and debentures of corporate bodies, where interest rates on these instruments are pre-determined, income could be booked on accrual basis, provided interest in serviced regularly and as such is not in arrears.

Banks may book income from dividend on shares of corporate bodies on accrual basis, provided dividend on the shares has been declared by the corporate bodies on annual general meeting and the owner's right to receive payment is established. This is also in accrual basis is not in order.

QUESTION 3

When can revenue be recognized in case of a transaction of rendering of services?

SOLUTION:

Revenue Recognition- Rendering of Services: Following conditions should be satisfied for recognition of revenue from rendering of services;

(a) Revenue should be recognised either under the completed service contract method or under the proportionate completion method whichever relates the service

(b) No significant uncertainty exists regarding the amount of the consideration that will be derived from rendering the service.

(c) It is not unreasonable to expect ultimate collection.

Proportionate completion method- If performance consists of the execution of more than one act, revenue is recognised proportionately by reference to the performance of each act on the basis of proportionate completion method.

Completed service contract method- If performance consists of the execution of a single act or consist of performance of more than a single act, and the services yet to be performed are very significant in relation to the transaction taken as a whole, revenue is recognised when the sole or final act takes place and the service becomes chargeable on the basis of completed service contract method.

QUESTION 4

When can revenue from Interest, Royalties and Dividends be recognized?

SOLUTION:

Revenue arising from the use by others of enterprise resources yielding interest, royalties and dividends should only be recognised as follows provided no significant uncertainty as to measurability or collectability exists.

Interest- on a time proportion basis taking into account the amount outstanding and rate

Royalties- on an accrual basis in accordance with the terms of the relevant agreement

Dividends- from investment in shares when the owner's right to receive payment is established

QUESTION 5 (VERY GOOD QUESTION)

When do you recognize revenue from sale of goods in following cases?

- Delivery is delayed at buyer's request and buyer takes title and accepts billing

- Delivered subject to conditions- (a) Installation and inspection, (b) On approval (c) Guaranteed sales, (d) Consignment sales, (e) Cash on delivery sales
- Installment payments & delivery on final payment
- Special order and shipments
- Sale/repurchase agreements
- Sales to intermediate parties
- Subscriptions for publications
- Installment sales
- Trade discounts and volume rebates

Revenue Recognition

SOLUTION:

Sale of Goods Delivery is delayed at buyer's request and buyer takes title and accepts billing

Revenue should be recognised notwithstanding that physical delivery has not been completed so long as there is every expectation that delivery will be made. However, the item must be on hand, identified and ready for deliver)- to the buyer at the time the sale is recognised rather than there being simply an intention to acquire or manufacture the goods in time for delivery.

Delivered subject to conditions:

(a) **Installation and inspection** i.e. goods are sold subject to installation, inspection etc. Revenue should normally not be recognised until the customer accepts delivery and installation and inspection are complete. In some cases, however, the installation process may be so simple in nature that it may be appropriate to recognise the sale notwithstanding that installation is not yet completed (e.g. installation of a factory-tested television receiver normally only requires unpacking and connecting of power and antennae).

(b) **On approval**

Revenue should not be recognised 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.

(c) **Guaranteed sales** i.e. delivery is made giving the buyer an unlimited right of return Recognition of revenue in such circumstances will depend on the substance of the agreement. In the case of retail sales offering a guarantee of "money back if not completely satisfied" it may be appropriate to recognise the sale but to make a suitable provision for returns based on previous experience. In other cases, the substance of the agreement may amount to a sale on consignment, in which case it should be treated as indicated below.

(d) **Consignment sales** i.e. a delivery is made whereby the recipient undertakes to sell the goods on behalf of the consignor

Revenue should not be recognised until the goods are sold to a third party.

(e) Cash on delivery sales: Revenue should not be recognised until cash is received by the seller or his agent.

Installment payments and delivery on final payment: Revenue from such sales should not be recognised until goods are delivered. However, when experience indicates that most such sales have been consummated, revenue may be recognised when a significant deposit is received.

Special order and shipments i.e. where payment (or partial payment) is received for goods not presently held in stock e.g. the stock is still to be manufactured or is to be delivered directly to the customer from a third party: Revenue from such sales should not be recognised until goods are manufactured, identified and ready for delivery to the buyer by the third party.

Sale/repurchase agreements i.e. where seller concurrently agrees to repurchase the same goods at a later date: For such transactions that are in substance a financing agreement, the resulting cash inflow is not revenue as defined and should not be recognised as revenue.

Sales to intermediate parties i.e. where goods are sold to distributors, dealers or others for resale: Revenue from such sales can generally be recognised if significant risks of ownership have passed; however in some situations the buyer may in substance be an agent and in such cases the sale should be treated as a consignment sale.

Subscriptions for publications: Revenue received or billed should be deferred and recognisedeither on a straight-line basis over time or, where the items delivered vary in value from period to period, revenue should be based on the sales value of the item delivered in relation to the total sales value of all items covered by the subscription.

Installment sales: When the consideration is receivable in instalments, revenue attributable to the sales price exclusive of interest should be recognised at the date of sale. The interest element should be recognised as revenue, proportionately to the unpaid balance due to the seller.

Trade discounts and volume rebates: 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.

QUESTION 6 (VERY GOOD QUESTION)

When do you recognize revenue from rendering of services in following cases?

- Installation Fees
- Advertising and insurance agency commissions
- Financial service commissions
- Admission fees
- Tuition fees
- Entrance and membership fees

SOLUTION:

Rendering of Services

Installation Fees: In cases where installation fees are other than incidental to the sale of a product, they should be recognisedas revenue only when the equipment is installed and accepted by the customer.

Advertising and insurance agency commissions: Revenue should be recognised when the service is completed. For advertising agencies, media commissions will normally be recognisedwhen the related advertisement or commercial appears before the public and the necessary intimation is received by the agency, as opposed to production commission, which will be recognised when the project is completed. Insurance agency commissions should be recognised on the effective commencement or renewal dates of the related policies.

Financial service commissions: A financial service may be rendered as a single act or may be provided over a period of time. Similarly, charges for such services may be made as a single amount or in stages over the period of the service or the life of the transaction to which it relate.

Admission fees: Revenue from artistic performances, banquets and other special events should be recognised when the event takes place. When a subscription to a number of events is sold, the fee should be allocated to each event on a systematic and rational basis.

Tuition fees: Revenue should be. recognised over the period of instruction.

Entrance and membership fees: Revenue recognition from these sources will depend on the nature of the services being provided. Entrance fee received is generally capitalised. If the membership fee permits only membership and all other services or products are paid for separately, or if there is a separate annual subscription, the fee should be recognised when received. If the membership fee entities the member to services or publications to be provided during the year,_ it should be recognised on a systematic and rational basis having regard to the timing and nature of all services provided.

QUESTION 7

When can revenue be recognized in case of a transaction of sale of goods?

SOLUTION:

Revenue Recognition- Sale of Goods

Revenue from sales should be recognised when all the following conditions are satisfied:

(a) 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 or seller retains no effective control of the goods transferred to a degree usually associated with ownership;

(b) No significant uncertainty exists regarding the amount of the consideration that will be derived from the sale of the goods.

(c) It is not unreasonable to expect ultimate collection.

QUESTION 8

Define revenue and items of revenue, which are dealt with by the AS-9.

SOLUTION:

Revenue is the gross inflow of cash, receivables or other consideration arising in the course of the ordinary activities of an enterprise from the:

- Sale of goods,
- Rendering of services, and
- Use by others of enterprise resources yielding interest, royalties and dividends.

AS-9 deals with the bases for recognition of revenue in the profit and loss account and concerned with the recognition of revenue arising in the course of the ordinary activities from:

- Sale of goods,
- Rendering of services, and
- Use by others of enterprise resources yielding interest, royalties and dividends.

AS-9 does not deal with the following revenue arising from:

- Construction contracts;
- Hire purchase, lease agreements;
- Government grants and other similar subsidies;
- Insurance companies arising from insurance contracts.

QUESTION 9

M/s Moon Ltd. Sold goods worth Rs 6,50,000 to Mr. star asked for a trade discount amounting to Rs 53,000 and same was agreed to by M/s Moon Ltd. The sales was effected and goods were dispatched. On receipt of goods, Mr. Star has found that goods worth ₹ 67,000 are defective. Mr. Star returned defective goods to M/s. Moon Ltd. And made payment due amounting to ₹ 5,30,000. The accountant of M/s Moon ltd. Booked the sale for ₹ 5,30,000. Discuss the connection of the accountant with reference to Accounting Standard. (AS) 9

SOLUTION

Assuming that the discount of ₹ 53000 is decided before or simultaneously at the time when the sales is effected and goods are dIspatched, it is a trade discount. According to appendix to AS-9"Revenue Recognition", trade discounts do not form part of revenue.

Further, since defective goods ₹ 67000 were returned immediately, the sales is said to be revoked with respect to that part and it becomes sales returns. This has to be reduced from sales revenue.

Therefore, initially the REVENUE IS to be recognised at ₹ 597000. Subsequently, the sales returns of ₹ 67000 has to be reduced from sales revenue. Therefore, revenue as per AS-9 is only is 530000.

QUESTION 10

A Ltd. entered into a contract with B Ltd. to dispatch goods valuing Rs 25,000 every month for 4 month upon receipt of entire payment B Ltd. accordingly made the payment of Rs 1,00,000 and A Ltd started dispatching the goods. In third month, due to a natural calamity, B Ltd. requested A Ltd. not to dispatch goods unit further notice through A Ltd. is holding the remaining goods worth Rs 50,000 ready for dispatch. A Ltd. accounted Rs 50,000 as sales and transferred the balance to Advance Received against Sales. Comment upon the treatment of balance amount with reference to the provisions of Accounting Standard 9.

SOLUTION:

Revenue Recognition- Sale of Goods

Revenue from sales should be recognised when all the following conditions are stisfied:

(a) 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 or seller retains no effective control of the goods transferred to a degree usually associated with ownership;

(b) No significant uncertainty exists regarding the amount of the consideration that will be derived from the sale of the goods,

(c) It is not unreasonable to expect ultimate collection.

CONCLUSION:

On the basis of above rules, treatment of A limited is correct because goods are still pending for delivery which is a must condition for recognition of sales. So amount received against pending delivery of goods should be considered as an advance.

QUESTION 11 (STUDY MATERIAL)

The Board of Directors decided on 31.3.20X2 to increase the sale price of certain items retrospectively from 1st January, 20X2. In view of this price revision with effect from 1st January 20X2, the company has to receive ₹ 15 lakhs from its customers in respect of sales made from 1st January, 20X2 to 31st March, 20X2. Accountant cannot make up his mind whether to include ₹ 15 lakhs in the sales for 20X1-20X2.Advise.

SOLUTION:

Price revision was effected during the current accounting period 20X1-20X2. As a result, the company stands to receive ₹ 15 lakhs from its customers in respect of sales made from 1st January, 20X2 to 31st March, 20X2. If the company is able to assess the ultimate collection with reasonable certainty, then additional revenue arising out of the said price revision may be recognized in 20X1-20X2.

QUESTION 12 (STUDY MATERIAL : HOMEWORK)

Y Ltd., used certain resources of X Ltd. In return X Ltd. received ₹ 10 lakhs and ₹ 15 lakhs as interest and royalties respective from Y Ltd. during the year 20X1-X2. You are required to state whether and on what basis these revenues can be recognized by X Ltd.

SOLUTION:

As per AS 9 on Revenue Recognition, revenue arising from the use by others of enterprise resources yielding interest and royalties should only be recognized when no significant uncertainty as to measurability or collectability exists. These revenues are recognized on the following bases:

(i) **Interest:** on a time proportion basis taking into account the amount outstanding and the rate applicable. Therefore X Ltd. should recognize interest revenue of ₹ 10 Lakhs

(ii) **Royalties:** on an accrual basis in accordance with the terms of the relevant agreement. X Ltd. therefore should recognize royalty revenue of ₹ 15 Lakhs.

QUESTION 13 (STUDY MATERIAL : HOMEWORK)

In the year 20X1-X2, XYZ supplied goods on Consignment basis to ABC – a retail outlet worth ₹ 10,00,000. As per the terms, ABC will only pay XYZ for the goods which are sold by them to the third party. Rest of the goods can be returned back to XYZ and ABC will not have any further liability for these goods.

During the year 20X1-X2, ABC has sold goods worth ₹ 5,50,000 only and rest of the goods are still lying in its store which may get sold by next year. Advise XYZ, how much revenue it can recognize in its books for period 20X1-X2.

SOLUTION:

As per AS 9, For consignment risk and rewards are not transferred to the customer on just delivery of the goods and no revenue should be recognized until the goods are sold to a third party. Therefore, XYZ can recognize revenue of ₹ 5,50,000 only.

QUESTION 14 (STUDY MATERIAL : HOMEWORK)

A Ltd. has sold its building for ₹ 50 lakhs to B Ltd. and has also given the possession to B Ltd. The book value of the building is ₹ 30 lakhs. As on 31st March, 20X1, the documentation and legal formalities are pending. The company has not recorded the sale and has shown the amount received as advance. Do you agree with this treatment?

SOLUTION :

A limited should not recognise it as sale because transfer of ownership is yet pending as legal formalities are still pending.. The possession of building has been transferred but ownership has still to be transferred which indicates that Conditions which are prescribed in AS 9 are not fulfilled.

So the treatment which is done by A limited is correct.

QUESTION 15 (STUDY MATERIAL)

The following information of Meghna Ltd. is provided:

(i) Goods of ₹ 60,000 were sold on 20-3-20X2 but at the request of the buyer these were delivered on 10-4-20X2.

(ii) On 15-1-20X2 goods of ₹ 1,50,000 were sent on consignment basis of which 20% of the goods unsold are lying with the consignee as on 31-3-20X2.

(iii) ₹ 1,20,000 worth of goods were sold on approval basis on 1-12-20X1. The period of approval was 3 months after which they were considered sold. Buyer sent approval for 75% goods up to 31-1-20X2 and no approval or disapproval received for the remaining goods till 31-3-20X2.

(iv) Apart from the above, the company has made cash sales of ₹ 7,80,000 (gross). Trade discount of 5% was allowed on the cash sales.

You are required to advise the accountant of Meghna Ltd., with valid reasons, the amount to be recognized as revenue in above cases in the context of AS 9.

SOLUTION :

As per AS 9 "Revenue Recognition", in a transaction involving the sale of goods, performance should be regarded as being achieved when the following conditions are fulfilled:

(i) the seller of goods has transferred to the buyer the property in the goods for a price or all significant risks and rewards of ownership have been transferred to the buyer and the seller retains no effective control of the goods transferred to a degree usually associated with ownership; and

(ii) no significant uncertainty exists regarding the amount of the consideration that will be derived from the sale of the goods.

Case (i)

The sale is complete but delivery has been postponed at buyer's request. The entity should recognize the entire sale of ₹ 60,000 for the year ended 31st March, 20X2.

Case (ii)

20% goods lying unsold with consignee should be treated as closing inventory and sales should be recognized for ₹ 1,20,000 (80% of ₹ 1,50,000). 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 ₹ 1,20,000 as the time period for rejecting the goods had expired.

Case (iv)

Trade discounts given should be deducted in determining revenue. Thus ₹ 39,000 should be deducted from the amount of turnover of ₹ 7,80,000 for the purpose of recognition of revenue. Thus, revenue should be ₹ 7,41,000.

QUESTION 16 (MAY 2019 5 MARKS)

Given below are the following informations of B.S. Ltd.

(i) Goods of ₹ 50,000 were sold on 18-03-2018 but at the request of the buyer these were delivered on 15-04-2018.

(ii) On 13-01-2018 goods of ₹ 1,25,000 are sent on consignment basis of which 20% of the goods unsold are lying with the consignee as on 31-03-2018.

(iii) ₹ 1,00,000 worth of goods were sold on approval basis on 01-12-2017. The period of approval was 3 months after which they were considered sold. Buyer sent approval for 75% goods up to 31-01-2018 and no approval or disapproval received for the remaining goods till 31-03-2018.

You are required to advise the accountant of B.S. Ltd., with valid reasons, the amount to be recognized as revenue for the year ended 31st March, 2018 in above cases in the context of AS-9.

SOLUTION:

Case (i)

The sale is complete but delivery has been postponed at buyer's request. B.S. Ltd. should recognize the entire sale of ₹ 50,000 for the year ended 31st March, 2018.

Case (ii)

In case of consignment sale revenue should not be recognized until the goods are sold to a third party.20% goods lying unsold with consignee should be treated as closing inventory and sales should be recognized for ₹ 1,00,000 (80% of ₹ 1,25,000).

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 ₹ 1,00,000 as the time period for rejecting the goods had expired.

Thus total revenue amounting ₹ 2,50,000 (50,000 + 1,00,000+ 1,00,000) will be recognized for the year ended 31st March, 2018 in the books of B.S. Ltd.

QUESTION 17 (CA INTER NOV 2019 5 MARKS)

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 ₹ 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.

AS 9 (REVENUES)

EXTRA QUESTIONS FOR SELF STUDY

QUESTION 1

A manufacturing company has the following stages of production and sale in manufacturing fine paper rolls:

Date	Activity	Cost to Date (₹)	Net Realizable Value (₹)
15.1.16	Raw Material	1,00,000	80,000
20.1.16	Pulp (WIP 1)	1,20,000	1,20,000
27.1.16	Rough & thick paper (WIP 2)	1,50,000	1,80,000
15.2.16	Fine Paper Rolls	1,80,000	3,50,000
20.2.16	Ready for sale	1,80,000	3,50,000
15.3.16	Sale agreed and invoice raised	2,00,000	3,50,000
02.4.16	Delivered and paid for	2,00,000	3,50,000

Explain the stage on which you think revenue will be generated and calculate how much would be net profit for year ending 31.3.16 on this product as per AS 9.

SOLUTION

According to AS 9 "Revenue Recognition", in a transaction involving the sale of goods, performance should be regarded as being achieved when the following conditions have been fulfilled:

(i) the seller of goods has transferred to the buyer the property in the goods for a price or all significant risks and rewards of ownership have been transferred to the buyer and the seller retains no effective control of the goods transferred to a degree usually associated with ownership; and

(ii) no significant uncertainty exists regarding the amount of the consideration that will be derived from the sale of the goods.

Thus, sales will be recognized only when following two conditions are satisfied:

(i) The sale value is fixed and determinable.

(ii) Property of the goods is transferred to the customer.

Both these conditions are satisfied only on 15.3.2016 when sales are agreed upon at a price and goods are allocated for delivery purpose through invoice. The amount of net profit ₹ 1,50,000 (3,50,000 – 2,00,000) would be recognized in the books for the year ending 31st March, 2016.

QUESTION 2

Fashion Limited is engaged in manufacturing of readymade garments. They provide you the following information on 31st March, 2017:

(i) On 15th January, 2017 garments worth ₹ 4,00,000 were sent to Anand on consignment basis of which 25% garments unsold were lying with Anand as on 31st March, 2017.

(ii) Garments worth ₹ 1,95,000 were sold to Shine boutique on 25th March, 2017 but at the request of Shine Boutique, these were delivered on 15th April, 2017.

(iii) On 1st November, 2016 garments worth ₹ 2,50,000 were sold on approval basis. The period of approval was 4 months after which they were considered sold. Buyer sent approval for 75% goods up to 31st December, 2016 and no approval or disapproval received for the remaining goods till 31st March, 2017.

You are required to advise the accountant of Fashion Limited, the amount to be recognised as revenue in above cases in the context of AS 9

SOLUTION

As per AS 9 "Revenue Recognition", in a transaction involving the sale of goods, performance should be regarded as being achieved when the following conditions are fulfilled:

(i) the seller of goods has transferred to the buyer the property in the goods for a price or all significant risks and rewards of ownership have been transferred to the buyer and the seller retains no effective control of the goods transferred to a degree usually associated with ownership; and

(ii) no significant uncertainty exists regarding the amount of the consideration that will be derived from the sale of the goods.

Case (i): 25% goods lying unsold with consignee should be treated as closing inventory and sales should be recognized for ₹ 3,00,000 (75% of ₹ 4,00,000) for the year ended on 31.3.17. In case of consignment sale revenue should not be recognized until the goods are sold to a third party.

Case (ii): The sale is complete but delivery has been postponed at buyer's request. Fashion Ltd. should recognize the entire sale of ₹1,95,000 for the year ended 31st March, 2017.

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 ₹ 2,50,000 as the time period for rejecting the goods had expired.

Thus total revenue amounting ₹ 7,45,000 (3,00,000+1,95,000+2,50,000) will be recognized for the year ended 31st March, 2017 in the books of Fashion Ltd.

QUESTION 3

Raj Ltd. entered into an agreement with Heena Ltd. to dispatch goods valuing ₹ 5,00,000 every month for next 6 months on receipt of entire payment. Heena Ltd. accordingly made the entire payment of ₹ 30,00,000 and Raj Ltd. started dispatching the goods. In fourth month, due to fire in premise of Heena Ltd., Heena Ltd. requested to Raj Ltd. not to dispatch goods worth ₹ 15,00,000 ready for dispatch. Raj Ltd. accounted ₹ 15,00,000 as sales and transferred the balance to Advance received against Sales account.

Comment upon the above treatment by Raj Ltd. with reference to the provision of AS-9.

SOLUTION

As per AS 9 "Revenue Recognition", in a transaction involving the sale of goods, performance should be regarded as being achieved when the following conditions are fulfilled:

(i) the seller of goods has transferred to the buyer the property in the goods for a price or all significant risks and rewards of ownership have been transferred to the buyer and the seller retains no effective control of the goods transferred to a degree usually associated with ownership; and

(ii) no significant uncertainty exists regarding the amount of the consideration that will be derived from the sale of the goods.

In the given case, transfer of property in goods results in or coincides with the transfer of significant risks and rewards of ownership to the buyer. Also, the sale price has been recovered by the seller. Hence, the sale is complete but delivery has been postponed at buyer's request. Raj Ltd. should recognize the entire sale of ₹ 30,00,000 (₹ 5,00,000 x 6) and no part of the same is to be treated as Advance Received against Sales.

QUESTION 4

Fashion Limited is engaged in manufacturing of readymade garments. They provide you the following information on 31st March, 2019:

(i) On 15th January, 2019 garments worth ₹ 4,00,000 were sent to Anand on consignment basis of which 25% garments unsold were lying with Anand as on 31st March, 2019.

(ii) Garments worth ₹ 1,95,000 were sold to Shine boutique on 25th March, 2019 but at the request of Shine Boutique, these were delivered on 15th April, 2019.

You are required to advise the accountant of Fashion Limited, the amount to be recognised as revenue in above cases in the context of AS 9 .

SOLUTION

As per AS 9 "Revenue Recognition", in a transaction involving the sale of goods, performance should be regarded as being achieved when the following conditions are fulfilled:

(i) the seller of goods has transferred to the buyer the property in the goods for a price or all significant risks and rewards of ownership have been transferred to the buyer and the seller retains no effective control of the goods transferred to a degree usually associated with ownership; and

(ii) no significant uncertainty exists regarding the amount of the consideration that will be derived from the sale of the goods.

Case (i): 25% goods lying unsold with consignee should be treated as closing inventory and sales should be recognized for ₹ 3,00,000 (75% of ₹ 4,00,000) for the year ended on 31.3.19. In case of consignment sale revenue should not be recognized until the goods are sold to a third party.

Case (ii): The sale is complete but delivery has been postponed at buyer's request. Fashion Ltd. should recognize the entire sale of ₹1,95,000 for the year ended 31st March, 2019.

QUESTION 5

(a) How will you recognize revenue in the following cases:

1. Installation Fees;
2. Advertising and insurance agency commissions;
3. Subscriptions for publications.

(b) Shipra Ltd., has been successful jewellers for the past 100 years and sales are against cash only (returns are negligible). The company also diversified into apparels. A young senior executive was put in charge of Apparels business and sales increased 5 times. One of the conditions for sales is that dealers can return the unsold stocks within one month of the end of season. Sales return for the year was 25% of sales. Suggest a suitable Revenue Recognition Policy, with reference to AS 9.

SOLUTION

(a) Installation Fees: In cases where installation fees are other than incidental to the sale of a product, they should be recognized as revenue only when the equipment is installed and accepted by the customer.

Advertising and insurance agency commissions: Revenue should be recognized when the service is completed. For advertising agencies, media commissions will normally be recognized when the related advertisement or commercial appears before the public and the necessary intimation is received by the agency, as opposed to production commission, which will be recognized when the project is completed. Insurance agency commissions should be recognized on the effective commencement or renewal dates of the related policies.

Subscription for publications: Revenue received or billed should be deferred and recognized either on a straight-line basis over time or, where the items delivered vary in value from period to period, revenue should be based on the sales value of the item delivered in relation to the total sales value of all items covered by the subscription.

(b) As per AS 9 "Revenue recognition", revenue recognition is mainly concerned with the timing of recognition of revenue in statement of profit and loss of an enterprise. The amount of revenue arising on a transaction is usually determined by the agreement between the parties involved in the transaction. When uncertainties exist regarding the determination of the amount, or its associated costs, these uncertainties may influence the timing of revenue recognition.

Effect of Uncertainty- In the case of the jewellery business the company is selling for cash and returns are negligible. Hence, revenue can be recognized on sales. On the other hand, in Apparels Industry, the dealers have a right to return the unsold goods within one month of the end of the season. In this case, the company is bearing the risk of sales return and therefore, the company should not recognize the revenue to the extent of 25% of its sales. The company may disclose suitable revenue recognition policy in its financial statements separately for both Jewellery and Apparels business.

QUESTION 6

(a) An infrastructure company has constructed a mall and entered into agreement with tenants towards license fee (monthly rental) and variable license fee, a percentage on the turnover of the tenant (on an annual basis). Chief Financial Officer of the company wants to account/recognize license fee as income for 12 months during current year and variable license fee as income during next year, since invoice is raised in the subsequent year. Comment whether the treatment desired by the CFO is correct or not.

(b) Indicate in each case whether revenue can be recognized and when it will be recognized as per AS 9.

(1) Trade discount and volume rebate received.

(2) Where goods are sold to distributors or others for resale.

(3) Where seller concurrently agrees to repurchase the same goods at a later date.

(4) Insurance agency commission for rendering services.

SOLUTION

(a) AS 9 on Revenue Recognition, is mainly concerned with the timing of recognition of revenue in the Statement of Profit and Loss of an enterprise. The amount of revenue arising on a transaction is usually determined by agreement between the parties involved in the transaction. However, when uncertainties exist regarding the determination of the amount, or its associated costs, these uncertainties may influence the timing of revenue recognition. Further, as per accrual concept, revenue should be recognized as and when it is accrued i.e. recorded in the financial statements of the periods to which they relate. In the present case, monthly rental towards license fee and variable license fee as a percentage on the turnover of the tenant (though on annual basis) is the income related to common financial year.

Therefore, recognizing the fee as revenue cannot be deferred simply because the invoice is raised in subsequent period. Hence it should be recognized in the financial year of accrual. Therefore, the contention of the Chief Financial Officer is not in accordance with AS 9.

(b) (1) Trade discounts and volume rebates received are not encompassed within the definition of revenue, since they represent a reduction of cost. Trade discounts and volume rebates given should be deducted in determining revenue.

(2) When goods are sold to distributor or others, revenue from such sales can be recognized if significant risks of ownership have passed; however, in some situations the buyer may in substance be an agent and in such cases the sale should be treated as a consignment sale.

(3) For transactions, where seller concurrently agrees to repurchase the same goods at a later date that are in substance a financing agreement, the resulting cash inflow is not revenue as defined and should not be recognized as revenue.

(4) Insurance agency commissions should be recognized on the effective commencement or renewal dates of the related policies.

QUESTION 7

When revenue will be recognized in the following situation:

(i) Where the purchaser makes a series of installment payments to the seller and the seller deliver the goods only when the final payment is received.

(ii) Where seller concurrently agrees to repurchase the same goods at a later date.

(iii) Where goods are sold to distributors, dealers or others for resale.

(iv) Commissions on service rendered as agent on insurance business.

SOLUTION

(i) Revenue from sales where the purchaser makes a series of instalment payments to the seller, and the seller delivers the goods only when the final payment is received, should not be recognised until goods are delivered. However, when experience indicates that most such sales have been consummated, revenue may be recognised when a significant deposit is received.

(ii) For sale where seller concurrently agrees to repurchase the same goods at a later date, such transactions are in substance a financing agreement. In such a situation, the resulting cash inflow should not be recognised as revenue.

(iii) Revenue from sales of goods to distributors, dealers or others for resale can generally be recognised if significant risks of ownership have passed. However, in some situations the buyer may in substance be an agent and in such cases the sale should be treated as a consignment sale.

(iv) Commissions on service rendered as agent on insurance business should be recognised as revenue when the service is completed. Insurance agency commissions should be recognised on the effective commencement or renewal dates of the related policies.

QUESTION 8

Old Era Publication Publishes a popular monthly magazine on 15th of every month. The publication sells the advertising space on terms of 90% payable in advance and the balance 10% payable within 30 days of release of the publication. The space for March 2020 issue of the magazine was sold in the month of February, 2020. The magazine was published as per schedule on 15th of the month. The amount of ₹ 2,70,000 has been received upto 31st March, 2020 and ₹ 30,000 was received on 10th April, 2020 for advertisement published in the March issue of the publication.

Please advise the accountant the amount of revenue to be recognized in the context of the provisions of AS 9 'Revenue Recognition' during the year ending on 31 st March, 2020.

SOLUTION

Definition: As per 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.

Analysis of given case: 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 appeared for public and hence revenue is recognized on that date. In this case, it is 15.03.2020, the date of publication of the magazine.

Accounting treatment for given situation: Hence, ₹ 3,00,000 (₹ 2,70,000 + ₹ 30,000) is recognized as income in March, 2020. The terms of payment are not relevant for considering the date on which revenue is to be recognized. ₹ 30,000 is treated as amount due from advertisers as on 31.03.2020 and ₹ 2,70,000 will be treated as payment received against the sale.

QUESTION 9

Fashion Limited is engaged in manufacturing of readymade garments. They provide you the following information on 31st March, 2021:

(i) On 15th January, 2021 garments worth ₹ 4,00,000 were sent to Anand on consignment basis of which 25% garments unsold were lying with Anand as on 31st March, 2021.

(ii) Garments worth ₹ 1,95,000 were sold to Shine boutique on 25th March, 2021 but at the request of Shine Boutique, these were delivered on 15th April, 2021.

(iii) On 1st November, 2020 garments worth ₹ 2,50,000 were sold on approval basis. The period of approval was 4 months after which they were considered sold. Buyer sent approval for 75% goods up to 31st December, 2020 and no approval or disapproval received for the remaining goods till 31st March, 2021.

You are required to advise the accountant of Fashion Limited, the amount to be recognised as revenue in above cases in the context of AS 9.

SOLUTION

As per AS 9 "Revenue Recognition", in a transaction involving the sale of goods, performance should be regarded as being achieved when the following conditions are fulfilled:

(i) the seller of goods has transferred to the buyer the property in the goods for a price or all significant risks and rewards of ownership have been transferred to the buyer and the seller retains no effective control of the goods transferred to a degree usually associated with ownership; and

(ii) no significant uncertainty exists regarding the amount of the consideration that will be derived from the sale of the goods.

Case (i): 25% goods lying unsold with consignee should be treated as closing inventory and sales should be recognized for ₹ 3,00,000 (75% of ₹ 4,00,000) for the year ended on 31.3.21. In case of consignment sale revenue should not be recognized until the goods are sold to a third party.

Case (ii): The sale is complete but delivery has been postponed at buyer's request. Fashion Ltd. should recognize the entire sale of ₹1,95,000 for the year ended 31st March, 2021.

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 ₹ 2,50,000 as the time period for rejecting the goods had expired.

Thus total revenue amounting ₹ 7,45,000 (3,00,000 + 1,95,000 + 2,50,000) will be recognized for the year ended 31st March, 2021 in the books of Fashion Ltd.

QUESTION 10

New Era Publications publishes a monthly magazine on 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 2020 issue was made in February 2020. The magazine was published on its scheduled date. It received ₹ 2,40,000 on 10.3.2020 and ₹ 60,000 on 10.4.2020 for the March, 2020 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 31.3.2020. What will be the treatment if the publication is delayed till 2.4.2020?

SOLUTION

As per 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 as the service is performed, 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 published and hence revenue is recognized on that date. In this case, 15.03.2020 is the date of publication of the magazine. Hence, ₹ 3,00,000 (₹ 2,40,000 + ₹ 60,000) is recognized as income in March, 2020. The terms of payment are not relevant for considering the date on which revenue is to be recognized.

Since, the revenue of ₹ 3,00,000 will be recognised in the March, 2020, ₹ 60,000 will be treated as amount due from advertisers as on 31.03.2020 and ₹ 2,40,000 will be treated as payment received against the sale. However, if the publication is delayed till 02.04.2020 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 in the year ended 31.03. 2020 after the magazine is published on 02.04.2020. The amount received from sale of advertising space on 10.03.2020 of ₹ 2,40,000 will be considered as an advance from advertisers as on 31.03.2020.

QUESTION 11 (CA INTER DEC. 2021 EXAMS : 5 MARKS)

Given the following information of Rainbow Ltd.

(i) On 15th November, goods worth ₹ 5,00,000 were sold on approval basis. The period of approval was 4 months after which they were considered sold. Buyer sent approval for 75% goods sold upto 31st January and no approval or disapproval received for the remaining goods till 31st March.

(ii) On 31st March, goods worth ₹ 2,40,000 were sold to Bright Ltd. but due to refurnishing of their show-room being underway, on their request, goods were delivered on 10th April.

(iii) Rainbow Ltd. supplied goods worth ₹ 6,00,000 to Shyam Ltd. and concurrently agrees to re-purchase the same goods on 14th April.

(iv) Dew Ltd, used certain assets of Rainbow Ltd. Rainbow Ltd. received ₹ 7.5 lakhs and ₹ 12 as interest and royalties respectively from Dew Ltd. during the year 2020 -21.

(v) On 25th December, goods of ₹ 4,00,000 were sent on consignment basis of which 40% of the goods unsold are lying with the consignee at the year-end on 31st March.

In each of the above cases, you are required to advise, with valid reasons, the amount to be recognized as revenue under the provisions of AS-9.

SOLUTION :

(i) As per AS 9 "Revenue Recognition", 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 ₹ 5,00,000 as the time period for rejecting the goods had expired.

(ii) The sale is complete but delivery has been postponed at buyer's request. The entity should recognize the entire sale of ₹ 2,40,000 for the year ended 31st March.

(iii) Sale/repurchase agreements i.e. where seller concurrently agrees to repurchase the same goods at a later date, such transactions that are in substance a financing agreement, the resulting cash inflow is not revenue as defined and should not be recognized as revenue. Hence no revenue to be recognized in the given case.

(iv) Revenue arising from the use by others of enterprise resources yielding interest and royalty should be recognized when no significant uncertainty as to measurability or collectability exists. The interest should be recognized on time proportion basis taking into account the amount outstanding and rate applicable. The royalty should be recognized on accrual basis in accordance with the terms of relevant agreement.

(v) 40% goods lying unsold with consignee should be treated as closing inventory and sales should be recognized for ₹ 2,40,000 (60% of ₹ 4,00,000). In case of consignment sale revenue should not be recognized until the goods are sold to a third party.

QUESTION 12 (CA INTER NOV. 2022 EXAMS : 5 MAKRS)

Indicate in each case whether revenue can be recognized and when it will be recognized as per AS-9.

(i) Delivery is delayed at buyer's request but buyer takes title and accepts billing.

(ii) Instalment Sales.

(iii) Trade discounts and volume rebates.

(iv) Insurance agency commission for rendering services.

(v) Advertising commission.

SOLUTION :

(i) **Delivery is delayed at buyer's request and buyer takes title and accepts billing** : Revenue should be recognized notwithstanding that physical delivery has not been completed so long as there is every expectation that delivery will be made. However, the item must be on hand, identified and ready for delivery to the buyer at the time the sale is recognized rather than there being simply an intention to acquire or manufacture the goods in time for delivery.

(ii) **Instalment sales:** When the consideration is receivable in instalments, revenue attributable to the sales price exclusive of interest should be recognized at the date of sale. The interest element should be recognized as revenue, proportionately to the unpaid balance due to the seller.

(iii) **Trade discounts and volume rebates:** 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.

(iv) **Insurance agency commissions for rendering services:** Insurance agency commissions should be recognized on the effective commencement or renewal dates of the related policies.

(v) **Advertising commission:** Revenue should be recognized when the service is completed. For advertising agencies, media commissions will normally be recognized when the related advertisement or commercial appears before the public and the necessary intimation is received by the agency, as opposed to production commission, which will be recognized when the project is completed.

ACCOUNTING STANDARD 11
FOREIGN EXCHANGE TRANSACTIONS

QUESTION NO 1

Compute the Loss/Gain for the financial year ending 31st March 20X1 and 20X2 from the following:-

Raw Materials imported on 1st Jan.20X1 USD 10,000	Rate of Exchange ₹55 Per USD
Financial Year ending on 31st March 20X1	Rate of Exchange ₹ 54 per USD
Date of Actual Payment 7th July 20X1	Rate of Exchange ₹ 53 Per USD

The Chief Accountant of Company passed an entry on 31st March 20X1, adjusting the cost of Raw Material Consumed for the difference between ₹55 and ₹ 53 per USD. Discuss whether this treatment is justified.

SOLUTION

The Raw Material Purchase should be recorded at the Transaction Rate, i.e. USD = ₹55 = Rs 5,50,000. The treatment of Exchange Differences will be as under:-

Purchase of Goods for 10,000 USD	**Financial Year Ending**	**Payment to Supplier**
Transaction Date 1st Jan.20X1	Balance Sheet Date 31st March	Settlement Date 7th July 20X1
USD = ₹ 55.00	USD = ₹ 54.00	USD = ₹ 53.00
Exchange Diff. = ₹1.00 Per USD (Gain) (due to Reporting) i.e.₹10,000 Credited to P&L A/c. for the year ending 31st March 20X1		Exchange Diff. = ₹1.00 Per USD (Gain) (due to Settlement) i.e. ₹ 10,000 Credited to P&L A/c. in next FY i.e. after 31st March 20X1

Conclusion:

For the year ended 31st March 20X1, the gain of ₹ 10,000 should be separately credited to P&L A/c. as an Exchange Difference and disclosed as required under AS-11, and Schedule III which requires specific disclosure of Net Gain/Loss on Foreign Currency Transaction and Translation. It should not be adjusted to the Cost of Materials Consumed.

QUESTION NO 2

Rudra Ltd. exported goods for USD 2,00,000 in February (Exchange Rate ₹ 54.38). The amount was received in June (Exchange Rate ₹ 54.43). The Company closes its books of accounts on 31st March every year. The Exchange Rate on 31st March current year was ₹ 54.50. Find out the Exchange Fluctuation Gain/Loss on the Balance Sheet date, and on the date of receipt.

SOLUTION

Export of Goods USD 2,00,000	Financial Year Ending	Receipt from Customer
Transaction Date=February	Balance Sheet Date= March	Settlement Date= June
USD = ₹ 54.38	USD = ₹ 54.50	USD = ₹ 54.43
Exchange Diff. = ₹0.12 Per USD (Gain) (due to Reporting) i.e.₹24,000 Credited to P&L A/c. for the year ending 31st March	Exchange Diff. = ₹0.07 Per USD (Loss) (due to Settlement) i.e. ₹ 14,000 Debited to P&L A/c. in next FY i.e. after 31st March	

QUESTION NO 3

Ambikapati Ltd. imported certain stock worth USD 60,000 on 30th June when 1 USD = ₹ 54.00. The payment is made on 31st December when 1 USD = ₹55.40. The Stock is in hand and lying unsold as on 30th September when the Company closes its accounts. Give Journal Entries under AS-11, if the rate on the Balance Sheet date was 1 USD = ₹ 53.85.

SOLUTION

Date	Particulars	Dr.(₹)	Cr. (₹)
30th June (Transaction Date)	Purchases A/c. Dr. To Vendor/Foreign Supplier A/c. (Being import of raw materials, recorded at spot rate, i.e. USD 60,000x ₹54.00)	32,40,000	32,40,000

30th Sept. (FY end)	Vendor/Foreign Supplier A/c. Dr. To Profit and Loss A/c. (Exchange Rate Difference) (Being translation of payable, i.e. monetary item at the Closing Rate and recognition of gain due to exchange difference (60,000 x (54.00 – 53.85)	9,000	 9,000
30th Sept. (FY end)	Closing stock A/c. Dr. To Trading A/c. (Being Stock, non-monetary item, carried at Fair Value, presumed equal to ₹32.40 Lakhs, i.e. cost)	32,40,000	 32,40,000
Next Fy 31st Dec. (Settlement Date)	Vendor/Foreign Supplier A/c. Dr. Profit & Loss A/c. (Exch. Rate Diff.) Dr. To Bank A/c. (Being payment made to Vendor at ₹55.40 x USD 60,000, the difference due to settlement (₹ 53.85 – ₹55.40) x USD 60,000, being loss transferred to P&L A/c.)	32,31,000 93,000	 33,24,000

QUESTION NO 4

Tejas Ltd. borrowed US $ 5,00,000 on 1st Jan. 2013 which will be repaid (settled) as on 30th June 2013. The Company prepares its Financial Statements ending on 31st March 2013. Assume that Exchange Rate between Reporting Currency (Rupee) and Foreign Currency (US $) on different dates are as under:-

1st Jan. 2013 : 1 US $ = ₹ 54.00 31st March 2013 30th June 2013
1 US $ = ₹54.50 1 US $ = ₹54.75

(a) Calculate the Borrowing in reporting currency to be recognised in the books on above mentioned dates. Also show the Journal Entries for the same.

(b) If Borrowings was repaid (settled) on 28th Feb. 2013 (Take Exchange Rate 1 US $ = ₹ 54.20) what entry should be passed in such case?

SOLUTION

	Date	Particulars	Dr.(₹)	Cr. (₹)
1.	1 Jan. 2013	Bank A/c. Dr. To Foreign Currency Loan Borrowing (5,00,000 USD at 54) (Being Foreign Currency Loan at 54 per USD, spot rate)	2,70,00,000	2,70,00,000
2.	31 Mar 2013	Profit & Loss A/c. (Exchange Rate Diff.) (5,00,000 x (54.50 – 54) Dr. To Foreign Currency Loan Borrowings (Being Foreign Currency Monetary Item, i.e. Loan reported using Closing Rate of ₹54.50), Carrying Amount of Loan = ₹272,50,000, difference being loss due to reporting difference, written off to P&L)	2,50,000	2,50,000
3A.	30 Jun 2013	Foreign Currency Loan Borrowings Dr. Profit & Loss A/c. (Exchange Rate Difference) (5,00,000 x (54.75 – 54.50)Dr To Bank A/c. (5,00,000 x 54.75) (Being Foreign Currency Loan settled at 54.75 per USD, difference being exchanged loss on settlement, written off to P&L A/c.)	2,72,50,000 1,25,000	2,73,75,000
		If Loan repaid (settled) on 28th Feb.2013:		
3B.	28 Feb 2013	Foreign Currency Loan Borrowings Dr. Profit & Loss A/c. (Exchange Rate Difference) (5,00,000 x (54.20 – 54.00)Dr (Being Foreign Currency Loan settled at 54.20 per USD, difference being exchanged loss on settlement, written off to P&L A/c.)	2,70,00,000 1,00,000	2,71,00,000

QUESTION NO 5

Amaresh bought a Forward Contract for three months of USD 1,00,000 on 1st December 20X1 at 1 USD = ₹ 52.10 when the Exchange Rate was 1 USD = ₹52.02. On 31st December 20X1, when he closed his books, the Exchange Rate was 1 USD = ₹ 52.15. On 31st January 20X2, he decided to sell the Contract at ₹52.18 per Dollar. Show how the profits from the Contract will be recognized in the books. Give the full accounting treatment assuming that the above transaction is on 'non-speculative basis".

Also discuss the accounting treatment, if the above transaction is on "speculative basis", on the assumption that on 31st December 20X2, the 2 months Forward Rate is 1 USD = ₹ 53.

SOLUTION

Situation A : If the above Forward Contract has been entered on "non-speculative" basis.

S.No.	Particulars	Dr.(₹)	Cr. (₹)
1st Dec. 20X1	Foreign Currency Receivable A/c.(1,00,000 USD x ₹52.02 Spot Rate) Dr. Forward Contract Deferred Premium A/c. (1,00,000 USD x (₹52.10 – ₹ 52.02) Dr. To Forward Contract Payable A/c. (1,00,000 USD x ₹52.10 Fwrd Rate) (Being 3 months Forward Contract entered into for 1,00,000 USD)	52,02,000 8,000	 52,10,000
31st Dec. 20X1	Foreign Currency Receivable A/c. Dr. (1,00,000 USD x (₹52.15-₹52.02) To Profit and Loss A/c. (Being re-statement of FC Receivable to Reporting Date Rate, gain adjusted)	13,000	 13,000
31st Dec. 20X1	Profit and Loss A/c. Dr. To Forward Contract Deferred Premium A/c. (Being the amortization of Forward Contract Premium ₹ 8,000 for 3 months, now transferred to P&L proportionately for 1 month period)	2,667	 2,667

31st Jan. 20X2	Forward Contract Payable A/c. Dr. Bank A/c. (1,00,000 USD x Dr. (₹52.18-₹52.10) To Foreign Currency Receivable A/c. To Profit and Loss A/c. (difference Gain adjusted) (Being settlement of Forward Contract)	52,10,000 8,000	 52,15,000 3,000
31st Jan. 20X2	Profit and Loss A/c. Dr. To Forward Contract Deferred Premium A/c. (Being the amortization of balance Forward Contract Premium)	5,333	 5,333

(STUDENTS ARE ADVISED TO PASS ENTRIES AS WE PASSED IN CLASS: CA PARVEEN JINDAL)

Situation B: If the above Forward Contract has been entered on **"speculative"** basis.

S.No.	Particulars	Dr.(₹)	Cr. (₹)
31st Dec. 20X1	Foreign Contract Asset Receivable A/c.(1,00,000 USD x ₹53.00-₹52.10) Dr. To Profit and Loss A/c. (Being adjustment of difference between Contract Forward Rate and B/s Date Rate of Forward Contract for remaining maturity period, Gain credited to P&L)	90,000	 90,000
31st Jan. 20X2	Profit and Loss A/c. (balancing figure) Dr. Bank A/c. (1,00,000 USD x (₹52.18 – ₹52.10) To Forward Contract Asset Rec'ble A/c. (reversal of B/s recognised amt) (Being settlement of Forward Contract, loss adjusted to P&L A/c)	82,000 8,000	 90,000

QUESTION NO 6

On 1st February 2013, an Indian Company sold goods to an American Company at an Invoice Price of USD 20,000 when the Spot Market Rate was 1 USD = ₹54.10. Payment was to be made in three months time, namely by 1st May 2013.

To avoid the risk of Foreign Exchange fluctuations, the Indian Exporter acquired a Forward Contract to sell USD 20,000 at ₹ 53.90 per USD on 1st May 2013.

The Indian Company's accounting year ended on 31st March 2013, and the Spot Rate on this date was ₹ 53.20 per USD. The Spot Rate on 1st May 2013, the date by which the money was due from the American Buyer, was ₹56 per USD.

Show the accounting entries in the books sof the Indian Exporter at the relevant period of time. .

SOLUTION

Journal Entries in the books of Indian Exporter (assumed as SME)

S.No.	Particulars	Dr.(₹)	Cr. (₹)
01.02.13	Sundry Debtors (American Company) A/c. Dr.	10,82,000	
	To Sales A/c.		10,82,000
	(Being Sales recorded at ₹10,82,000 (USD 20,000 x ₹ 54.10)		
01.02.13	Forward (₹) Contract Receivable A/c. Dr.	10,78,000	
	(USD 20,000 x ₹ 53.90)		
	Deferred Discount A/c. Dr.	4,000	
	(USD 20,000 x ₹ 0.20)		
	To Forward ($) Contract Payable A/c.		10,82,000
	(USD 20,000 x ₹ 54.10)		
	(Being Translation Loss USD 20,000 x (₹54.10-₹53.20) by re-statement of Debtors, Difference between Rates on Date of Transaction and Reporting Date)		
31.03.13	Profit & Loss A/c. Dr.	18,000	
	To Sundry Debtors (American Company) A/c.		18,000
	(Being Translation Loss USD 20,000 x (₹54.10-₹53.20) by re-statement of Debtors, Difference between Rates on Date of Transaction and Reporting Date)		

31.03.13	Forward ($) Contract Payable A/c. Dr. To Profit and Loss A/c. (Being Translation Loss USD 20,000 x (₹54.10-₹53.20) as less Rupees becoming payable to Exchange Dealer based on Spot Rate at year end)	18,000	 18,000
31.03.13	Discount A/c. Dr. To Deferred Discount A/c. (Being proportionate discount (2/3rd of ₹4,000) charged as Discount Expense)	2,666	 2,666
01.05.13	Bank A/c. (USD 20,000 x 56,000) Dr. To Sundry Debtors A/c.(USD 20,000x₹53.20) To Profit and Loss A/c.(USD 20,000ax₹2.80) (Being actual receipt of money from the Buyer recorded)	11,20,000	 10,64,000 56,000
01.05.13	Forward ($) Contract Payable A/c. Dr. (USD 20,000 x ₹ 53.20) Profit and Loss A/c. (USD 20,000 x ₹2.80) To Bank A/c. (USD 20,000x₹ 56.00) (Being delivery of 20,000 USD against Forward Contract at Spot Rate on 1st May)	10,64,000 56,000	 11,20,000
01.05.13	Bank A/c. Dr. To Forward (₹) Contract Receivable A/c. (Being Forward Contract Settled)	10,78,000	 10,78,000
01.05.13	Discount A/c. Dr. To Deferred Discount A/c. (Being balance amount of Discount recognized/ transferred to P&L)	1,334	 1,334

QUESTION NO 7

Kapali Ltd. purchased a Plant for USD 20,000 on 31st December 2012, payable after 4 months. The Company entered into a Forward Contract for 4 months at ₹54.85 per USD. On 31st December 2012, the Exchange Rate was ₹53.50 per USD.

How will you recognize the Profit or Loss on the Forward Contract in the books of Kapali Ltd. for the year ended 31st March 2013? (Journal Entries are not required).

SOLUTION

Particulars	₹
1. Value at the rate prevailing at the inception of Forward Contract (USD 20,000 x 53.50)	10,70,000
2. Value at the Forward Rate (USD 20,000 x 54.85)	10,97,000
3. Total Loss on entering into the Forward Contract = arising at inception for 4 months Contract Period	27,000
4. Loss to be recognised for the year ended 31st March 2013, i.e. for 3 months = 27,000 x $\frac{3}{4}$	20,250

QUESTION NO 8

How would you deal with the following foreign exchange transactions on the annual accounts for the year ending March 31, 2002?

- Insight India Ltd. imports a Plant & Machinery on 31st July, 2001 on deferred payment basis for US $ 200000. On March 31, 2002 the exchange rate, which was rs. 38 per dollar on 31st July, 2001, has gone up to ₹ 42.

(Ans: ₹ 800000 to be included in fixed assets

QUESTION NO 9

AD Softex India Ltd. imports certain stock worth US $ 600000 on 15th Aug., 2009 at which date the exchange rate is ₹46 per dollar. The payment are made on March 31, 2010. When the exchange rate is ₹ 47.10 per dollar. The stock is in hand as on 31st March 2002.

(Ans: ₹ 660000 debited to P&L Account)

QUESTION NO 10

Almaz Impex Ltd. obtains a short term foreign exchange loan of US $ 20,00,000 on 2nd Sept., 2006 when the exchange rate is ₹ 44.50 per dollar. On 31st March 2007, the exchange rate has gone up to ₹ 47.40 per dollar.

(Ans: ₹ 58 Lakhs debited in P&L Account).

QUESTION NO 11

AD Softex India Ltd. imported goods worth US $ 5,00,000 from a US based company ACS Inc. on 12.8.2009 when the exchange rate was 1 US $= 43.90. AD Softex India Ltd. agreed to pay its creditors in four equal instalments falling on 12.9.2009, 12.10.2009, 12.11.2009 and 12.12.2009. The exchange rates on the settlement dates were 43.80, 44.60, 44.90 and 45.60 respectively. Prepare ledger accounts of ACS Inc. in books of AD Softex India Ltd. and calculate net exchange fluctuation loss/gain.

(Ans: Loss of ₹ 412.500 Dr. to Profit and Loss Account).

QUESTION NO 12

Almaz Impex Ltd. an Indian Company took a foreign currency loan of US $ 5,00,000 @ 10% p.a. on 1.1.2009. Interest is payable half-yearly with an instalment for principal of US $ 50,000. The company closes books of account as on 31st March every year. Exchange rates are :-

1.1.2009	42.25
31.3.2009	42.50
31.6.2009	42.90
31.12.2009	43.90
31.3.2010	43.50

Prepare loan account of the company and calculate the exchange fluctuation loss/gain for the financial year ended on 31.3.2009 and 31.3.2010 respectively.

(Ans: Loss – ₹ 1,25,000 (31.3.2009): Loss – ₹ 4,95,000 (31.3.2010)

QUESTION NO 13

Stem Ltd. purchased a Plant for US$ 30,000 on 30th November 2013, payable after 6 months. The Company entered into a forward contract for 6 months @ rs.62.15 per Dollar. On 30th November 2013, the Exchange Rate wass.60.75 per Dollar. How will you recognize the Profit or Loss on Forward Contact in the books of Stem Ltd. for the year ended 31st March 2014?

SOLUTION

The treatment under AS-11 is as under:-

Particulars	₹
1. Value at the rate prevailing at the inception of forward Contract 30,000 $ x 60.75	18,22,500
2. Value at the forward rate 30,000 $ x 62.15	18,64,500
3. Total Loss on entering into forward contract = arising at inception for 6 months contract (1-2)	42,000
4. Loss to be recognized for the year ended 31st March 2014 i.e .for 4 months = 42000 x 4/6	28,000

Interest Payments should be charged to Profit and Loss Account of each year at the Transaction Value on payment dates.

QUESTION 14(CA INTER JAN 21)(5MARKS)

Explain briefly the accounting treatment needed in the following cases as per AS 11 as on 31.03.2020

(i) Debtors include amount due from Mr. S ₹ 9,00,000 recorded at the prevailing exchange rate on the date of sales, transaction recorded at US $1 = ₹ 72.00

US $ 1=₹ 73.50 on 31st March,2020

US $ 1= ₹ 72.50 on 1st April,2019.

(ii) Long term loan taken on 1st April, 2019 from a U.S. company amounting to ₹ 75,00,000. ₹5,00,000 was repaid on 31st December, 2019, recorded at US $ 1 = ₹ 70.50. interest has been paid as and when debited by the US company.

US $1= ₹ 73.50 on 31st March,2020

US $1=1₹ 72.50 on 1st April, 2019

SOLUTION

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

However, at the option of an entity, exchange differences arising on reporting of long - term foreign currency monetary items at rates different from those at which they were initially recorded during the period, or reported in previous financial statements, in so far as they relate to the acquisition of a non-depreciable capital asset can be accumulated in a "Foreign Currency Monetary Item Translation Difference Account" in the enterprise's financial statements and amortized over the balance period of such long-term asset/ liability, by recognition as income or expense in each of such periods.

	Foreign Currency Rate	₹
Debtors Initial recognition US $12,500 (9,00,000/72)	1 US $ = ₹72	9,00,000
Rate on Balance sheet date	1 US $ = ₹ 73.50	
Exchange Difference Gain US $ 12,500 X (73.50-72)		18,750
Treatment: Credit Profit and Loss A/c by ₹ 18,750 Long term Loan		
Initial recognition US $ 1,03,448.28 (75,00,000/72.50)	1 US $ = ₹ 73.50	75,00,000
Rate on Balance sheet date	1 US $ = ₹ 73.50	
Exchange Difference Loss after adjustment of exchange gain on repayment of ₹ 5,00,000		
₹ 67,987.48 [82,171.88 (US $ 96,356.08 X ₹ 73.5 less ₹ 70,00,000) less profit 14,184.40		
US $ 7,092.2 (5,00,000/70.5) X ₹ 2)] NET LOSS Treatment: Credit Loan A/c and Debit FCMITD A/C or Profit and Loss A/c by ₹ 67,987.48		67,987.48*

Thus, Exchange Difference on Long term loan amounting ₹ 67,987.48 may either be charged to Profit and Loss A/c or to Foreign Currency Monetary Item Translation Difference Account but exchange difference on debtors amounting ₹ 18,750 is required to be transferred to Profit and Loss A/c.

NOTE 1: *Exchange Difference Loss (net of adjustment of exchange gain on repayment of ₹ 5,00,000) has been calculated in the above solution. Alternative considering otherwise also possible.

NOTE 2: Date of sales transaction of ₹ 9 lakhs has not been given in the question and hence it has been assumed that the transaction took place during the year ended 31 March 2020.

QUESTION 15

Classify the following items as monetary or non-monetary item :

Inventories

Trade Receivables

Investment in Equity Shares

Property, Plant and Equipment

QUESTION 16

	Exchange Rate per $
Goods purchased on 1.120X1 for US $ 15,000	₹ 75
Exchange rate on 31.3.20X1	₹ 74
Date of actual payment 7.7.20X1	₹ 73

You are required to ascertain the loss/gain to be recognized for financial years ended 31st March, 20X1 and 31st March, 20X2 as per AS 11.

QUESTION 17

Kalim Ltd. borrowed US$ 4,50,000 on 01/01/20X1, which will be repaid as on 31/07/20X1. Kalim Ltd. prepares financial statement ending on 31/03/20X1. Rate of exchange between reporting currency (INR) and foreign currency (USD) on diferent dates are as under :

01/01/20X1 1 US$ = ₹ 48.00

31/03/20X1 1 US$ = ₹ 49.00

31/07/20X1 1 US$ = ₹ 49.50

QUESTION 18

Rau Ltd. purchased a plant for US$ 1,00,000 on 01st February 20X1, payable after three months. Company entered into a forward contract for three months @₹ 49.15 per dollar. Exchange rate per dollar on 01st Feb. was ₹ 48.85. How you recognise the profit or loss on forward contract in the books of Rau Ltd. ?

QUESTION 19

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

QUESTION 20

Assets and liabilities and income and expenditure items in respect of foreign branches (integral foreign operations) are translated into Indian rupees at the prevailing rate of exchange at the end of the year. The resultant exchange differences in the case of profit, is carried to other Liabilities Account and the Loss, if any, is charged to the statement of profit and loss. Comment.

QUESTION 21

A Ltd. purchased fixed assets costing ₹ 3,000 lakhs on 1.1.20X1 and the same was fully financed by foreign currency loan (U.S. Dollars) payable in three annual equal instalments. Exchange rates were 1 Dollar = ₹ 40.00 and ₹ 42.50 as on 1.1.20X1 and 31.12.20X1 respectively. First instalment was paid on 31.12.20X1. The entire difference in foreign exchange has been capitalised.

You are required to state, how these transactions would be accounted for.

QUESTION 22 (CA INTER DEC. 2021 EXAMS : 5 MARKS)

(i) PP Ltd. an Indian Company acquired long term finance from WW (P) Ltd. a U.S. company, amounting to ₹ 40,88,952. The transaction was recorded at US $1 = ₹ 72.00, taking exchange rate prevailing at the date of transaction. The exchange rate on balance sheet date (31.03.2021) is US $1 = ₹ 73.60.

(ii) Trade receivables of PP Ltd. include amount receivable from Preksha Ltd., ₹ 20,00,150 recorded at the prevailing exchange rate on the date of sales, transaction recorded at US $1 = ₹ 73.40. The exchange rate on balance sheet date (31.03.2021) is US $1 = ₹ 73.60. Exchange rate on 1st April, 2020 is US $1 = ₹ 74.00.

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 PP Ltd.

SOLUTION :

(i) Long term Finance

	Foreign Currency Rate	₹
Initial recognition US $ 56,791 (40,88,952/72)	1 US $ = ₹ 72	40,88,952
Rate on Balance sheet date	1 US $ = ₹ 73.60	
Exchange Difference Loss [US $ 56,791 x (73.60 – 72)]		90,866 (rounded off)

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.

However, at the option of an entity, exchange differences arising on reporting of long-term foreign currency monetary items at rates different from those at which they were initially recorded during the period, or reported in previous financial statements, in so far as they relate to the acquisition of a non-depreciable capital asset can be accumulated in a "Foreign Currency Monetary Item Translation Difference Account" in the enterprise's financial statements and amortized over t he balance period of such long-term asset/ liability, by recognition as income or expense in each of such periods.

Treatment needed in this case: PP Ltd. can either Debit Foreign Currency Monetary Item Translation Difference (FCMITD) A/c or Debit Profit and Loss A/c by ₹ 90,866 and Credit Loan A/c

(ii) Trade Receivables

	Foreign Currency Rate	₹
Initial recognition US $ 27,250 (20,00,150/ 73.40)	1 US $ = ₹ 73.40	20,00,150
Rate on Balance sheet date	1 US $ = ₹ 73.60	
Exchange Difference Gain [US $ 27,250 X (73.60-73.40)]		5,450

As per AS 11 "The Effects of Changes in Foreign Exchange Rates", exchange differences on trade receivables amounting ₹ 5,450 is required to be transferred to Profit and Loss A/c.

Treatment needed in this case: Credit Profit and loss account by ₹ 5,450.

QUESTION 23 (CA INTER NOV. 2022 EXAMS : 5 MARKS)

(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 31 st 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

For the year ended 31st March, 2022 exchange diffefence 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.

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ACCOUNTING STANDARD:10
PROPERTY,PLANT & EQUIPMENT

QUESTION NO 1

On 1st March, K Ltd. purchased 50,00,000 worth of land for a Factory Site. The Company demolished an old building on the property and sold the material for l,00,000. The Company incurred additional cost & realized salvaged proceeds during March as follows:

Legal Fees for purchase contract and recording ownership	2,50,000
Title Guarantee Insurance	1,00,000
Cost for Demolition of Building	5,00,000

Compute the balance to be shown in the Land Account on 31st March Balance Sheet.

QUESTION 2

Fire Ltd. purchased equipment for its power plant from Urja Ltd. during the year 2006- 07 at a cost of 100 Lacs. Out of this they paid only 90% and balance 10% was to be paid after one year on satisfactory performance of the equipment. During the financial year 2007-08, Urja Ltd. waived off the balance 10% amount which was credited to Profit and Loss Account by Fire Ltd. as discount received.

SOLUTION

In the given case, supplier has given a discount of 10 lacs which was payable at the time of acquisition of assets. The amount of discount of 10 Lacs should not be transferred to PL Account because it is related to acquisition of fixed assets, So it should be adjusted against the cost of assets. The following entries shall be passes as follows:

JOURNAL ENTRIES

1)	FIXED ASSETS DR	100	
	TO BANK (90%)		90
	TO PAYABLES(10%)		10
	(BEING ASSETS ACQUIRED)		
2)	PAYABLES DR	10	
	TO FIXED ASSETS		10
	(BEING DISCOUNT GIVEN BY SUPPLIER)		

QUESTION 3

ABC Ltd. is constructing a fixed asset. Following are the expenses incurred on the construction:

	Rs
Materials	10,00,000
Direct Expenses	2,50,000
Total Direct Labour	5,00,000
(1 / 10th of the total labour time was chargeable to the construction)	
Total office & administrative expenses	8,00,000
(5% is chargeable to the construction)	
Depreciation on the assets used for the construction of this asset	10,000

Calculate the cost of fixed assets.

QUESTION 4

M/s. Tiger Ltd. allotted 7,500 equity shares of 100 each fully paid upto Lion Ltd. in consideration for supply of a special machinery. The shares exchanged for machinery are quoted at National Stock Exchange (NSE) at 95 per share, at the time of transaction. In the absence of fair market value of the machinery acquired, how the value of the machinery would be recorded in the books of Tiger Ltd.?

QUESTION 5

A new plant X was acquired in exchange of old plant B and on payment of 20,000. The carrying amount of the old plant B was Rs 1,75,000 (Historial cost less depreciation). The fair value of the Plant B on that date of exchange was Rs 1,50,000.

Suggest the accounting in the books of the enterprise.

QUESTION 6

One customer from whom Rs 5 lacs are recoverable for credit sales gives a motor car in full settlement of the dues. The directors estimate that the market rate of the motor car transferred is 5.25 lacs. As on the date of the Balance Sheet the car has not been registered in the name of the Auditee.

SOLUTION

In the given case, cost of Car shall be recorded at 5 lacs because we had to recover 5 lacs from the customer. We have not paid anything additionally for acquiring this car. So our actual cost shall be recorded at 5 lacs which is equal to recoverable balance of debtors.

QUESTION 7

During the Current Year 2009-10 M/s L & C Ltd. made the following expenditure relating to its plant and machinery:

	Rs
General repair	4,00,000
Repairing of electric motorS	1,00,000
Partial replacement of parts of machinery	50,000
Substantial improvements to the electrical wiring system	
Which will increase efficiency of the plant and machinery	10,00,000

SOLUTION

Expenditure that increases the future benefit from existing assets beyond its previously assessed standard of the format is included in the gross book value of fixed assets.

In the given case repairs amounting to 5,00,000 and partial replacement of parts of machinery should be charged to profit and loss statement. 10,00,000 incurred by substantial improvement to the electrical writing system which will increase efficiency should be capitalised.

QUESTION 8

Further during the year company made addition to its factory by using its own workforce, at a cost of Rs. 4,50,000 as wages and materials. The lowest estimate from an outside contractor to carry out the same work was Rs. 6,00,000. The directors contend that, since they are fully entitled to employ an outside contractor, it is reasonable to debit the factory building account with Rs. 6,00,000. Comment whether the director's contention is rieght in view of the provisions of Accounting Standard 10 "Accounting for Fixed Assets" ?

SOLUTION

Additions to Factory Buildings: The contention of the Board to debit the Factory Building Account by Rs. 6,00,000 is incorrect. Despite the fact that addition to factory buildings have been made at a cost of Rs. 4,50,000. In the case of a fixed asset, which is held for the purpose of earning income and not for resale, it would be improper to value the asset in excess of the amount, which has been paid for it. The additions made to the factory buildings must appear in the balance sheet at a figure not exceeding its actual cost to the company. AS-10 on "Accounting for Fixed Assets", makes clear that gross book of self-constructed fixed assets should be computed on the basis actual cost incurred/allocated. Even internal profits, if any, are eliminated in arising at such costs. Hence the Board's contention is not correct.

QUESTION 9

PQR Ltd. constructed fixed asset and incurred the following expenses on its construction:

	Rs
Materials	16,00,000
Direct Expenses	3,00,000
Total Direct Labour	6,00,000
(1/15th of the total labour time was chargeable to be construction)	
Total office & Administrative Expenses	9,00,000
(4% is chargeable to the construction)	
Depreciation on assets used for the construction of this asset	15,000

Calculate the cost of the fixed asset.

SOLUTION

As per Accounting standard - 10, "Accounting for Fixed Assets" cost of self constructed assets shall be calculated as follows:

Calculation of the cost of construction of Assets

Particulars	Rs.
Direct Materials	16,00,000
Direct Expenses	3,00,000
Direct Labour (Rs 6,00,000/15)	40,000
Office & Administrative Expenses (Rs. 9,00,000* 4%)	36,000
Depreciation	15,000
Cost of the Asset	19,91,000

QUESTION 10

Amna Ltd. contracted with a supplier to purchase a specific machinery to be installed in Department A in two months time. Special foundations were required for the plant, which were to be prepared within this supply lead time.

The cost of site preparation and laying foundation were Rs 47,290. These activities were supervised by a technician during the entire period, who is employed for this purpose of Rs 15,000 per month. The Technician's services were given to Department A by Department B, which billed the services at Rs 16, 500 per month after adding 10% profit margin.

The machine was purchased at Rs 52,78,000. Sales Tax was charged at 4% on the invoice. Rs 18,590 transportation charges were incurred to bring the machine to the factory. An Architect was engaged at a fee of Rs 10,000 to supervise machinery installation at the factory premises. Also. payment under the invoice was due in 3 months. However, the Company made the payment in 2nd month. The company operates on Bank overdraft @ 11%.

SOLUTION

NOTE 1: As per the provisions of AS-10, we should consider all the expenses while computing the cost of fixed assets which are directly incurred for acquisition of fixed assets. The format was provided in class notes.

NOTE 2: The amount is payable in 3 months but company made the payment in 2nd month which indicates that company has made the payment in advance (1 month) at loss of interest due to bank overdraft. Such interest should not be considered as a part of cost of assets because installation period is only 2 months and we can not consider any expense for capitalization for ready for use assets. We should write off such interest in profit and loss account.

NOTE 3: We should always value all the assets at cost or market value whichever is lower. So we should ignore profit added by department in services of technician.

Statement showing calculation of cost of fixed assets

Particulars	Amount
Purchase Price	52,78,000
Sales tax(4%)	211120
Transportation charges	18590
Professional fees	10000
Technician services (15000x2)	30000
Site preparation Expenses	47290
	5595000

QUESTION NO 11 (C A FINAL NOV 2003)

Kapil Ltd. purchased machinery from Parveen Ltd. on 30.09.2001. The price was Rs.370.44 lakhs after charging 8% sales tax and giving a trade discount of 2% on the quoted price. Transport charges were 0.25% on the quoted price and installation charges 1% on the quoted price.

A loan of Rs.300 lakhs was taken on the trial from the bank on which interest at 15% per annum was to be paid. Expenditure incurred on the trial run was materials Rs.35,000, wages Rs.25,000 and overheads Rs.15,000.

The machinery was ready for use on 1.12.2001, but it was actually put to use only on 1.5.2002. Find out the cost of the machine and suggest the accounting treatment for the expenses incurred in the interval between the dates 1.12.2001 to 1.05.2002. the entire loan amount remained unpaid on 1.5.2002.

SOLUTION:

Particulars	Computations	Rs. in lakhs
Quoted price	(370.44/108*100)*100/98	3,50.000
Less: discount 2%	2% of 3,50.000	7.000
Net price		3,43.000
Add: sales tax 8%	8% of 3,43.000	27.440
Add: Transportation	0.25% on quoted price of 3,50.000	0.875
Add: installation	1.00% of quoted price of 3,50.000	3.500
Add: trial run expense	Material+ wages+ OH=0.35+0.25+0.15	0.750
Add: Borrowing cost	300*15%*2/12 (30.9.2001 to 1.12.2001)	7.500
Total cost of asset		383.065

- Capitalization of Borrowing costs should cease when substantially all the activities necessary to prepare the qualifying asset for its intended use are complete. In the above case, this period ends on 1-12-2001 when the asset was ready for use.
- Other Borrowing costs (i.e, not capitalized under As-16) should be written off as an expense in the profit and loss account. Hence the interest for the period 1.12.2001 and 1.5.2002 on Rs.300 lakhs, amounting to Rs.18.75 lakhs should be expensed off.

QUESTION 12 (CA INTER NOV 2020) (5MARKS)

A Ltd. had following assets. Calculate depreciation for the year ended 31st March, 2020 for each asset as per AS 10 (Revised):

(i) Machinery purchased for ₹ 10 lakhs on 1st April, 2015 and residual value after useful life of 5 years, based on 2015 prices is ₹ 10 lakhs.

(ii) Land for ₹ 50 lakhs.

(iii) A Machinery is constructed for ₹ 5,00,000 for its own use (useful life is 10 years). Construction is completed on 1st April, 2019, but the company does not begin using the machine until 31st March, 2020.

(iv) Machinery purchased on 1st April.2017 for ₹ 50,000 with useful life of 5 years and residual value is NIL. On 1st April, 2019, management decided to use this asset for further 2 years only.

SOLUTION

Computation of amount of depreciation as per AS 10

		₹
(i)	Machinery purchased on 1/4/15 for ₹ 10 lakhs (having residual value of ₹ 10 lakhs) **Reason:** The company considers that the residual value, based on prices prevailing at the balance sheet date, will equal the cost. Therefore, there is no depreciable amount and depreciation is correctly zero.	Nil
(ii)	Land (50 lakhs) (considered freehold) **Reason:** Land has an unlimited useful life and therefore, it is not depreciated.	Nil
(iii)	Machinery constructed for own use (₹ 5,00,000/10) **Reason:** The entity should begin charging depreciation from the date the machine is ready for use i.e. 1st April,2019. The fact that the machine was not used for a period after it was ready to be used is not relevant in considering when to begin charging depreciation.	50,000

(iv)	Machinery having revised useful life **Reason:** The entity has charged depreciation using the straight-line method at ₹ 10,000 per annum i.e (50,000/5 years). On 1st April,2019 the asset's net book value is [50,000 – (10,000 x 2)] i.e. ₹ 30,000. The remaining useful life is 2 years as per revised estimate. The company should amend the annual provision for depreciation to charge the unamortized cost over the revised remaining life of 2 years. Consequently, it should charge depreciation for the next 2 years at ₹ 15,000 per annum i.e. (30,000 / 2 years).	15,000

QUESTION 13 (CA INTER JULY 21)(5 MARKS)

(i) A Limited has contracted with a supplier to purchase machinery which is to be installed at its new plant in four months time. Special foundations wer e required for the machinery which were to be prepared within this supply lead time. The cost of the site preparation and laying foundations were ₹ 2,10,000. These activities were supervised by an Architect during the entire period, who is employed for t his purpose at a salary of ₹ 35,000 per month. The machinery was purchased for ₹ 1,27,50,000 and a sum of ₹ 2,12,500 was incurred towards transportation charges to bring the machinery to the plant site. An Engineer was appointed at a fees of ₹ 37,500 to supervise the installation of the machinery at the plant site. You are required to ascertain the amount at which the machinery should be capitalized in the books of A Limited.

(ii) B Limited, which operates a major chain of retail stores, has acquired a new store location. The new location requires substantial renovation expenditure. Management expects that the renovation will last for 4 months during which the store will be closed. Management has prepared the budget for this period including expenditure r elated to construction and re-modelling costs, salary of staff who shall be preparing the store before its opening and related utilities cost. How would such expenditure be treated in the books of B Limited?

SOLUTION

(i) Statement Showing the Computation of the amount at which the Machinery should be capitalized in the books of A Limited

Particulars		**Amount (₹)**
Purchase cost of machinery	Given	1,27,50,000
Add: Site Preparation Cost	Given	2,10,000
Architect's Salary	Specific / Attributable overheads for 4 months (₹ 35,000 x 4)	1,40,000
Initial Delivery Cost	Transportation	2,12,500
Professional Fees for Installation	Engineer's Fees	37,500
Total Cost of Machinery to be capitalized		1,33,50,000

(ii) Management should capitalize the costs of construction and remodelling the store, because they are necessary to bring the store to the condition necessary for it to be capable of operating in the manner intended by management. The store cannot be opened without incurring the remodelling expenditure, and thus the expenditure should be considered part of the asset. However, if the cost of salaries, utilities and storage of goods are in the nature of operating expenditure that would be incurred if the store was open, then these costs are not necessary to bring the store to the condition necessary for it to be capable of operating in the manner intended by management and should be expensed.

QUESTION 14

(Capitalising the cost of "Remodelling" a Supermarket)

Entity A, a supermarket chain, is renovating one of its major stores. The store will have more available space for in store promotion outlets after the renovation and will include a restaurant. Management is preparing the budgets for the year after the store reopens, which include the cost of remodelling and the expectation of a 15% increase in sales resulting from the store renovations, which will attract new customers. State whether the remodelling cost will be capitalised or not.

QUESTION 15

What happens if the cost of the previous part/inspection was/ was not identified in the transaction in which the item was acquired or constructed?

QUESTION 16

Entity A has an existing freehold factory property , which it intends to knock down and redevelop. During the redevelopment period the company will move its production facilities to another (temporary) site. The following incremental costs will be incurred:

1. Setup costs of ₹ 5,00,000 to install machinery in the new Location.
2. Rent of ₹ 15,00,000
3. Removal costs of ₹ 3,00,000 to transport the machinery from the old Location to the temporary Location.

Can these costs be capitalised into the cost of the new building?

QUESTION 17

Omega Ltd. contracted with a supplier to purchase machinery which is to be installed in its one department in three months' time. Special foundations were required for the machinery which were to be prepared within this supply Lead time. The cost of the site preparation and Laying foundations were ₹ 1,40,000. These activities were supervised by a technician during the entire period, who is employed for this purpose of ₹ 45,000 per month. The machine was purchased at ₹ 1,58,00,000 and ₹ 50,000 transportation charges were incurred to bring the machine to the factory site. An Architect was appointed at a fee of ₹ 30,000 to supervise machinery installation at the factory site. You are required to ascertain the amount at which the Machinery should be capitalized.

QUESTION 18

(Capitalisation of directly attributable costs)

Entity A which operates a major chain of supermarkets/ has acquired a new store Location. The new Location requires significant renovation expenditure. Management expects that the renovations will Last for 3 months during which the supermarket will be closed.

Management has prepared the budget for this period including expenditure related to construction and remodelling costs/ salaries of staff who will be preparing the store before its opening and related utilities costs. What will be the treatment of such expenditures?

QUESTION 19

(Operating costs incurred in the start-up period)

An amusement park has a 'soft' opening to the public, to trial run its attractions. Tickets are sold at a 50% discount during this period and the operating capacity is 80%. The official opening day of the amusement park is three months Later. Management claim that the soft opening is a trial run necessary for the amusement park to be in the condition capable of operating in the intended manner. Accordingly, the net operating costs incurred should be capitalised. Comment.

QUESTION 20

(Consideration received comprising a combination of non monetary and monetary assets)

Entity A exchanges Land with a book value of ₹ 10,00,000 for cash of ₹ 20,00,000 and plant and machinery valued at ₹ 25,00,000. What will be the measurement cost of the assets received. (Consider that the transaction has commercial substance)?

QUESTION 21

(Exchange of assets that lack commercial substance)

Entity A exchanges car X with a book value of ₹ 13,00,000 and a fair value of ₹ 13,25,000 for cash of ₹ 15,000 and car Y which has a fair value of ₹ 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?

QUESTION 22

(Revaluation on a class by class basis)

Entity A is a large manufacturing group. It owns a number of industrial buildings, such as factories and warehouses and office buildings in several capital cities. The industrial buildings are located in industrial zones, whereas the office buildings are in central business districts of the cities. Entity A's management want to apply the revaluation model as per AS 10 (Revised) to the subsequent measurement of the office buildings but continue to apply the historical cost model to the industrial buildings.

State whether this is acceptable under AS 10 (Revised) or not with reasons?

QUESTION 23

Entity A has a policy of not providing for depreciation on PPE capitalised in the year until the following year, but provides for a full year's depreciation in the year of disposal of an asset. Is this acceptable?

QUESTION 24

(Change in estimate of useful life)

Entity A purchased an asset on 1st January 20X1 for ₹ 1,00,000 and the asset had an estimated useful life of 10 years and a residual value of nil.

On 1st January 20X5, the directors review the estimated life and decide that the asset will probably be useful for a further 4 years.

Calculate the amount of depreciation for each year, if company charges depreciation on Straight Line basis.

QUESTION 25

(Depreciation where residual value is the same as or close to Original cost)

A property costing ₹ 10,00,000 is bought in 20X1. Its estimated total physical life is 50 years. However, the company considers it likely that it will sell the property after 20 years.

The estimated residual value in 20 years ' time, based on 20X1 prices, is:

Case (a) ₹ 10,00,000

Case (b) ₹ 9,00,000.

Calculate the amount of depreciation.

QUESTION 26

(Determination of appropriate Depreciation Method)

Entity 8 manufactures industrial chemicals and uses blending machines in the production process. The output of the blending machines is consistent from year to year and they can be used for different products.

However, maintenance costs increase from year to year and a new generation of machines with significant improvements over existing machines is available every 5 years. Suggest the depreciation method to the management.

QUESTION 27

(Gain on replacement of Insured Assets)

Entity A carried plant and machinery in its books at ₹ 2,00,000. These were destroyed in a fire. The assets were insured 'New for old' and were replaced by the insurance company with new machines that cost ₹ 20,00,000. The machines were acquired by the insurance company and the company did not receive ₹ 20,00,000 as cash compensation. State, how Entity A should account for the same?

QUESTION 28 (CA INTER MAY 2022 EXAMS : 5 MARKS)

XYZ Limited provided you the following information for the year ended 31 st March, 2022.

(i) The carrying amount of a property at the end of the year amounted to ₹ 2,16,000 (cost/value ₹ 2,50,000 and accumulated depreciation ₹ 34,000). On this date the property was revalued and was deemed to have a fair value of ₹ 1,90,000. The balance in the revaluation surplus relating to a previous revaluation gain for this property was ₹ 20,000.

You are required to calculate the revaluation loss as per AS 10 (Revised) and give its treatment in the books of accounts.

(ii) An asset that originally cost ₹ 76,000 and had accumulated depreciation of ₹ 62,000 was disposed of during the year for ₹ 4,000 cash.

You are required to explain how the disposal should be accounted for in the financial statements as per AS 10 (Revised).

SOLUTION :

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

Calculation of revaluation loss and its accounting treatment

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

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

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

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

ACCOUNTING STANDARD-26
INTANGIBLE ASSETS
(IAS 38 & IND AS 38)

QUESTION NO 1

A Ltd. is developing a new production process. It has incurred the following expenditure. Find out value of Intangible Assets.

Date	Particulars	Amount (₹ in lacs)
Upto 31March 2001	Research expenditure when intention to commercialise was not establish	20
2001-02	Development expenses	
	Salaries and wages	30
	Overheads	12
	Staff Training	10
	Apportioned Administrative Expenses	10
2002-03	Salary and wages	40
	Recoverable Amount (AS-28)	70

QUESTION NO 2

A Limited has an intangible asset on 1.4.2003 where cost was ₹ 10 lakhs when it was acquired on 1.4.1991. How should this amount be treated if?

A Ltd. has never amortized this asset.

A Ltd. amortizes it on straight-line basis over a period of 20 years?

QUESTION NO 3

An enterprise is developing a new production process. During the year 2001, expenditure incurred was ₹ 10 lakhs, of which ₹ 9 lakhs was incurred before 1 December 2001 and 1 lakh was incurred between 1 December 2001 and 31 December 2001. The enterprise is able to demonstrate that, at 1 December 2001, the production process met the criteria for recognition as an intangible asset.

SOLUTION

At the end of 2001, the production process is recognized as an intangible asset at a cost of ₹ 1 lakh (expenditure incurred since the date when the recognition criteria were met, that is, 1 December 2001). The ₹ 9 lakhs expenditure incurred before 1 December 2001 is recognized as an expense because the recognition criteria were not met until 1 December 2001.

QUESTION NO 4

A pharma company spent ₹ 33 lakhs during the year to develop a drug on AIDS. It will take four years to establish whether the drug will be successful. The company wants to treat the expenditure as deferred revenue expenditure.

SOLUTION

In the given case, the pharma company should not capitalize ₹ 33 lakhs since capitalization conditions as per AS-26 are not fulfilled. The same should charged to the P&L account.

QUESTION NO 5 (CA FINAL NOV 2006)

A company with a turnover of ₹ 250 crores and an annual advertising budget of ₹ 2 crore had taken up the marketing of a new product. It was estimated that the company would have a turnover of ₹ 25 crores from the new product. The company had debited to its Profit and Loss Account the total expenditure of ₹ 2 crore incurred on extensive special initial advertisement campaign for the new product.

Is the procedure adopted by the company correct ?

SOLUTION

With the introduction of AS - 26 - "Intangible Assets', the concept of deferred revenue expenditure no longer prevails except in respect of a very few items, such as ancillary costs on borrowings, share issue expenses, etc. AS-26 does not permit the capitalization of expenses incurred on advertising or brand promotion, etc. Thus the accounting treatment by the company of debiting the entire advertising expenditure of ₹ 50 lakhs to the profit and loss account of the year is correct.

QUESTION NO 6

During 2003, an enterprise incurred costs to develop and produce a routing, low risk computer software product, as follows :

	Amount / ₹
Completion of detailed programme and design	25,000
Coding and testing	20,000
Other coding costs	42,000
Testing costs	12,000
Product masters for training materials	13,000

What should be capitalised as software costs in the books of the company, on B/S date ?

SOLUTION

As per Para 44 of AS - 26, cost incurred in creating a computer software producer 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 has been established upon completion of detailed program design or working model. In this case, ₹ 45,000 would be recorded as expenses (₹ 25,000 for completion of detailed program design and ₹ 20,000 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 the products costs are incurred are capitalised as software cost (₹ 42,000 + ₹ 12,000 + ₹ 13,000 = ₹ 67,000).

QUESTION NO 7

Himalaya Ltd. in the past three years spent ₹ 75,00,000 to develop a Drug to treat Cancer, which was charged to Profit and Loss Account since they did not meet AS-26 criteria for capitalization. In the current year approval of the concerned Govt. Authority has been received, The Company wishes to capitalize ₹ 75,00,000 and disclose it as a prior period item. Is It correct ?

Give reason for your views.

QUESTION NO 8 (RTP MAY 2006)

An Enterprise has incurred expense for purchase of Technical Know-how for manufacturing a Moped. The Enterprise has paid ₹ 5 crores for the use of Know-how for a period of 4 years. The Enterprise estimates the production of mopeds as follows :

Year	No. of Mopeds
1	25,000
2	50,000
3	75,000
4	1,00,000

On going into production, at the end of the 1st year it achieved its targeted production, but considered to revise the estimates for the next 3 years as follows :

Year	No. of Mopeds
1	35,000
2	65,000
3	80,000

(a) How will the Enterprise amortise the Technical Know-how Fees as per AS-26.

(b) Whether this amortisation should be directly charged as an expense or should form part of Production Cost of the Mopdes.

SOLUTION

Based on the revised estimate, total sales is 2,05,000 the first year charge should be a proportion of 25,000 / 2,05,000 on ₹ 5 crores, second year will be 35,000 / 2,05,000, and so on unless the estimates are again revised. If these estimates cannot be determined reliably it would be preferable to charge them off on a straight line basis, otherwise, as can be seen from the above example, significant amortisation amount is inappropriately postponed to later years. As already mentioned above, there will rarely, if ever, be persuasive evidence to support an amortisation method for intangible assets that results in a lower amount of accumulated amortisation than under the straight-line method. In the given case, amortisation expense will be included as cost of inventory.

QUESTION NO 9 (C A FINAL AUDITING)

As a statutory Auditor, how would you deal with the following ? A Pvt. Ltd. started stock broking activities in 2005. For this purpose it acquired membership of a Stock Exchange for ₹ 100 lacs. While finalizing the accounts, the company disclosed the above amount under the Fixed Assets schedule as “Stock Exchange Membership Rights”. The company also does not write off any amount since the rights would enable the company to perpetually carry on its business.

SOLUTION:

No, treatment of company is not correct because the licence fee which is paid by company for stock exchange membership should be disclosed as an intangible asset. If its life is not measurable then we should show it at cost. But impairment test should be conducted every year.

QUESTION NO 10(C A FINAL)

Swift Ltd. acquired a Patent at a cost of ₹ 80,00,000 for a period of 8 years and the product life-cycle is also 8 years. The company capitalized the cost and started amortizing the asset at ₹ 10,00,000 per annum. After two years it was found that the product life-cycle may continue for another 5 years from then. The net cash flows from the product during these 5 years were expected to be ₹ 36,00,000; ₹ 46,00,000; ₹ 44,00,000; ₹ 40,00,000 and ₹ 34,00,000. Find out the amortization cost of the patent for each of the years

Hint: Ratio of cash inflow should be used to write off the intangible asset of 60,00,000 (36:46:44:40:34).

SOLUTION:

As per AS-26 "Intangible Assets", the amortization method used should reflect the pattern in which the asset's economic benefits are consumed by the enterprise, if that pattern cannot be determined reliably, the straight-line method should be used.

In the instant case, pattern of economic benefit in the form of net cash flows is determined reliably after two years. In the initial two years the pattern of economic benefits could not have been reliably estimated therefore amaoritzation was done at straight-line method i.e. ₹ 10 Lakhs per annum. However, after two years pattern of economic benefits for next five years in the form net cash flows is reliably estimated as under and therefore amortization will also be done as per the pattern of cash in flows:-

Cash in flows (₹)	**Amt. of amortization in next 5 years (₹) Balance WDV**
36,00,000	10,80,000 (60,00,000 x 36,00,000/200,00,000)
46,00,000	13,80,000 (60,00,000 x 46,00,000/200,00,000)
44,00,000	13,20,000 (60,00,000 x 44,00,000/200,00,000)
40,00,000	12,00,000 (60,00,000 x 40,00,000/200,00,000)
34,00,000	10,20,000 (60,00,000 x 34,00,000/200,00,000)
200,00,000	60,00,000

QUESTION NO 11 (C A FINAL MAY 1999)

Note No. 6 of Published Accounts of V Ltd. reads as follows -

"The Company being a manufacturer of pollution control equipment, has entered into collaboration agreements with foreign manufacturers for technical know-how comprising the supply of drawings and training of personnel for manufacture of different types of pollution control equipments. These agreements were concluded after the commencement of production at the beginning of the year. The collaboration amount of ₹ 100 lakhs is payable in five annual instalments. The Company has amortised the entire cost of technical know-how as a depreciable assets and has shown the same in the schedule of Fixed Assets". As an Auditor state your views.

SOLUTION:

Amounts of 100 lakh should be recognised as Intangible assets.

QUESTION NO 12

While executing a new project, the company had to pay ₹ 50 lakhs to the State Government as part of the cost of roads built by the State Government in the vicinity of the project for the purpose of carrying machinery and materials to the project site. The road so built is the property of the State Government.

Advice the company about the accounting treatment.

Hint: Refer class notes on toll road licence accounting as per schedule ii.

QUESTION NO 13

Vishnu Ltd. is engaged in research on a new process design for its product. It had incurred an expenditure of ₹ 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 ₹ 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 ₹ 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 ₹ 265.37 lakhs should be expensed in the year in which it is incurred. It is presumed that the entire expenditure ₹ 265.37 lakhs is incurred in financial year 2002-2003. Hence, it should be written off as an expense in that year itself.

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 years	= ₹ 40 lakhs per annum
Company's Cost of Capital	= 10%
Annuity Factor at 10% for five years	= 3.7908
(from the annuity tables)	

Present value of future cash flows = ₹ 40 x 3.7908 = ₹ 151.63 lakhs.

Carrying Amount of the Asset :- Since the Present Value of Future Cash Flows is only ₹ 151.63 lakhs, (which is lower than the cost of ₹ 180 lakhs), it is prudent to recognize an impairment loss of ₹ 180.00 lakhs - ₹ 151.63 lakhs = ₹ 28.37 lakhs in the financial year 2003-2004.

Amortisation Period and Amount :- The Company can amortise ₹ 151.63 lakhs over a five year period by charging ₹ 30.33 lakhs per annum for the financial year 2004-2005 onwards.

QUESTION NO 14 (SIMILAR QUESTION IN CA FINAL)

Ganguly International Ltd. is developing a new production process. During the financial year ended 31st March 2004, the total expenditure incurred on this process was ₹ 50 lakhs. The production process met the criteria for recognition as an intangible asset on 1st December 2003. Expenditure incurred till this date was ₹ 22 lakhs.

Further expenditure incurred on the process for the financial year ending 31st March 2005 was ₹ 80 lakhs. As at 31st March 2005, the recoverable amount of the know-how embodied in the process is estimated to be ₹ 72 lakhs. This includes estimates of future cash outflow as well as inflows :

You are required to work out :

What is the expenditure to be charged to the P &L Account for the financial year ended 31st March 2004 ? (Ignore depreciation for this purpose)

(i) What is the carrying amount of the intangible asset as at 31st March 2004 ?

(ii) What is the expenditure to be charged to the P &L Account for the financial year 2005 (Ignore depreciation for this purpose)

(iii) What is the carrying amount of the intangible asset as at 31st March 2005 ?

SOLUTION:

(a) Expenditure incurred up to 1.12.2009 will be taken up to profit and loss account for the financial year ended 31.3.2010 = ₹ 22 Lakhs.

(b) Carrying amount as on 31.3.2010 will be the expenditure incurred after 1.12.2009 = ₹ 28 Lakhs.

(c) Book cost of intangible asst as on 31.3.2011 is worked out as:

Carrying amount as on 31.3.2010	-	₹ 28 Lakhs
Expenditure during 2010-11	-	₹ 80 Lakhs
Total Book Cost	-	₹ 108 Lakhs
Recoverable amount, as estimated	-	₹ 72 Lakhs

Difference to be charged to Profit and loss account as impairment.

(d) Carrying amount as on 31.3.2011 will be (cost less Impairment loss) ₹ 72 Lakhs

QUESTION NO 15

A company is showing an Intangible Asset at ₹88 Lakhs as on 0104.2013. This asset was acquired for ₹ 120 Lakhs on 01.04.2009 and the same was available for use from that date. The Company has been following the policy of amortization of the Intangible Assets over a period of 15 years on Straight line basis. Comment on the accounting treatment of the above with reference to the relevant Accounting Standard.

SOLUTION:

1. Rebuttable Presumption : AS – 26 assumes that the useful life of an Intangible Asset will not exceed a period of 10 years, but this presumption is rebuttable.

2. Amortisation Amount as per Company Policy:

   (a) Amoritsation Amount ₹ 120 Lakhs ÷ 15 years = ₹ 8 Lakhs p.a.

   (b) Accumulated Amoritsation upto 31st March 2014

   (for four years) = ₹ 8 Lakhs x 4 = ₹ 32 Lakhs

   (c) Carrying Amount = ₹ 120 Lakhs – ₹32 Lakhs = ₹ 88 Lakhs

   = as per books

3. Future Amortisation: The balance Carrying Amount of ₹88 Lakhs should be amortised over the balance. Useful Life (11 Years) at ₹ 8 Lakhs per annum.

QUESTIO NO 16

Sunny Limited is developing a now production process. During the financial year ended 31st March 2013, the Company has incurred total expenditure of ₹ 40 Lakhs on the process. On 1st December 2012, the process has met the norms to be recognized as "Intangible Assets" and the expenditure incurred till that date is ₹ 16 Lakhs. During the financial year ending on 31st March 2014, the Company has further incurred ₹ 70 Lakhs.T he Recoverable Amount as on 31st March 2014 of the process is estimated to be ₹ 62 Lakhs. You are required to work out:

(i) Expenditure to be charged to Profit and Loss Account for the financial year ending on 31st March 2013and31st March 2014 (ignore Depreciation).

(ii) Carrying Amount of the Intangible Assets as at 31st March 2013 and 31st March 2014.

SOLUTION:

1. Expenditure charged to P&L for 2012-2013: ₹ 16 Lakhs will be recognized as an Expense because the recognition criteria were not met until1st December 2012. The expenditure will not form part of the cost of the Production Process recognized in the Balance Sheet.

2. Carrying Amount of Intangible Asset as on 31.03.2013: The Production Process will be recognized (i.e. Carrying Amount), as an Intangible Asset at a cost of ₹ 24 Lakhs (i.e. expenditure incurred till the date in which recognition criteria were met, i.e. Total during FY 2012-2013 ₹ 40 Lakhs less Expenses upto 1st Dec. 2012 ₹ 16 Lakhs).

3. Expenditure charged to P&L A/c. for 2013-2014:

Particulars	₹ Lakhs
Book Value on 31.3.2014 = Carrying Amt. on 31.3.2013 + Expenditure in 2013-2014 = 24 ÷ 70 Less: Recoverable Amount	94 62
Impairment Loss to be charged to P&L A/c.	32

4. Carrying Amount of Intangible Asset as on 31.03.2014: The Production Process will be shown at Book value ₹ 94 Lakhs, or Recoverable Amount ₹ 62 Lakhs, whichever is less, hence at ₹ 62 Lakhs as above.

QUESTION NO 17 CA FINAL NOV 2015 8MARKS

During the Financial year 2014-2015, Power Ltd. had the following transactions.

(i) ON 01.04.2014 Power Ltd. purchased a new Asset of Dark Ltd. for ₹ 11,40,000. The fair Value of Dark Ltd.'s identifiable Net Assets was ₹ 8,50,000. Power Ltd. is of the view that due to popularity of Dark Ltd.'s product the life of Goodwill is 10 years.

(ii) On 01.05.2014 Power Ltd. purchased a franchise to operate Transport Service from the Government for ₹ 12,00,000 and at a Annual Fee of 4% of Transport Revenues. The Franchise expires after 5 years. Transport Revenue were ₹1,20,000 for Financial year 2014-2015. Power Ltd. projects future Revenue of ₹ 2,40,000 in 2015-2016 and ₹ 3,50,000 p.a. for 3 years thereafter.

(iii) On 5.07.2014, Power Ltd. was granted a Patent that had been applied for by Dark Ltd. During 2014-2015, Power Ltd. incurred Legal Cost of ₹ 1,10,000 to register the Patent and an additional ₹3,00,000 to successfully prosecute a Patent infringement suit against a Computer. Power Ltd. expects the Patent's economic lie to be 10 years. Power Ltd. follows an Accounting Policy to amortize all Intangibles on SLM basis over a maximum period permitted by Accounting Standard, taking a full year amortization in the year of acquisition.

SOLUTION:

1. Treatment under AS-26

Point	Principle and Treatment (amounts in ₹000s)
(i)	* The excess of consideration paid over the Fair value of identifiable Net Asset is recognized as Goodwill, Hence, Goodwill= 1140-850=290. * AS-26 assumes that the useful life does not exceed 10 years. So, the amortization over 10 years is proper. Amortisation p.a. = $\frac{290}{10}$ = 29
(ii)	• Lumpsum franchise fee 1200 would be recognized as Intangibel Asset. • The Depreciation Amount should be allocated over the assets useful i.e, on a systematic basis, (e.g. SLM, or Radio of Revenues to be earned, etc.) • In this case Total Revenues to be earned in 5 years are – **Year** 1 2 3 4 5 Total **Revenue** 120 240 350 350 350 1410 **Amortisation** **Apportioned** 102 204 298 298 298 1200

	• Alternatively, Amortisation p.a. under SLM = 1200 / 5 = 240 • Revenue in each year and 4% Annual Fee should be recognized as Income/ Expenses in P&L of each year. Note: Impairment Testing nor considered in this cases.
(iii)	• Cost of Patent = Registration + Directly attributable Cost = 110+300=410 • Amortisation p.a. = 410 /10 years = 41 • Note: Assumed that 410 represents cost relating to right to use, and hence capitalized under AS-26.

QUESTION NO 18

During the current year, Mathangi Ltd. incurred ₹ 12 Lakhs as Direct Costs in developing the Patents having working life of fifteen years. The Accountant of the Company wants to write-off these costs over the period of fifteen years. Another view is to write off over their legally valid period, which is twelve years. Decide as per AS-26.

CONCLUSION:

In the given case, the costs incurred in developing the Patents should be capitalised and written off over their legal term of validity or over their working life, whichever is shorter. Therefore, the amount of ₹ 12 Lakhs should be written off over their legal term of validity, i.e. 12 years.

QUESTION NO 19

Srimathi Ltd. acquired patent right for ₹ 400 Lakhs. The product life cycle has been estimated to be 5 yeas and the amortization was decided in the ratio of estimated future cash flows which are as under:-

Year	1	2	3	4	5
Estimated Future Cash Flows **(₹ in Lakhs)**	200	200	200	100	100

After the 3rd year, it was ascertained that the Patent would have an estimated balance future life of 3 years and the Estimated Cash Flow after 5thyear is expected to be ₹ 50 Lakhs each year. Determine the amortization under AS-26.

SOLUTION

1. Initial Estimate of Total Cash Inflow = 200+200+200+100+100= ₹ 800 Lakhs.
2. So, as per initial estimate, the cost of Patent should be written off in the ratio 2:2:2:1:1 i.e. (₹ Lakhs) 100, 100, 100, 50 and 50 respectively, for the five years.
3. Unamortised Amount (WDV) of Patent at the end of 3rd year = 400 – (100+100+100) = ₹ 100 Lakhs.
4. Revised Estimate of Useful Life at the end of 3rd year = 3 future years, with estimated Cash Inflows being as under – Year 4 ₹ 100 Lakhs Year 5 ₹ 100 Lakhs, year 6: ₹ 50 Lakhs.
5. Hence, the unamortized Carrying Amount should be written off over the next 3 years, in the ratio of 100:100:50, i.e. ₹ 40 Lakhs, ₹ 40 Lakhs and ₹ 20 Lakhs respectively for years 4,5 and 6.

Hence, If it is assumed that the Patent Right is not renewable, the present unamortized amount of ₹ 100 Lakhs may be written off in years 4 and 5, as per initial estimate, at ₹ 50 Lakhs p.a.

QUESTION NO 20

Preetha Ltd. got a license to manufacture certain medicines for 10 years at a License Fee of ₹ 200 Lakhs. Given below is the pattern of expected production and expected Operating Cash Inflow:

Year	Production in Bottles (in Lakhs)	Net Operating Cash Flow (₹ in Lakhs)
1	300	900
2	600	1800
3	650	2300
4 to 10	800 p.a.	3200 p.a.

Net Operating Cash Flow has increased for third year because of better Inventory management and handling method. Suggest the amortization method.

SOLUTION

As per AS-26, Amortisation Method should be based on the expected pattern of consumption of economic benefits. Hence, the ratio of Net Operating Cash Flow can be used for amortization purposes.

Year	Net Operating Cash Flow	Amortisation Amt. (₹ in Lakhs) (in above ratio)
1	900	6
2	1,800	12
3	2,300	16
4	3,200	24
5	3,200	24
6	3,200	24
7	3,200	24
8	3,200	24
9	3,200	24
10	3,200	22 (bal. fig)
Total	27,400	200

QUESTION NO 21

A Company has deferred R&D Cost of ₹ 150 Lakhs. Sales expected in the subsequent years are as under:-

Year	I	II	III	IV
Sales (₹ in Lakhs)	400	300	200	100

Suggest how R&D Cost should be charged to Profit & Loss Account.

SOLUTION

1. The Deferred Research and Development costs is to be charged to P&L A/c. on the basis of Expected Sales as follows:-

Year	Sales (₹ Lakhs)	Percentage of R&D Costs to be amortized in each year (on the basis of Sales)	Amount charged to P&L Account (₹ Lakhs)
I	400	40%	150x40% = 60
II	300	30%	150x30% = 45
III	200	20%	150x20% = 30
IV	100	10%	150x10% = 15

2. Requirements under AS-26:

   (a) Para 78-80: The period of Amortization should be reviewed periodically to determine proper method of amortization.

   (b) Change of Amortization period: If the expected benefit from the asset is significantly different from the previous estimates, the amortization period should be changed accordingly.

QUESTION NO 22 (GOOD QUESTION)

Refiners and Projects Limited is a Company in the Oil and Gas Sector. It undertakes extensive Research and Development work as part of its operations. It has till the end of the Financial Year 31.03.2012, spent rs. 592.23 Crores on research expenses.

The development of a new process was completed in the Accounting year 2012-2013 after incurring an expenditure of Rs 322.26 Crores. In the Accounting year 2013-2014, the Company implemented the new process resulting in a post tax saving of ₹ 100 Crores in the first year of operation and savings of ₹80 Crores per annum thereafter for the next four years. Cost of Capital to the Company is 12%.

Kindly indicate how you will proceed to record the transactions in the books of accounts of the Company.

You are informed that the Research Expenses shown above do not include any General or selling and Administrative Expenses. Present Value of a Rupee discounted at 12% can be taken at 0.893, 0.797, 0712, 0.636 & 0.567.

SOLUTION

1. **Initial Recognition:**

Fin. Year	Amount Spent	Nature	Accounting Treatment
2011-12	₹ 592.23 Crores	Research Expenses	Expensed off by debiting Profit and Loss Account as per Para 41.
2012-13	₹ 322.26 Crores	Development Expenses	Capitalized as it fulfills conditions in Para 44.

2. **Testing for Impairment:** Value in Use of the development Expenses (as at 31.03.2013) (assuming the future post tax benefits can be estimated on 31.03.2013 itself).

Year	Cash Flow	Discount Factor at 12%	Discounted Cash Flow
1	100.00	0.893	89.30
2-5	80.00	2.712	216.96
Value in Use			306.26

Impairment Loss to be recognized = Carrying Amt. ₹ 322.26 Crores Less Value in Use ₹306.26 Crores =₹ 16 Crores

3. **Amortisation:** The revised Carrying Amount (after recognizing Impairment Loss), ₹ 306.26 Crores should be amortised over the useful life of 5 years, in the ratio of expected economic benefits, i.e. Post Tax Savings ratio 100:80:80:80:80.

QUESTION NO 23

Priya Ltd. purchased a Trademark for ₹ 45 Lakhs. The legal validity/useful life of the Trademark is 15years. At the end of each of the first six years, the recoverable amount of the Trademark was (in ₹ Lakhs) 45.50, 40.00, 35.50, 34.00, 29.00 and 25.00 respectively. Determine the amount of Impairment Loss to be recognized, if any.

(NOTE : PLEASE IGNORE QUESTION 23, IT IS GIVEN IN CA INTER BOOK BY MISTAKE BECAUSE ITS RELATED WITH AS 28 IMPAIRMENT)

QUESTION NO 24

State how you will deal with the following matter in the accounts of U Ltd. for the year ended 31st March 2010 with reference to Accounting Standard.

"The company had spent ₹ 45 Lakhs for publicity and research expenses on one of its new consumer product, which was marketed in the accounting year 2009-2010, but proved to be a failure".

SOLUTION:

As per AS-26 "Intangible Assets" research cost is to be expensed when incurred.

Further no intangible assets is created on account of publicity cost incurred on product provided to be a failure, therefore publicity expenses also to be expensed.

₹45 Lakhs spent on publicity and research to be expensed in the year 2009-2010.

QUESTION 25

ABC Ltd. developed know-how by incurring expenditure of ₹20 lakhs, The know-how was used by the company from 1.4.20X1. The useful life of the asset is 10 years from the year of commencement of its use. The company has not Amortised the asset till 31.3.20X8. Pass Journal entry to give effect to the value of know-how as per Accounting Standard-26 for the year ended 31.3.20X8.

SOLUTION:

JOURNAL ENTRY

		₹	₹
Profit and Loss A/c (Prior period item)	Dr.	12,00,000	
Amortization A/c	Dr.	2,00,000	
To Know-how A/c			14,00,000
[Being amortization of 7 years (out of which amortization of 6 years charged as prior period item)]			

QUESTION 26

The company had spent ₹ 45 lakhs for publicity and research expenses on one of its new consumer product, which was marketed in the accounting year 20X1-20X2, but proved to be a failure. State, how you will deal with the following matters in the accounts of U Ltd. for the year ended 31st March, 20X2.

SOLUTION:

In the given case, the company spent ₹ 45 lakhs for publicity and research of a new product which was marketed but proved to be a failure. It is clear that in future there will be no related further revenue/benefit because of the failure of the product. Thus according to AS 26 'Intangible Assets', the company should charge the total amount of ₹ 45 lakhs as an expense in the profit and loss account.

QUESTION 27

AB Ltd. launched a project for producing product X in October, 20X1. The Company incurred ₹ 20 lakhs towards Research. Due to prevailing market conditions, the Management came to conclusion that the product cannot be manufactured and sold in the market for the next 10 years. The Management hence wants to defer the expenditure write off to future years.

Advise the Company as per the applicable Accounting Standard.

SOLUTION:

As per para 41 of AS 26 "Intangible Assets", expenditure on research should be recognised as an expense when it is incurred. Hence, the expenses amounting ₹ 20 lakhs incurred on the research has to be charged to the statement of profit and loss in the current year ending 31st March, 20X2.

QUESTION 28

During 20X1-X2, an enterprise incurred costs to develop and produce a routine low risk computer software product, as follows:

Particular	₹
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.

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, ₹ 90,000 would be recorded as an expense (₹ 50,000 for completion of detailed program design and ₹ 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) = ₹1,00,500. Packing cost ₹ 16,500 should be recognized as expenses and charged to P & L A/c.

QUESTION 29 (CA INTER NOV 2019)(5 MARKS)

As per provisions of AS-26, how would you deal to the following situations:

(1) ₹ 23,00,000 paid by a manufacturing company to the legal advisor for defending the patent of a product is treated as a capital expenditure.

(2) During the year 2018-19, a company spent ₹ 7,00,000 for publicity and research expenses on one of its new consumer product which was marketed in the same accounting year but proved to be a failure.

(3) A company spent ₹ 25,00,000 in the past three years to develop a product, these expenses were charged to profit and loss account since they did not meet AS-26 criteria for capitalization. In the current year approval of the concerned authority has been received. The company wishes to capitalize ₹ 25,00,000 by disclosing it as a prior period item.

(4) A company with a turnover of ₹ 200 crores and an annual advertising budget of ₹ 50,00,000 had taken up for the marketing of a new product by a company. It was estimated that the company would have a turnover of ₹ 20 crore from the new product.

The company had debited to its Profit & Loss Account the total expenditure of ₹ 50,00,000 incurred on extensive special initial advertisement campaign for the new product.

SOLUTION:

As per AS 26 "Intangible Assets", subsequent expenditure on an intangible asset after its purchase or its completion should be recognized as an expense when it is incurred unless (a) it is probable that the expenditure will enable the asset to generate future economic benefits in excess of its originally assessed standard of performance; and (b) expenditure can be measured and attributed to the asset reliably. If these conditions are met, the subsequent expenditure should be added to the cost of the intangible asset.

(i) In the given case, the legal expenses to defend the patent of a product amounting ₹ 23,00,000 should not be capitalized and be charged to Profit and Loss Statement.

(ii) The company is required to expense the entire amount of ₹ 7,00,000 in the Profit and Loss account for the year ended 31st March, 2019 because no benefit will arise in the future.

(iii) As per AS 26, expenditure on an intangible item that was initially recognized as an expense by a reporting enterprise in previous annual financial statements should not be recognized as part of the cost of an intangible asset at a later date. Thus the company cannot capitalize the amount of ₹ 25,00,000 and it should be recognized as expense

(iv) Expenditure of ₹ 50,00,000 on advertising and promotional activities should always be charged to Profit and Loss Statement. Hence, the company has done the correct treatment by debiting the sum of 50 lakhs to Profit and Loss Account.

QUESTION 30 (CA INTER NOV 2020) (5MARKS)

Swift Limited acquired patent rights to manufacture Solar Roof Top Panels at a cost of ₹ 600 lacs. The product life cycle has been estimated to be 5 years and the amortization was decided in the ratio of future cash flows which are estimated as under:

Year	1	2	3	4	5
Cash Flows (₹ in lacs)	300	300	300	150	150

After 3rd year, it was estimated that the patents would have an estimated balance future life of 3 years and Swift Ltd. expected the estimated cash flow after 5th year to be ₹ 75 Lacs. Determine the amortization cost of the patent for each of the above years as per Accounting Standard 26.

SOLUTION:

AMORTIZATION OF COST OF PATENT AS PER AS 26

Year	Estimated future cash flow (₹ in lakhs)	Amortization Ratio	Amortized Amount (₹ in lakhs)
1	300	.25	150
2	300	.25	150
3	300	.25	150
4	150	.10	60
5	150	.10	60
6	75	.05	30
		1.00	600

In the first three years, the patent cost will be amortized in the ratio of estimated future cash flows i.e. (300: 300: 300: 150: 150).The unamortized amount of the patent after third year will be ₹ 150 lakh (600-450) which will be amortized in the ratio of revised estimated future cash flows (150:150:75 or 2:2:1) in the fourth, fifth and sixth year.

QUESTION 31 (CA INTER NOV 2020 EXAMS)

M/s. Pasa Ltd. is developing a new production process. During the financial year ended 31st March, 2019, the total expenditure incurred on the process was ₹ 80 lakhs. The production process met the criteria for recognition as an intangible asset on 1st November, 2018. Expenditure incurred till this date was ₹ 42 lakhs.

Further expenditure incurred on the process for the financial year ending 31st March, 2020 was ₹ 90 lakhs. As on 31.03.2020, the recoverable amount of know how embodied in the process is estimated to be ₹ 82 lakhs. This includes estimates of future cash outflows and inflows.

You are required to work out :

(1) What is the expenditure to be charged to Profit and Loss Account for the year ended 31st March, 2019 ?

(2) What is the carrying amount of the intangible asset as on 31st March, 2019?

(3) What amount of expenditure to be charged to Profit and Loss Account for the year ended 31st March, 2020?

What is the carrying amount of the intangible asset as on 31st March, 2020?

SOLUTION:

As per AS 26 'Intangible Assets'

(i) Expenditure to be charged to Profit and Loss account for the year ending 31.03.2019

₹ 42 lakhs is recognized as an expense because the recognition criteria were not met until 1st November, 2018. This expenditure will not form part of the cost of the production process recognized as an intangible asset in the balance sheet.

(ii) Carrying value of intangible asset as on 31.03.2019

At the end of financial year, on 31st March 2019, the production process will be recognized (i.e. carrying amount) as an intangible asset at a cost of ₹ 38 (80-42) lakhs (expenditure incurred since the date the recognition criteria were met, i.e., from 1st November 2018)

(iii) Expenditure to be charged to Profit and Loss account for the year ended 31.03.2020

	(₹ in lacs)
Carrying Amount as on 31.03.2019	38
Expenditure during 2019 – 2020	90
Book Value	128
Recoverable Amount	(82)
Impairment loss to be charged to Profit and loss account	46

₹ 46 lakhs to be charged to Profit and loss account for the year ending 31.03.2020.

(iv) Carrying value of intangible asset as on 31.03.2020

	(₹ in lacs)
Book Value	128
Less: Impairment loss	(46)
Carrying amount as on 31.03.2020	82

QUESTION 32 (CA INTER JAN 21 EXAMS)

(a) A Company acquired for its internal use a software on 01.03.2020 from U.K. for £ 1,50,000. The exchange rate on the date was as ₹ 100 per £. The seller allowed trade discount @ 2.5%. The other expenditures were:

(i) Import Duty 10%

(ii) Additional Import Duty 5%

(iii) Entry Tax 2% (Recoverable later from tax department).

(iv) Installation expenses ₹ 1,50,000.

(v) Professional fees for clearance from customs ₹ 50,000.

Compute the cost of software to be Capitalized as per relevant AS.

SOLUTION:

(a) Calculation of cost of software (intangible asset) acquired for internal use

Purchase cost of the software	£ 1,50,000
Less: Trade discount @ 2.5%	£ (3,750)
	£1,46,250
Cost in ₹ (UK £1,46,250 x ₹ 100)	146,25,000
Add: Import duty on cost @ 10%	14,62,500
	160,87,500
Add: Additional import duty @ 5%	8,04,375
	168,91,875
Add: Installation expenses	1,50,000
Add: Professional fee for clearance from customs (₹)	50,000
Cost of the software to be capitalized (₹)	170,91,875

Note: Since entry tax has been mentioned as a recoverable / refundable tax, it is not included as part of the cost of the asset.

QUESTION 33

K Ltd. launched a project for producing product X in October, 2016. The Company incurred ₹ 40 lakhs towards Research and Development expenses upto 31st March, 2017. Due to prevailing market conditions, the Management came to conclusion that the product cannot be manufactured and sold in the market for the next 10 years. The Management hence wants to defer the expenditure write off to future years.

You are required to advise the Company as per the applicable Accounting Standard.

SOLUTION

As per provisions of AS 26 "Intangible Assets", expenditure on research should be recognized as an expense when it is incurred. An intangible asset arising from development (or from the development phase of an internal project) should be recognized if, and only if, an enterprise can demonstrate all of the conditions specified in para 44 of the standard. An intangible asset (arising from development) should be derecognized when no future economic benefits are expected from its use according to para 87 of the standard. Thus, the manager cannot defer the expenditure write off to future years in the given case. Hence, the expenses amounting ₹ 40 lakhs incurred on the research and development project has to be written off in the current year ending 31st March, 2017.

QUESTION 34

A Company with a turnover of ₹ 375 crores and an annual advertising budget of ₹ 3 crores had taken up the marketing of a new product. It was estimated that the company would have a turnover of ₹ 37.5 croes from the new product. The company had debited to its Profit and Loss account the total expenditure of ₹ 3 crores incurred on extensive special initial advertisement campaign for the new product.

Is the procedure adopted by the Company correct?

SOLUTION

According to AS 26 'Intangible Assets', "expenditure on an intangible item should be recognized as an expense when it is incurred unless it forms part of the cost of an intangible asset".

In the given case, advertisement expenditure of ₹ 3 crores had been taken up for the marketing of a new product which may provide future economic benefits to an enterprise by having a turnover of ₹37.5 crores. Here, no intangible asset or another asset is acquired or created that can be recognized.

Therefore, the accounting treatment by the company of debiting the entire advertising expenditure of ₹3 crores to the Profit and Loss account of the year is correct.

QUESTION 35

X Ltd. carried on business of manufacturing of Bakery products. The company has two trademarks "Sun" and "Surya". One month before the company knows 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 36

A company is showing an intangible asset at ₹ 88 lakhs as on 01.04.2021. This asset was acquired for ₹ 120 lakhs on 01.04.2017 and the same was available for use from that date. The company has been following the policy of amortization of the intangible assets over a period of 15 years on straight line basis. Comment on the accounting treatment of the above with reference to the relevant Accounting Standard.

SOLUTION

As per AS 26 'Intangible Assets', the depreciable amount of an intangible asset should be allocated on systematic basis over the best estimate of its useful life. There is a rebuttable presumption that the useful life of an intangible asset will not exceed ten years from the date when the asset is available for use. Company has been following the policy of amortization of the intangible asset over a period of 15 years on straight line basis. The period of 15 years is more than the maximum period of 10 years specified as per AS 26. Accordingly, the company would be required to restate the carrying amount of intangible asset as on 01.04.2021 at ₹ 72 lakhs i.e.

$$\text{₹ 120 lakhs less ₹ 48 lakhs } \left(\frac{\text{₹ 120 lakhs}}{\text{10 years}} \times \text{4 years = 48 lakhs}\right)$$

The difference of ₹ 16 Lakhs (₹ 88 lakhs – ₹ 72 lakhs) will be adjusted against the opening balance of revenue reserve. The carrying amount of ₹ 72 lakhs will be amortized over remaining 6 years by amortizing ₹ 12 lakhs per year.

QUESTION 37

(a) PQR Ltd. has acquired a Brand from another company for ₹ 100 lakhs. PQR Ltd. contends that since the said brand is a very popular and famous brand, no amortization needs to be provided. Comment on this in line with the Accounting Standards.

(b) X Ltd. is engaged in the business of newspaper and radio broadcasting. It operatesthrough different brand names. During the year ended 31st March, 2021, it incurred substantial amount on business communication and branding expenses by participation in various corporate social responsibility initiatives. The company expects to benefit by this expenditure by attracting new customers over a period of time and accordingly it has capitalized the same under brand development expenses and intends to amortize the same over the period in which it expects the benefits to flow. As the accountant of the company do you concur with these views? You are required to explain in line with provisions of Accounting Standards.

SOLUTION

(a) AS 26 'Intangible Assets" provides that an intangible asset should be measured initially at cost. After initial recognition, an intangible asset should be carried at cost less any accumulated amortization and any accumulated impairment losses. The amount of an intangible asset should be allocated on a systematic basis over the best estimate of its useful life for computing amortization. There is a rebuttable presumption that the useful life of an intangible asset will not exceed 10 years from the date when the asset is available for use. It must be ensured that the value of brand is amortized in accordance with AS 26, as brand is considered to be intangible asset. The contention of PQR Ltd. that Brand is very popular and famous, hence no amortization needs to be provided is not correct as there is no persuasive evidence that the useful life of the intangible asset will exceed 10 years.

(b) As per AS 26 on Intangible Assets, expenditure on an intangible item should be recognized as on expense when it is incurred unless it forms part of the cost of an intangible asset that meets the recognition criteria. An intangible asset should be recognized if, and only if: (i) it is probable that the future economic benefits that are attributable to the asset will flow to the enterprise; and (ii) the cost of the asset can be measured reliably. In the given case, no intangible assets or other asset is acquired or created that can be recognized, the accounting treatment by the company to amortize the entire expenditure over the period in which it expects the benefits to flow is not correct and the same should be debited to the profit and loss statement during the year ended 31st March, 2021.

QUESTION 38

K Ltd. launched a project for producing product X in October, 2021. The Company incurred ₹ 40 lakhs towards Research and Development expenses upto 31 st March, 2022. Due to prevailing market conditions, the Management came to conclusion that the product cannot be manufactured and sold in the market for the next 10 years. The Management hence wants to defer the expenditure write off to future years.

Advise the Company as per the applicable Accounting Standard.

SOLUTION

As per AS 26 "Intangible Assets", expenditure on research should be recognized as an expense when it is incurred. An intangible asset arising from development (or from the development phase of an internal project) should be recognized if, and only if, an enterprise can demonstrate all of the conditions specified in the standard. An intangible asset (arising from development) should be derecognised when no future economic benefits are expected from its use according to the standard. Thus, the manager cannot defer the expenditure write off to future years in the given case.

Hence, the expenses amounting ₹ 40 lakhs incurred on the research and development project has to be written off in the current year ending 31 st March, 2022.

QUESTION 39

PIL Ltd. is showing an intangible asset at ₹ 72 lakhs as on 31-3-2022. This asset was acquired for ₹ 120 lakhs as on 01-04-2016 and the same was used from that date. The company has been following the policy of amortization of the intangible assets over a period of 15 years, on straight line basis.

You are required to comment on the accounting treatment of asset with reference to AS 26 "Intangible Assets" and also give the necessary rectification journal entry in the books.

SOLUTION

As per AS 26 'Intangible Assets', the depreciable amount of an intangible asset should be allocated on systematic basis over the best estimate of its useful life. There is a rebuttable presumption that the useful life of an intangible asset will not exceed ten years from the date when the asset is available for use. The Company has been following the policy of amortization of the intangible asset over a period of 15 years on straight line basis. The period of 15 years is more than the maximum period of 10 years specified as per AS 26.

Accordingly, the company would be required to restate the carrying amount of intangible asset as on 31.3.2022 at ₹ 48 lakhs i.e. ₹ 120 lakhs less ₹ 72 lakhs (₹ 120 Lakhs / 10 years x 6 years = 72 Lakhs). The difference of ₹ 24 Lakhs (₹ 72 lakhs – ₹ 48 lakhs) will be adjusted against the opening balance of revenue reserve. The carrying amount of ₹ 48 lakhs will be amortized over remaining 4 years by amortizing ₹ 12 lakhs per year.

The necessary journal entry (for rectification) will be

Revenue Reserves	Dr.	₹ 24 Lakhs	
To Intangible Assets			₹ 24 Lakhs

(Adjustment to reserves due to restatement of the carrying amount of intangible asset)

QUESTION 40 (CA INTER DEC. 2021 EXAMS : 5 MARKS)

Surgical Ltd, is developing a new production process of surgical equipment. During the financial year ended 31st March 2020 the total expenditure incurred on the process was ₹ 67 lakhs. The production process met the criteria for recognition as an intangible asset on 1st January 2020. Expenditure incurred till this date was ₹ 35 lakhs.

Further expenditure incurred on the process for the financial year ending 31st March 2021 ₹ 105 lakhs. As on 31st March 2021, the recoverable amount of technique embodied in the process is estimated to be ₹ 89 lakhs. This includes estimates of future cash outflows and inflows.

Under the provisions of AS 26, you are required to ascertain:

(i) The expenditure to be charged to Profit and Loss Account for the year ended 31st March 2020;

(ii) Carrying amount of the intangible asset as on 31st March 2020;

(iii) Expenditure to be charged to Profit and Loss Account for the year ended 31 st March 2021;

(iv) Carrying amount of the intangible asset as on 31st March 2021.

SOLUTION :

As per AS 26 'Intangible Assets'

(i) **Expenditure to be charged to Profit and Loss account for the year ended 31.03.2020**

₹ 35 lakhs is recognized as an expense because the recognition criteria were not met until 1stJanuary 2020. This expenditure will not form part of the cost of the production process recognized as an intangible asset in the balance sheet.

(ii) **Carrying value of intangible asset as on 31.03.2020**

At the end of financial year, on 31st March 2020, the production process will be recognized (i.e. carrying amount) as an intangible asset at a cost of ₹ 32 (67-35) lacs (expenditure incurred since the date the recognition criteria were met, i.e., from 1stJanuary 2020).

(iii) **Expenditure to be charged to Profit and Loss account for the year ended 31.03.2021**

	(₹ in lacs)
Carrying Amount as on 31.03.2020	32
Expenditure during 2020 – 2021	105
Book Value	137
Recoverable Amount	(89)
Impairment loss	48

₹ 48 lakhs to be charged to Profit and loss account for the year ending 31.03.2021.

(iv) **Carrying value of intangible asset as on 31.03.2021**

	(₹ in lacs)
Book Value	137
Less: Impairment loss	(48)
Carrying amount as on 31.03.2021	89

ACCOUNTING STANDARD 12

ACCOUNTING FOR GOVERNMENT GRANTS

QUESTION 1

Krithivasa Ltd. received an area of Land, free of cost, from the Government. This amount is not recorded at all. The Company argues that – (a) No money has been spent by the Company on its acquisition, and (b) Land is not a depreciable assets, Comment.

SOLUTION

1. Principle: Non-Monetary Grants/Assets received free of cost, are recorded at a Nominal Value for the purposes of identification and control) . Whether it is depreciable or non-depreciable is not relevant in this regard.
2. Conclusion: As per AS-12, the above Land should be recorded at a Nominal Value, for identification and control purposes. Hence, the Company's stand is not in accordance with AS-12.

QUESTION NO 2

Ram Ltd. purchased a Machinery for ₹1.00 Crore. The State Government granted the Company a subsidy of ₹40 Lakhs to meet partial cost of Machinery. The Company credited the Subsidy received from the State Government to its Profit and Loss Account for the year ended 31st March. Comment on the above.

SOLUTION

1. Principle: Where a Government Grant is received towards a specific depreciable Fixed Asset, it should be accounted for either under Cost Reduction Method or Deferred Income Method.
2. Conclusion: The accounting treatment of the Company, i.e. crediting P&L A/c. is incorrect.

QUESTION NO 3

Haribhakti Ltd. acquired the Fixed Asset of ₹ 100 Lakhs on which it received a Grant of ₹ 10 Lakhs. What will be the cost of the Fixed Assets as per AS-12 and how it will be disclosed in the Financial Statements?

SOLUTION

Principle: Where a Government Grant is received towards a specific depreciable Fixed Assets, it should be accounted for either under Cost Reduction Method or Deferred Income Method. The accounting will be as under:-

1. Asset Reduction Method: Cost ₹ 100 Lakhs Less Grant ₹ 10 Lakhs = ₹ 90 Lakhs will be the Carrying Amount, and written off over its useful life.
2. Deferred Income Method: ₹ 10 Lakhs in Deferred Income Account shall be shown in Balance Sheet separately under an appropriate head. A portion of this ₹ 10 Lakhs will be credited to P&L A/c. every year, over the useful life of the asset.

QUESTION NO 4

Gowri Shankar Ltd. purchased a special machinery on 1st April of a Financial year, for ₹ 25 Lakhs. It received a Government Grant for 20% of the Price. The machine has an effective life of 10 years. Advise the Company of the accounting treatment(s)

SOLUTION

Under AS-12, where the Grant relates to a specific depreciable Fixed Asset, the Company can follow any of the following accounting methods, as illustrated below:-

Particulars	Cost Reduction Method	Deferred Income Method
1. Original Cost of Machinery	₹ 25 Lakhs	₹ 25 Lakhs
2. Scarp Value of Asset	Nil	Nil
3. Specific Grant Received	₹ 5 Lakhs (reduced from cost).	₹ 5 Lakhs (treated as Deferred Income)
4. Depreciable Value (1)-(2)-(3)	₹ 20 Lakhs	₹ 25 Lakhs
5. Useful Life of Machinery	10 Years	10 Years
6. Depreciation provided p.a. (4) ÷ (5)	₹ 2 Lakhs	₹ 2.5 Lakhs
7. Other Income credited to P&L A/c. every year	Not applicable	(3) ÷ (5) ₹ 0.5 Lakhs

Note: The balance in the Deferred Income Account shall be shown in the Balance Sheet separately as 'Deferred Government Grants' under an appropriate head.

QUESTION NO 5

Kripanidhi Ltd. purchased a Fixed Asset for ₹ 75 Lakhs, which has an estimated useful life of 5 years, with the Salvage Value of ₹ 7,50,000. On Purchase of the Asset, the Government have the Company a grant of ₹ 15 Lakhs. Pass the necessary journal entries in the books of the Company for the first two years.

SOLUTION

Journal Entries under Asset Cost Reduction Method

(₹ in Lakhs)

Year	Particulars		Dr.	Cr.
1	Machinery A/c.	Dr.	75.00	
	To Bank A/c.			75.00
	(Being Machinery Purchased)			
	Bank A/c.	Dr.	15.00	
	To Machinery A/c.			15.00
	(Being Government Grant received and credited to Fixed Asset A/c.)			
	Depreciation A/c. (Cost 75 (-) Grant 15 (-) Salvage Dr. Value 7.5) ÷ 5 Years		10.50	10.50
	To Machinery A/c.			
	(Being Depreciation Charged on Straight Line Method on Cost net of Grant & SV)			
	Profit & Loss A/c.	Dr.	10.50	
	To Depreciation A/c.			10.50
	(Being Depreciation transferred to P&L A/c.)			
2.	Depreciation A/c.	Dr.	10.50	
	To Machinery A/c.			10.50
	(Being Depreciation charged on Straight line method)			
	Profit & Loss A/c.	Dr.	10.50	
	To Depreciation A/c.			10.50
	(Being Depreciation transferred to P&L A/c.)			

Journal Entries under Deferred Income Method

(₹ in Lakhs)

Year	Particulars		Dr.	Cr.
1	Machinery A/c.	Dr.	75.00	
	To Bank A/c.			75.00
	(Being Machinery Purchased)			
	Bank A/c.	Dr.	15.00	
	To Deferred Income			15.00
	(Being Government Grant received as Deferred Income)			
	Government Grants Deferred Income A/c. (15 Lakhs ÷ 5 years)		3.00	
	To Profit & Loss A/c.			3.00
	(Being Grant Portion for this year, considered as Income in P&L A/c).			
	Depreciation A/c. (Cost 75 (-) Salvage Value 7.5) ÷ 5 Years		13.50	
	To Machinery A/c.			13.50
	(Being Depreciation Charged on Straight Line Method on Cost net of Grant & SV)			
	Profit & Loss A/c.	Dr.	13.50	
	To Depreciation A/c.			13.50
	(Being Depreciation transferred to P&L A/c.)			
2.	Government Grants Deferred Income A/c. (15 Lakhs ÷ 5 Years)		3.00	
	To Profit & Loss A/c.			3.00
	(Being Grant portion for this year, considered as Income in P&L A/c.)			
	Depreciation A/c.	Dr.	13.50	
	To Machinery A/c.			13.50
	(Being Depreciation charged on Straight line method)			

Profit & Loss A/c.	Dr.	13.50	
To Depreciation A/c.			13.50
(Being Depreciation transferred to P&L A/c.)			

QUESTION NO 6

Bhava Limited purchased a Machinery for ₹ 25,00,000 which has an Estimated Useful Life of 10 years and a Salvage Value of ₹ 5,00,000. On Purchase of the Assets, the Central Government pays a Grant for ₹ 5,00,000.

Pass the Journal Entries with narrations in the books of the Company for the first year, treating Grant as Deferred income.

SOLUTION

Journal Entries under Deferred Income Method

(₹ in Lakhs)

Year	Particulars		Dr.	Cr.
1	Machinery A/c.	Dr.	25.00	
	To Bank A/c.			25.00
	(Being Machinery Purchased)			
2	Bank A/c.	Dr.	5.00	
	To Government Grants Deferred Income A/c.			5.00
	(Being Government Grant received and retained as Deferred Income)			
3	Government Grants Deferred Income A/c. (5 Lakhs ÷ 10 years)	Dr	0.50	
	To Profit & Loss A/c.			0.50
	(Being Grant Portion for this year, considered as Income in P&L A/c.)			
4	Depreciation A/c. (Cost 25 (-) Salvage Value 5) ÷ 10 Years	Dr.	2.00	
	To Machinery A/c.			2.00
	(Being Depreciation Charged on Straight Line Method on Cost net of Grant & Salvage value)			

5	Profit & Loss A/c.	Dr.		
	To Depreciation A/c.		2.00	2.00
	(Being Depreciation transferred to P&L A/c.)			

QUESTION NO 7

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 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

1. ₹ 8 Crores is in the nature of Promoter's Contribution, and hence should be transferred to Capital Reserve. Its distribution as Dividend is inappropriate.
2. Land received free of cost, being Non-Monetary Grant, should be recorded at Nominal Value.

QUESTION NO 8

Supriya Ltd. received a grant of ₹ 2,500 Lakhs from the Government during the last accounting year for welfare activities to be carried on by the Company for its Employees. The Grant prescribed conditions for its utilization. However, during the current year, it was found that the conditions of Grants wee not complied with and the Grant had to be refunded to the Government in full. Explain the accounting treatment, under AS-12.

1. The above Grant is in the nature of Revenue Grant, since it is for welfare activities for its Employees. Therefore, when received, it should have been credited to P&L Account.
2. Therefore, in the event of refund, the amount refunded should be debited to P&L account.
3. Such debt should be shown as an Extra Ordinary item in the P&L Statement.

QUESTION NO 9

Three years ago, Sankara Ltd. had received Subsidy of ₹ 25 Lakhs from Government by way of contribution towards its Total Capital Outlay. However, due to non-fulfilment of some specified conditions. ₹ 16 Lakhs was recovered by the Government during the current accounting year. Discuss the accounting treatment.

SOLUTION

Principle: Where a Grant, which is in the nature of Promoter's Contribution becomes refundable to the Government, in part or in full, due to non- fulfillment of some specified conditions, the relevant amount recoverable by the Government is reduced from the Capital Reserve.

Conclusion: In the above case, the amount of ₹ 16 Lakhs should be reduced from the Capital Reserve. The balance in the Capital Reserve will be ₹ 9 Lakhs.

QUESTION NO 10

Neelakanta Ltd. purchased a Machinery for ₹ 40 Lakhs (Useful Life 4 years and Residual value ₹ 8 Lakhs). Government Grant received is ₹ 16 Lakhs. Due to non- compliance of certain condition, the Grant become refundable in 3rd year to the extent of ₹ 12 Lakhs. Show the Journal Entry to be passed at the time of refund of Grant and the value of the Fixed Assets, if (a) the Grant is credited to Fixed Assets (b) the Grant is credited to Deferred Grant A/c.

A. If Grant is credited to Fixed Assets (i.e. Assets Cost Reduction Method)

Particulars		Dr. (₹)	Cr. (₹)
Fixed Assets A/c.	Dr.	12,00,000	
To Bank A/c.			12,00,000
(Being Grant refunded to the Government on non-compliance of related conditions, and Cost of the Asset thereby increased) (See Note below)			

* Depreciation p.a. = $\dfrac{\text{Cost 40 Lakhs – Grant 16 Lakhs – Residual Value 8 Lakhs}}{\text{4 Years Useful Life}}$

= ₹ 4,00,000 p.a.

- WDV of Asset before the above Journal Entry = Cost ₹40,00,000 less Grant Credited at inception ₹ 16,00,000 less Depreciation of ₹ 4,00,000 for 2 years = ₹16,00,000
- Carrying Book Value of Asset after above Journal Entry = ₹16,00,000 + ₹12,00,000 = ₹ 28,00,000

B. If Grant is credited to Deferred Grant A/c. (i.e. Deferred Income Method)

Particulars		Dr. (₹)	Cr. (₹)
Deferred Government Grant A/c.	Dr.	8,00,000	
Profit and Loss A/c.	Dr.	4,00,000	
To Bank A/c.			12,00,000
(Being Grant refunded to Government, and excess provided from Profit & Loss A/c).			

- Depreciation p.a. under Deferred Income Method

  $$= \frac{\text{Cost 40 Lakhs – Residual Value 8 Lakhs}}{\text{4 Years Useful Life}}$$

  = ₹ 8,00,000 p.a.
- WDV of Asset at beginning of year 3 = Cost ₹40,00,000 less Depreciation of ₹ 8,00,000 for 2 years = ₹24,00,000
- Balance of Deferred Grant at the end of 2 years ₹16,00,000 – (₹4,00,000 x 2 years) = ₹ 8,00,000
- There will not be any change in the Carrying Amount of the Asset.

QUESTION NO 11

Srikanta Ltd. received a specific grant of ₹ 30 Lakhs for acquiring the Plant of ₹150 Lakhs during 2010-11 having useful life of 10 years. The Grant received was credited to Deferred Income in the Balance Sheet. During 2013- 14, due to non-compliance of conditions laid down, for the grant, the Company had to refund the whole grant to the Government Balance in the Deferred Income on that date was ₹ 21 Lakhs and Written Down Value of Plant was ₹ 105 Lakhs.

SOLUTION

If Grant is credited to Deferred Grant A/c. (i.e. Deferred Income Method)

Particulars		Dr. (₹)	Cr. (₹)
Deferred Government Grant A/c.	Dr.(given)	21,00,000	
Profit and Loss A/c.	Dr.(balancing figure)	9,00,000	
To Bank A/c.			30,00,000
(Being Grant refunded to Government, and excess provided from Profit & Loss A/c).			

Note: There will not be any change in the carrying Amount of the Asset. Depreciation will be charged on the same basis as charged in the earlier years.

QUESTION NO 12

Markandeya Ltd. applied for a Government Grant for purchase of a special machinery. The machinery costs ₹ 80 Lakhs and the Grant was ₹ 30 Lakhs. The Machinery has a useful life of 10 years and the Company follows SLM Depreciation. The Grant was promptly received but certain conditions regarding production were attached to it. Four years later, an amount of ₹ 4 Lakhs become refundable to the Government since the Company did not adhere to the conditions imposed earlier. Explain the accounting treatment.

SOLUTION

1.	Where Asset Cost Reduction Method is followed:		
	(a)	Original cost of the Machinery	₹ 80 Lakhs
	(b)	Government Grant reduced from cost	₹ 30 Lakhs
	(c)	Depreciable Amount of Machinery (a-b)	₹ 50 Lakhs
	(d)	Usefull Life	10 Years
	(e)	Depreciation per annum (c ÷ d)	₹ 5 Lakhs
	(f)	Accumulated Depreciation for four years	₹ 20 Lakhs (₹ 5 Lakhs x 4 years)
	(g)	Book Value of the asset in fourth year	₹30 Lakhs (₹ 50 Lakhs – ₹20 Lakhs)
	(h)	Add back: Amount of Refundable Grant	₹ 4 Lakhs
	(i)	Revised Book Value of Machinery (g + h)	₹ 34 Lakhs
	(j)	Balance Useful Life	10-4 = 6 years
	(k)	Depreciation to be provided for next 6 years	34 ÷ 6 = ₹ 5.67 Lakhs per annum
2.	Where Deferred Income Method is followed:		
	(a)	Original cost of the Machinery	₹ 80 Lakhs
	(b)	Usefull Life	10 Years
	(c)	Depreciation per annum	₹8 Lakhs
	(d)	Government Grant treated as Deferre income	₹ 30 Lakhs

(e)	Amount allocated/credited to P&L A/c. every year	₹ 3 Lakhs (₹ 30 Lakhs 10 ÷ years)
(f)	Total Amount credited to P&L for our years	₹ 12 Lakhs
(g)	Balance in Deferred Income Account for 4th year	₹18 Lakhs (₹ 30 Lakhs – ₹12 Lakhs)
(h)	Less: Grant Refundable – now adjusted	₹ 4 Lakhs
(i)	Revised Balance in Deferred Income Account	₹ 14 Lakhs
(j)	Amount to be credited to P&L for next 6 years	₹ 2.33 Lakhs (₹ 14 Lakhs 6 ÷ years)

QUESTION NO 13

A Fixed Asset is purchased for ₹ 20 Lakhs. Government Grant received towards it is R. 8 Lakhs. Residual value is ₹ 4 Lakhs and useful life is 4 years. Assumed SLM Depreciation. Asset is shown net of Grant. After 1 years, Grant becomes refundable to the extent of ₹ 5 Lakhs due to non- compliance with conditions. Pass Journal Entries.

SOLUTION

Year	Particulars		Dr.	Cr.
1	Fixed Assets A/c.	Dr.	20,00,000	
	To Bank A/c.			20,00,000
	(Being Purchased of Fixed Asset for ₹20,00,000			
2	Bank A/c.	Dr.	8,00,000	
	To Fixed Asset A/c.			8,00,000
	(Being Grant recorded as reduction from Cost of Asset)			
3	Depreciation A/c.	Dr.	2,00,000	
	To Fixed Asset A/c.			2,00,000
	(Being Depreciation for year of acquisition, under SLM before Grant Refund) (Note 1)			

4	Fixed Assets A/c.	Dr.	5,00,000	
	To Bank A/c.			5,00,000
	(Being grant refunded to Government on non-compliance of related conditions and cost of the asset thereby increased).			
5	Depreciation A/c.	Dr	3,66,667	
	To Fixed Assets A/c.			3,66,667
	(Being depreciation charged on Fixed Asset under SLM after Grant Refund (Note 2)			

Note:

1. Depreciation (before Grant Refund) =

$$= \frac{\text{Cost } 20{,}00{,}000 \text{ (–) Grant } 8{,}00{,}000 \text{ – Residual Value } 4{,}00{,}000}{\text{4 Years Useful Life}}$$

= ₹ 2,00,000

2. Depreciation (after Grant Refund) =

$$= \frac{\text{WDV } 10{,}00{,}000 \text{ (+) Grant } 5{,}00{,}000 \text{ – Residual Value } 4{,}00{,}000}{\text{Balance Useful Life 3 Years}}$$

= ₹ 3,66,667

QUESTION NO 14

Shivam Ltd. acquired a Fixed Asset for ₹ 50,00,000. The estimated useful life of the asset is 5 years. The salvage value after useful life was estimated at ₹ 5,00,000. The State Government gave a grant of ₹ 10,00,000 to encourage the asset acquisition. At the end of the second year, the subsidy of the State Government became refundable. What is the Fixed Asset value after refund of Grant/Subsidy to the State Government but before amortising the asset value at the end of the second year?

SOLUTION

Particulars	₹
Original Cost of Fixed Assets	50,00,000
Less: State Government Grant received	(10,00,000)
	40,00,000
Less: Amount to be written off in the first year (40,00,000 – 5,00,000) ÷ 5 years	(7,00,000)
Add: Refund of State Government Grant.	10,00,000
Value of Fixed Assets, at the end of the 2nd year, after refund but before depreciation.	43,00,000

QUESTION NO 15

On 1st April 2010, Sundaram Ltd. received a Government Grant of ₹ 300 Lakhs for acquisition of a Machinery costing ₹ 1,500 Lakhs. The Grant was credited to the cost of the Asset. The life of the Machinery is 5 years. The Machinery is depreciated at20% on WDV basis. The Company had to refund the Grant in May 2013 due to non-fulfillment of certain conditions. How you would deal with the refund of Grant?

SOLUTION

Particulars		₹
Original Cost of the Machinery		1,500
Less: Government Grant	(Reduced from Cost)	(300)
Depreciable Cost as on 1.4.2009		1,200
Less: Depreciation for 2010-11	(₹1,200 x 20%)	(240)
WDV on 1.4.2011		960
Less: Depreciation for 2011-12	(₹ 960 x 20%)	(192)
WDV on 1.4.2012		768
Less: Depreciation for 2012-13	(₹ 78 x 20%)	(154)
WDV on 1.4.2013		614
Add: Refundable Government Grant		300
Revised Book Value of Machinery		914

QUESTION NO 16

A Steel Manufacturing Company has a turnover of Rs, 45 Crores and Net Tax Profit of ₹ 6 Crores. The company's financial year ends on 31st March. The Company's policy is to treat Grants received in respect of Fixed Assets as Deferred income and to deduct all Grants identified as relating to specific revenue expenditure against that expenditure. All other Grants recognized are credited to P&L Account. Answer the following questions:-

A. During the year the Company received a Grant from the Defence Department of Government of India for ₹3,00,000 towards the cost of new equipment. The equipment has an estimated useful economic life of 10 years and cost ₹ 7,00,000. The Company policy is to depreciate all depreciable Fixed Assets by the Straight Line Method.

B. During the year, the Company spent ₹ 70,000 on training in respect of which it is due to receive Government Grant of 50%. The Grant formalities year.

C. In October, a Grant of ₹ 40,000 was received from the Government in recognition of the high quality that the Company's production had maintained over the five years, which had ended on 31st March, the previous accounting year.

SOLUTION

Situation A : The Government Grant has been received relating to specific Fixed Assets. There are two methods for dealing with the Grant in the books:-

Particulars	Asset Cost Reduction Method	Deferred Income Method
1. Original Cost of Equipment	₹7,00,000	₹7,00,000
2. Specific Grant Received	₹ 3,00,000 (reduced from Cost)	₹ 3,00,000
3. Depreciable Value (1)-(2)	₹ 4,00,000	₹ 7,00,000
4. Useful Life of Machinery	10 Years	10 Years
5. Depreciation Provided p.a. (3)- (4)	₹ 40,000	₹ 70,000
6. Other Income credited to P&L A/c. every year	Not Applicable	(2) ÷ (4) ₹30,000

Note: The balance in the Deferred Income Account shall be shown in the Balance Sheet separately with a description, as 'Deferred Government Grants' under the appropriate head.

Situation B : The Government Grant to be received can be shown either as income or as deduction from Training Expenses. As the Grant has not been received till the year end, it has to be shown as Receivable.

Situation C : This is not a Grant related to specific Fixed Asset or for conditions to be complied in future. This Grant should be credited to P&L Account in the year of receipt only.

QUESTION NO 17

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 ₹ 80 Crores in the eligible investments. The Company is eligible for the Subsidy and has received ₹ 20 Crores from the Government in February 2014. The Company wants to recognize the said Subsidy as of the Company in accordance with the Accounting Standards?

SOLUTION

1. The Government Grants may be in the nature of Promoters' Contribution, i.e.
   (a) they are given with reference to the Total Investment in an undertaking, or
   (b) by way of contribution towards its total Capital Outlay, (e.g. Central Investment Subsidy Scheme).
2. They cannot be shown as income in the Profit and Loss Account. Such Grants are not ordinarily expected to be repaid. Hence, they are treated as Capital Reserve, and as part of Shareholders' Funds which cannot be distributed as dividend or considered as Deferred Income.
3. Only Grants which are not revenue in nature can be capitalized. The correct treatment is to credit the Subsidy to Capital Reserve.

QUESTION NO 18

A Ltd. has set up its business in a designated backward area with an investment of ₹200 Lakhs. The Company is eligible for 25% subsidy and has received ₹50 Lakhs from the Government. Explain the treatment of the Capital Subsidy received from the Government in the books of the Company.

SOLUTION

1. The Government Grants may be in the nature of Promoters' Contribution i.e.-
   (a) they are given with reference to the Total Investment in an undertaking, or
   (b) by way of contribution towards its Total Capital Outlay,(e.g. Central Investment Subsidy Scheme).

2. Such Grants are not ordinarily expected to be repaid. Hence, they are treated as Capital Reserve, and as part of Shareholders' Funds which cannot be distributed as dividend or considered as Deferred Income.

3. Subsidy received in this case, is not in relation to specific Fixed Assets or in relation to revenue, Hence, it should not be treated as Deferred Income or as an Item of Revenue. The correct treatment is to credit the Subsidy to capital Reserve.

QUESTION 19 (CA INTER NOV 2020)(5MARKS)

On 1st April, 2016, Mac Ltd. received a Government Grant of ₹ 60 lakhs for acquisition of machinery costing ₹ 300 lakhs. The grant was credited to the cost of the asset. The estimated useful life of the machinery is 10 years. The machinery is depreciated @ 10% on WDV basis. The company had to refund the grant in June 2019 due to non - compliance of certain conditions.

How the refund of the grant is dealt with in the books of Mac Ltd. assuming that the company did not charge any depreciation for the year 2019-20.

Pass necessary Journal Entries for the year 2019-20.

SOLUTION

		(₹ in lakhs)
1st April, 2016	Acquisition cost of machinery	300.00
	Less: Government Grant	60.00
		240.00
31st March, 2017	Less: Depreciation @ 10%	(24.00)
1st April, 2017	Book value	216.00
31st March, 2018	Less: Depreciation @ 10%	(21.60)
1st April, 2018	Book value	194.40
31st March, 2019	Less: Depreciation @ 10%	(19.44)
1st April, 2019	Book value	174.96
	Less: Depreciation @10% for 2 months	(2.916)
1st June, 2019	Book value	172.044
June 2019	Add: Refund of grant*	60.00
	Revised book value	232.044

Depreciation @10% on the revised book value amounting to ₹ 232.044 lakhs is to be provided prospectively over the residual useful life of the machinery.

*considered refund of grant at beginning of June month and depreciation for two months already charged. Alternative answer considering otherwise also possible.

Journal Entries

Machinery Account	Dr.	60	
To Bank Account			60
(Being government grant on asset partly refunded which increased the cost of fixed asset)			
Depreciation Account	Dr.	19.337	
To Machinery Account			19.337
(Being depreciation charged on revised value of fixed asset prospectively for 10 months)			
Profit & Loss Account	Dr.	22.253	
To Depreciation Account			22.253
(Being depreciation transferred to Profit and Loss Account amounting to ₹ (2.916 + 19.337= 22.253)			

QUESTION 20 (CA INTER JAN 21) (5MARKS)

Darshan Ltd. purchased a Machinery on 1st April, 2016 for ₹ 130 lakhs (Useful life is 4Years). Government grant received is ₹ 40 lakhs for the purchase of above Machinery.

Salvage value at the end of useful life is estimated at ₹ 60 lakhs.

Darshan Ltd. decides to treat the grant as deferred income.

Your are required to calculate the amount of depreciation and grant to be recognized in profit & loss account for the year ending 31st March, 2017,31st March, 2018, 31st March, 2019& 31st March, 2020.

Darshan Ltd. follows straight line method for charging depreciation.

SOLUTION:

As per 12 "Accounting for government grants", grants related to depreciable assets, if treated as deferred income are recognized in the profit and loss statement on a systematic and rational basis over the useful life of the asset.

Amount of depreciation and grant to be recognized in the profit and loss account each year

Depreciation per year:

	₹ in lakhs
Cost of the Asset	130
Less: Salvage value	(60)
	70
Depreciation per year(70lakhs/4)	17.50

₹ 17.50 Lakhs depreciation will be recognized for the year ending 31st March, 2017, 31st March, 2018, 31st March, 2019 and 31st March, 2020.

Amount of grant recognized in Profit and Loss account each year :

40 lakhs /4 years = ₹ 10 Lakhs for the year ending 31st March, 2017, 31st March, 2018, 31st March, 2019 and 31st March, 2020.

QUESTION 21 (CA INTER JULY 21) (5MARKS)

Alps Limited has received the following Grants from the Government during the year ended 31st March, 2021:

(i) ₹ 120 Lacs received as Subsidy from the Central Government for setting up an Industrial undertaking in Medak, a notified backward area.

(ii) ₹ 15 Lacs Grant received from the Central Government on installation of Effluent Treatment Plant.

(iii) ₹ 25 Lacs received from State Government for providing Medical facilities to its workmen during the pandemic.

Advise Alps Limited on the treatment of the above Grants in its books of Account in accordance with AS-12 "Government Grants".

SOLUTION:

(i) 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 an industrial undertaking in Medak is neither in relation to specific fixed asset nor in relation in revenue. Thus, the amount of ₹ 120 Lacs should be credited to capital reserve.

(**Note:** Subsidy for setting up an industrial undertaking is considered to be in the nature of promoter's contribution)

(ii) As per AS 12 'Accounting for Government Grants', two methods of presentation in financial statements of grants related to specific fixed assets are regarded as acceptable alternatives –

(a) 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. Where the grant equals the whole, or virtually the whole, of the cost of the asset, the asset is shown in the balance sheet at a nominal value.

(b) Grants related to depreciable asset 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.

In the given case, ₹ 15 Lacs was received as grant from the Central Government for installation of Effluent Treatment Plant. Since the grant was received for a fixed asset, either of the above methods can be adopted.

(iii) ₹ 25 lacs received from State Government for providing medical facilities to its workmen during the pandemic is a grant received in nature of revenue grant. Such grants are generally presented as credit in the profit and loss statement, either separately or under a general heading such as "Other Income". Alternatively, ₹ 25 lacs may be deducted in reporting the related expense i.e., employee benefit expense.

QUESTION 22 (CA INTER MAY 2022 EXAMS : 5 MARKS)

Suraj Limited provides you the following information:

(i) It received a Government Grant @40% towards the acquisition of Machinery worth ₹ 25 Crores.

(ii) It received a Capital Subsidy of ₹ 150 Lakhs from Government for setting up a Plant costing ₹ 300 Lakhs in a notified backward region.

(iii) It received ₹ 50 Lakhs from Government for setting up a project for supply of arsenic free water in a notified area.

(iv) It received ₹ 5 Lakhs from the Local Authority for providing Corona Vaccine free of charge to its employees and their families.

(v) It also received a performance award of ₹ 500 Lakhs from Government with a condition of major renovation in the Power Plant within 3 years. Suraj Limited incurred 90% of amount towards Capital expenditure and balance for Revenue Expenditure.

State, how you will treat the above in the books of Suraj Limited.

SOLUTION :

(i) As per AS 12 "Accounting for Govt. Grants", two methods of presentation in financial statements of grants related to specific fixed assets are regarded as acceptable alternatives. Under the first alternative, the grant of ₹ 10 crores (40% of 25 crores) is shown as a deduction from the gross value of the asset concerned in arriving at its book value. The grant is thus recognized the profit and loss statement over the useful life of a depreciable asset by way of a reduced depreciation charge. Under second alternative method, grant amounting ₹ 10 crores is treated as deferred income which is recognized in the profit and loss statement on a systematic and rational basis over the useful life of the asset.

(ii) In the given case, the grant amounting ₹ 150 lakhs received from the Central Government for setting up a plant in notified backward area may be considered as in the nature of promoters' contribution. Thus, amount of ₹ 150 lakhs should be credited to capital reserve and the plant will be shown at ₹ 300 lakhs.

(iii) ₹ 50 lakhs received from Govt. for setting up a project for supply of arsenic free water in notified area should be credited to capital reserve.

Alternatively, if it is assumed that the project consists of capital asset only, then the amount of ₹ 50 lakhs received from Govt. for setting up a project for supply of arsenic free water should either be deducted from cost of asset of the project concerned in the balance sheet or treated as deferred income which is recognized in the profit and loss statement on a systematic and rational basis over the useful life of the asset.

(iv) ₹ 5 lakhs received from the local authority for providing corona vaccine to the employees is a grant received in nature of revenue grant. Such grants are generally presented as a credit in the profit and loss account, either separately or under a general heading 'Other Income'. Alternatively, ₹ 5 lakhs may be deducted in reporting the related expense i.e. employee benefit expenses.

(v) ₹ 500 Lakhs will be reduced from the renovation cost of power plant or will be treated as deferred income irrespective of the expenditure done by the entity out of it as it was specifically received for the purpose major renovation of power plant. However, it may be, later on, decided by the Govt. whether the grant will have to be refunded or not due to non-compliance of conditions attached to the grant.

ACCOUNTING STANDARD-16
ACCOUNTING FOR BORROWING COSTS

QUESTION NO 1 (PROGRESS PAYMENT)

Given below are some relevant data as regards a construction contract.

	₹ In lacs
Expenditure incurred till 31.3.2000	450
Interest cost capitalized for the year 1999-2000 @ 12% p.a.	24
Amount specifically borrowed till 31.3.2000	200
Assets transferred to construction during 2000-01	100
Cash payments during 2000-01	78
Progress payment received	300
New borrowings during 2000-01 @ 12%	200

The company intends to capitalize total borrowing cost of ₹48 lacs. Is it possible to do that as per AS16?

QUESTION NO 2 (CESSATION IN PARTS)

Given below are expenses incurred in three phases of a project relating to construction of a captive power plant:

(₹)

	Phase 1	Phase 2	Phase 3	Total
Cash payments	500000	700000	500000	
Transfer of assets	500000	200000	300000	
Total	1000000	900000	800000	2700000

Money borrowed at the rate of 12% per annum is ₹2200000.

The phase 1 is complete. How should the company capitalize borrowing costs?

QUESTION NO 3 (DEFINITION OF Q.ASSETS)

Parveen jindal Limited obtained term loan during the year ended 31st March, 2002 itd uses extent of ₹650lacs for modernization and development of its factory. Building worth ₹120lacs were completed and plant and machinery worth ts.350lacs were installed by 31st March, 2002. A sum of ₹70 lacs has been advanced for Assets the installation of which is expected in the following year. ₹110lacs have been utilized for working capital requirements. Interest paid on the loan of ₹650lacs during the year 2001-2002 amounted to ₹58.50lacs. How should the interest amount be treated in the Accounts of the company.

QUESTION NO 4 (DEFINITION OF Q.ASSETS)

R Ltd. has borrowed ₹25 crores from financial institution during the financial year 2001-02. These borrowings are used to invest in shares of A Ltd , a subsidiary company, which is implementing a new project estimated to cost 50 crores. As on 31st march,2002 since the said project was not yet complete, the directors of R ltd, resolved to capitalize the interest on the borrowings amounting to ₹3 crores and add it to the cost of investments. As a statutory auditor, please comment.

QUESTION NO 5 (MONTHWISE CAPITALISATION)

XYZ Ltd. Has undertaken a profit for expansion of company of capacity as per the following details;

	Plan (RS.)	Actual (RS.)
April 2002	2,00,000	2,00,000
May 2002	2,00,000	3,00,000
June 2002	10,00,000	---
July 2002	1,00,000	---
August 2002	2,00,000	1,00,000
September 2002	5,00,000	7,00,000

The company pays to its bankers at the rate of 12% p.a., interest being debited on a monthly basis. During the half year company had ₹10 lakhs overdraft upto 31st July, surplus cash in August and again overdraft of over ₹10 lakhs from 01-09-2002. The company had a strike during June and hence could not continue the work during June. Work was again commenced on 1st July and all the works were completed on 30th September. Assume that expenditure were incurred on 1st Day of each month. Calculate:

1. Interest to be capitalized
2. Give reasons wherever necessary.

QUESTION NO 6 (CAPITALISATION RATE)

The British Company Limited made the following borrowings:

Amount borrowed	Date on which borrowing is made	Amount (₹ In lacs)	Objective for amount borrowed	Related expenses (in lacs)
15%Debentures	1.1.2001	400	General	1.00
10%Term loan	1.4.2001	200	Specific to acquisition of plant and machinery	2.00
12%Term loan	1.11.2001	300	General	2.50

15% Debentures and 12% Term loans were raised for the entire project and 10% Term loan were raised for financing plant and machinery. Qualifying Assets for General Borrowings are:

	(₹ In Lacs)
Factory shed	100
Plant and Machinery	900
Other fixed assets	100
	1100

Show how the allocation of Borrowing costs for specific loan as well as general loans to the qualifying assets.

QUESTION NO 7

G company has incurred an amount of ₹80 lakhs as borrowing cost during the year ended 31.12.2002 calculated as under:

Amount borrowed	Date on which borrowing is made	Amount (₹ In lacs)	Interest
14%Debentures	1.12.2001	200	28
12%Term loan	1.12.2001	300	36
16%Term loan	1.10.2002	400	16

The 16% secured loan has been specifically raised for construction of factory building. The estimated cost being ₹6 crores. The plant is likely to be completed in two years. The other qualifying assets in which these funds have been utilized are:

Plant 1	200Lacs	18months
Internal roads	100Lacs	14 months
Plant 11	100Lacs	20 months

Compute the amount of borrowing costs to be capitalized for the year ended 31.3.2002.

QUESTION NO 8

ICS & company is a sugar company. Due to the regulations by Central Government, the company cannot decide the quantity to be sold in the market. It is regulated on the basis of release orders issued by the Central government on a monthly basis. Because of the seasonal nature of production, the company has to carry large inventories throughout the year. The average holding period of the sugar stock is generally 12-15 months. In the years when there is surplus stock of sugar, the government creates a buffer stock and reimburses the carrying charges to the sugar factories, for the inventory to be carried by the sugar mill, which includes interest. Sweet & company incurs high interest costs since borrowings are required to meet the large demand for the working capital and payment to sugarcane producers. Interest costs are the second largest item in the Profit and Loss account of the company next to raw material consumed. Can interest be capitalized under AS 16 as a part of inventory.

QUESTION NO 9

The main object of a company is to undertake plantation activities, raising of teak and other forestry operations. It takes about 10 to 15 years for the teak trees to grow. The company has issued Debentures for the fund to meet all the expenses. The company included all cost of planetary and interest paid in the valuation of stock of teak. Give comment.

QUESTION NO 10

In may, 2004 speed Ltd. took a bank loan to be used specifically for the construction of a new factory building. The construction was completed in January 2005 and the building was put to its use immediately thereafter. Interest on the actual amount used for construction of the building till its completion was ₹18 lakhs, whereas the total interest payable to the bank on the loan for the period till 31st March,2005 amounted to ₹25 lakhs. Can ₹25 lakhs be treated as a part of the cost of factory building and thus be capitalized on the plea that the loan was specifically taken for the construction of factory building.

QUESTION NO 11 (EXPECTED COST OF COMPLETION)

A fixed asset is in the construction period. Actual costs incurred till date and expected costs to complete along with borrowings and planned borrowings are given below:

(₹ in lacs)

Year	Actual	Estimated	Money specifically borrowed	Planned borrowings
1	100		60	
2	100		60	
3		80		40
4		60		40
5		50		30

Borrowed funds costs @ of 12% per annum. Determine the estimated cost of the asset at the end of 5th year.

QUESTION NO 12

Advise X Ltd. on the weighted average cost of borrowing and the interest cost to be capitalized based on the following:

Total borrowings and interest of X Ltd. for year ending 31.3.2003 are as follows:

Borrowings	Date of borrowing	Amount ('000)	Interest ('000)
18% Bank loan	1.5.2001	1,000	180
14% debentures	1.10.2002	2,000	140
16% term loan	1.7.2002	3,000	360
Total		6,000	680

Qualifying assets in which these borrowed funds are utilized are:

Assets	₹('000)	Period
Factory shed	2,500	12 months
Plant 1	1,500	9 months
Plant 2	1,000	7 months

QUESTION NO 13

Determine the dates from which capitalization should cease

Building A	Stage of completion
	Completed in full in march
Building B	Completed in full in April but not accessible until Building C is completed.
Building C	Completed in December
Building D	Completed in June but got electricity connection and was ready for intended use in July.

QUESTION NO 14

What do you understand by the term Borrowing costs? Briefly indicate the items

Which are included in the expression "Borrowing cost" as explained in AS-16.

SOLUTION:

Borrowing costs are interest and other costs incurred by an enterprise In connection with the borrowing of funds. Borrowing costs may include:

(a) Interest and commitment charges on bank borrowing and short term and long term borrowings.

(b) Amortization of discounts or premiums relating to borrowings.

(c) Amortization of ancillary costs incurred in connection with the arrangement of borrowings.

(d) Finance charges in respective of assets acquired under finance leases or under other similar arrangements

(e) Exchange differences arising from foreign currency borrowings to the extent that they are regarded as an adjustment to interest costs.

QUESTION NO 15

The notes to accounts of Sharma Ltd. for the year ended 31st March includes the following "interest on bridge loan from bank and financial institutions and on debentures specifically obtained for the company's fertilizer project amounting to ₹1,80,80,000 has been capitalized during the year, which includes approximately ₹1,70,33,465 capitalized in respect of the utilization of loan and debentures money for the said purpose". Is the treatment correct? Briefly comment

SOLUTION:

For specific borrowing, amount to be capitalized = actual borrowing cost on that borrowing during the period less income on the temporary investment of those borrowings, if any. Hence the amount of capitalized borrowing cost can not exceed actual interest cost.

For general borrowing and use of Capitalization rate, AS-16 provides the amount of borrowing costs Capitalized during a period should not exceed the amount of Borrowing cost incurred during that period.

The given case is one of specific Borrowings for fertilizer project and hence the Capitalized Borrowing cost is restricted to the actual amount of interest expenditure that is ₹1,70,33,465. Capitalization of ₹1,80,80,000 has resulted in over statement of profit and assets by ₹10,46,535.

Hence the company's policy is not in accordance with AS-16.

QUESTION NO 16

Jindal Ltd. borrowed ₹12Crores for its capital expansion which lasted for 18 months. The relevant borrowing rate was 12.5%. During this period the company invested the temporary surplus funds at 4.5% on short term basis and earned an interest of 25lakhs Which was offered as miscellaneous income in the profit and loss account. The company has Capitalized the entire interest cost and added to its plant and machinery. Is this correct?

SOLUTION:

For specific borrowing, amount to be capitalized = actual borrowing cost on that borrowing during the period less income on the temporary investment of those borrowings, if any.

In the above case, the correct accounting treatment will be:

Actual borrowing cost (12crores*12.5%*18months)	= 2.25Crores
Less: interest on temporary investment	= 0.25Crores
Borrowing cost to be Capitalized under As-16	= 2.00Crores

The company's treatment in crediting the amount of 0.25crores as miscellaneous income is not proper. This amount should be used to reduce the amount of Borrowing cost eligible for Capitalization.

QUESTION NO 17

Harihara Limited obtained a Loan for ₹ 70Lakhs on 15th April 20X1 from a Nationalised Bank to be utilized as under:

Particulars	₹
Construction of Factory Shed	25,00,000
Purchase of Machinery	20,00,000
Working Capital	15,00,000
Advance for Purchase of Truck	10,00,000

In March 20X2, Construction of the Factory Shed was completed and Machinery which was ready for its intended use installed. Delivery of Truck was received in the next Financial year. Total Interest RS. 9,10,000 charged by the Bank for the Financial year ending 31.03.20X1. Show the treatment of Interest under AS-16.

QUESTION NO 18

Guha Limited borrowed an amount of ₹ 150 Crores on 1st April, for construction of Boiler Plant at 11% p.a. The Plant is expected to be completed in 4 years. The Weighted Average Cost of Capital is 13% p.a. The Accountant of Guha Ltd. capitalized interest of ₹ 19.50 Crores for the accounting period ending on 31st March. Due to Surplus Funds out of ₹ 150 Crores, an income ₹ 3.50Crores was earned and credited to P&L A/c. comment.

SOLUTION

1. Capitalization based on the Weighted Average Cost of Capital 13% is not proper in the above case, since the above is a case of Specific Borrowings.
2. Income received on Temporary Investments should be reduced from the Borrowing Cost and should not be credited to Profit & Loss A/c. The correct treatment is as under:-

Actual Interest Cost = ₹ 150 Crores x 11%	₹ 16.50 Crores
Less: Income from Temporary Investments	₹ 3.50 Crores
Borrowing Costs to be Capitalised under AS-16	₹ 13.00 Crores

QUESTION NO 19

Madhav Limited began construction of a New Plant on 1st April 2013 and obtained a special Loan of ₹ 8 Lakhs at 10% p.a. to finance the construction of the Plant. The expenditure that was made on the project of Plant construction was as -

On 01.04.2014 ₹ 10,00,000 On 01.08.2014 : ₹ 24,00,000 On 01.01.2014 ₹4,00,000

The Company's other outstanding Non-Specific Loan was ₹ 46,00,000 at an interest of 12% p.a. The construction of Plant was completed on 31.03.2014. Compute the amount of interest to be capitalized.

SOLUTION

Computation of Interest Amount to be capitalized

Date	Amount Spent (₹)	Computation	Interest Amount (Rs)
01.04.2013	10,00,000	₹ 8,00,000 from Specific Loan = ₹ 8,00,000 x 10% ₹ 2,00,000 from Non Specific Loan = ₹2,00,000 x 12%	80,000 24,000
01.08.2013	24,00,000	From Non Specific Loan ₹ 2400,000 x 12% x 8/12	1,92,000
01.01.2014	4,00,000	From Non Specific Loan ₹4,00,000 x 12% x 3/12	12,000
Total	38,00,000		3,08,000

Total Amount Capitalized = Cost Incurred ₹ 38,00,000 + Interest capitalized under AS – 16 ₹ 308,000 = ₹ 41,08,000.

QUESTION NO 20

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

January 2004	200000
April 2004	300000
July 2004	400000
December 2004	120000

Compute the cost to be capitalized including borrowing cost

QUESTION NO 21

On 1st April, Aruna Construction Ltd. obtained a loan of rs. 32 Crores to be utilized as under:-

Particulars	₹ in Crores	Particulars	₹ in Crores
Construction of Sea link across 2 cities (work was held up totally for a month during the year due to high water levels)	25.00	Working Capital	2.00
		Purchase of Vehicles	0.50
		Advance for Tools/Cranes,etc.	0.50
		Purchase of Technical know-How	1.00
Purchase of Equipment's and Machineries	3.00		

Total Interest charged by the Bank for the relevant financial year in ₹ 80 Lakhs. Show the treatment of Interest by Aruna Construction Ltd. under AS-16.

SOLUTION

$$\text{Effective Interest Rate} = \frac{80.00 \text{ Lakhs}}{3{,}200.00 \text{ Lakhs}} = 2.5\%.$$

The treatment for the Total Interest of ₹ 80 Lakhs is as under:-

Note: Interest Amount = Loan Amount = 2.5% Both Amounts in ₹ Lakhs

Purpose/Utilisation	Loan Amt.	Interest Amount	Accounting Treatment
1. Construction of Sea-Link across two cities	2,500	62.50	Added to Cost of Asset (It is assumed that during temporary suspension, some Administrative Activities were carried on)
2. Purchase of Equipments & M/c.	300	7.50	Added to Cost of Equipments and Machineries
3. Working Capital	200	5.00	Written off to P&L A/c. as Expense. as per AS-16

4. Purchase of Vehicles	50	1.25	Debited to P&L A/c. (Assumed immediate delivery taken and it is ready for use and hence not a Qualifying Asset)
5. Advance for Tools / Cranes etc.	50	1.25	Write off in Profit & Loss Account assuming advances Are not made for Q.A.
6. Purchase of Technical Know-how	100	2.50	Added to the cost of Intangibles. (know how takes time)
Total Borrowing Cost	3,200.00	80.00	

QUESTION 22 (CA INTER MAY 2022 EXAMS : 5 MARKS)

Zebra Limited began construction of a new plant on 1st April,2021 and obtained a special loan of ₹ 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:

	₹
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 ₹ 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 provisions 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":

	₹
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

		₹	₹
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			₹
1st April, 2021	10,00,000	On specific borrowing	₹ 10,00,000 x 10%	1,00,000
1st August, 2021	24,00,000	On specific borrowing	₹ 10,00,000 x 10%	1,00,000
1st August, 2021		On non-specific borrowings	₹ 14,00,000 x $\frac{8}{12}$ x 12%	1,12,000
1st January, 2022	4,00,000	On non-specific borrowings	₹ 4,00,000 x $\frac{3}{12}$ x 12%	12,000
				3,24,000

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 14,00,000 x 8/12	10,00,000 9,33,333
1st January, 2022	4,00,000 x 3/12	1,00,000
		30,33,333

Computation of interest to be capitalized:

		₹
On specific borrowing	₹ 20,00,000 x 10%	2,00,000
On non-specific borrowing	₹ (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.

CASH FLOW STATEMENTS

QUESTION NO 1

The financial position of ABC Ltd. on 1st April 2001 and 31.3.2002 was as follows:

Liabilities	1.4.2001	31.03.2002	Assets	1.4.2001	31.03.2002
Current liabilities	72,000	82,000	Cash	8,000	7,200
Loan from			Debtors	70,000	76,800
associated			Stock	50,000	44,000
company	—	40,000	Land	40,000	60,000
Loan from bank	60,000	50,000	Building	1,00,000	1,10,000
Capital and			Machinery	2,14,000	2,44,000
reserves	2,96,000	2,98,000	Provision for dep.	(54,000)	(72,000)
	4,28,000	4,70,000		4,28,000	4,70,000

During the year ₹ 52,000 were paid as dividends, prepare cash flow statement as per AS-3.

QUESTION NO 2

Particulars	2000	2001
Liabilities:		
Share capital	3,00,000	3,50,000
Share premium	—	30,000
General reserve	45,000	65,000
Profit and loss account	30,000	80,800
6% Debentures	—	70,000
Sundry creditors	85,000	90,700
Provision for taxation	22,500	40,500
Proposed dividend	30,000	35,000
	5,12,500	7,62,000

Particulars	2000	2001
Assets:		
Land and Building	2,30,000	3,90,000
Machinery	85,400	1,40,000
Furniture	5,500	6,500
Stock	82,400	95,700
Sundry debtors	75,000	85,500
Bank	34,200	44,300
	5,12,500	7,62,000

Additional information:

Depreciation written off during the year:

Land and Building	60,000
Plant and Machinery	50,000
Furniture	1,200

You are required to prepare a Cash Flow Statement.

QUESTION NO 3

From the following balances you are required to calculate cash from operation:

	31.12.2003	31.12.2004
Debtors	50,000	47,000
Bills receivable	10,000	12,500
Creditors	20,000	25,000
Bills payable	800	6,000
Outstanding expenses	1,000	1,200
Prepaid expenses	800	700
Accrued income	600	750
Income received in advance	300	250
Profit made during the year		1,30,000

QUESTION NO 4 (C.S.FINAL JUNE 1999)

The summarized Balance Sheet of XYZ Limited as at 31st December 2000 and 2001 are given below:

Particulars	2000	2001
Assets:		
Fixed Assets	4,00,000	3,20,000
Investments	50,000	60,000
Stock	2,40,000	2,10,000
Sundry debtors	2,10,000	4,55,000
Bank	1,49,000	1,97,000
	10,49,000	12,42,000
Liabilities:		
Share capital	4,50,000	4,50,000
General reserve	3,00,000	3,10,000
Profit and loss account	56,000	68,000
Creditors	1,68,000	1,34,000
Provision for taxation	75,000	10,000
Bank loan (long term)	—	2,70,000
	10,49,000	12,42,000

Additional information:

(i) Investment costing ₹ 8000 were sold during the year 2001 for ₹ 8500.

(ii) Provision for tax made during the year was ₹ 9000.

(iii) During the year, part of the fixed assets costing ₹ 10,000 was sold for ₹ 12,000 and the profit was included in Profit and Loss account.

(iv) Dividend paid during the year amounted to ₹ 40,000.

You are required to prepare a statement of cash flow.

SOLUTION:

CASH FLOW STATEMENT Of XYZ Ltd. FOR THE YEAR ENDING 31.12.2001

Particulars	Amounts	Amounts
Cash from Operating Activities:		
Net profit	12,000	
Proposed dividend	40,000	
Transfer to general reserve	10,000	
Depreciation	70,000	
Provision for tax	9,000	
Profit on sale of investments	(500)	
Profit on sale of fixed assets	(2,000)	
Working capital adjustments:		
Decrease in stocks	30,000	
Increase in Debtors	(2,45,000)	
Decrease in creditors	(34,000)	
Income tax paid	(74,000)	(1,84,500)
Cash from investing Activities:		
Sale of investments	8,500	
Sale of fixed assets	12,000	
Purchase of investments	(18,000)	2,500
Cash from financing Activities:		
Mortgage loan raised	2,70,000	
Dividend paid	(40,000)	2,30,000
Total of all activities (O+I+F)		48,000
Add: opening balance of cash and bank		1,49,000
Closing balance of cash and bank		1,97,000

QUESTION NO 5 (I.C.W.A. FINAL JUNE 1998)

From the following prepare a cash flow statement for XYZ Limited for the year 2001:

XYZ Limited

Balance Sheet as at March 31, 2000

Liabilities	Amount ('000)	Assets	Amount ('000)
Paid up capital	50	Gross fixed assets	1,000
Retained earnings	350	Less: Depreciation	100
Long term debt	500		900
Notes payable	80	Inventory	100
Accounts payable	80	Accounts Receivable	50
		Cash	10
	1,060		1,060

Balance Sheet as at March 31, 2001

Liabilities	Amount ('000)	Assets	Amount ('000)
Paid up capital	50	Gross fixed assets	1,125
Retained earnings	415	Less: Depreciation	175
Long term debt	550		950
Notes payable	100	Inventory	110
Accounts payable	90	Accounts Receivable	60
		Cash	85
	1,205		1,205

Income statement of March 31, 2001

Sales	1,200
(-) Cost of goods sold	800
Gross profit	400
(-) Selling, general, administration expenses	150
EBIT	250
(-) Interest	50

EBT	200
(-) Taxes (50%)	100
Net Income	100

Additional information:

(i) Dividend paid ₹ 35,000

(ii) Depreciation ₹ 75,000.

QUESTION NO 6 (MAY 2002)

From the following details relating to the accounts of Grow More Limited. Prepare the cash flow statement.

	31.3.2002	31.3.2001
Liabilities:		
Share capital	10,00,000	8,00,000
Reserves	2,00,000	1,50,000
Profit and loss account	1,00,000	60,000
Debentures	2,00,000	—
Provisions for taxation	1,00,000	70,000
Proposed dividend	2,00,000	1,00,000
Sundry creditors	7,00,000	8,20,000
	25,00,000	25,00,000
Assets:		
Plant and machinery	7,00,000	5,00,000
Land and building	6,00,000	4,00,000
Investments	1,00,000	—
Sundry debtors	5,00,000	7,00,000
Stock	4,00,000	2,00,000
Cash on hand/ bank	2,00,000	2,00,000
	20,00,000	20,00,000

Other information:

1. Depreciation @ 25% was charged on the opening value of plant and machinery.
2. During the year one old machine costing 50,000 (WDV 20,000) was sold for ₹ 35,000.
3. ₹ 50,000 was paid towards income tax during the year.
4. Building under construction was not subject to any depreciation.

QUESTION NO 7

The following summary of cash account has been extracted from the company's accounting records:-

Summary of cash account

		(₹ '000)
Balance at 1.1.98		35
Receipts from customers		2,783
Issue of shares		300
Sale of fixed assets		128
		3,246
Payments to suppliers	2,047	
Payments for fixed assets	230	
Payments for overheads	115	
Wages and salaries	69	
Taxation	243	
Dividends	80	
Repayments of bank loan	250	(3,034)
Balance at 31.12.98		212

Prepare the cash flow statement of this company Hills Limited for the year ended 31st December 1998 in accordance with AS-3 (revised).

SOLUTION:

CASH FLOW STATEMENT FOR THE YEAR ENDING 31.03.2006

Particulars	Amounts	Amounts
Cash from Operating Activities:		
Receipts from customers	2,783	
Payment to suppliers	(2,047)	
Payments for overheads	(115)	
Wages and salaries	(69)	
taxation	(243)	309
Cash from investing Activities:		
Sale of fixed assets	128	
Payments for fixed assets	(230)	(102)
Cash from financing Activities:		
Issue of shares	300	
Dividends	(80)	
Repayment of bank loan	(250)	(30)
Total of all activities (O+I+F)		177
Add: opening balance of cash and bank		35
Closing balance of cash and bank		212

QUESTION NO 8 (CA FINAL NOV 2001)

From the following summary Cash account of X Limited prepare cash flow statement for the year ended 31st March 2001, in accordance with AS-3 (revised) using the direct method. The company does not have any cash equivalents:-

Summary cash account for the year ended 31.3.2001

Particulars	Amount	Particulars	Amount
Balance on 1.4.2000	50	Payment to suppliers	2,000
Issue of equity shares	300	Purchase of fixed assets	200
Receipts from customers	2800	Overhead expense	200
Sale of fixed assets	100	Wages and salaries	100
		Taxation	250
		Dividend	50
		Repayment of Bank loan	300
		Balance of 31.3.2001	150
	3250		3250

QUESTION NO 9 (CA FINAL MAY 2001)

Ms Jyothi of star oils Limited has collected the following information for the preparation of cash flow statement for the year 2000:

Particulars	₹ in Lakhs
Net profits	25000
Dividend paid	8535
Provision for income tax	5000
Income tax paid during the year	4248
Loss on sale of asset	40
Book value of sold asset	185
Depreciation charged to Profit and Loss account	20000
Profit on sale of investment	100
Carrying amount of investment sold	27765
Interest income on investment	2506
Interest expenses	10000
Interest paid during the year	10520
Increase in working capital (excluding cash and bank bal)	56075
Purchase of fixed asset	14560

Investment in joint venture	3850
Expenditure in construction work in progress	34740
Proceeds from call in arrear	2
Proceeds from long term borrowings	25980
Proceeds from short term borrowings	20575
Opening cash and bank balances	5003
Closing cash and bank balances	6982

Prepare the cash flow statement for the year 2000 in accordance with AS-3, cash Flow statements issued by the institute of chartered accountants of India.

QUESTION NO 10

The following date were provided by the accounting records of Ryan Limited at year end March 31,1997:

Income statement

		(₹)
Sales		6,98,000
Cost of goods sold		(5,20,000)
Gross margin		1,78,000
Opening expenses (including depreciation expenses of ₹ 37,000)		(1,47,000)
		31,000
Other income (expenses)		
Interest expenses paid	(23,000)	
Interest income received	6,000	
Gain on sale of investment	12,000	
Loss on sale of plant	(3,000)	(8,000)
		23,000
		7,000
Income tax		16,000

Comparative Balance Sheet

	31.3.97	31.3.96
Assets:	7,15,000	5,05,000
Plant assets	(1,03,000)	(68,000)
Less: accumulated depreciation	6,12,000	4,37,000
Investments (long term)	1,15,000	1,27,000
Inventory	1,44,000	1,10,000
Accounts receivable	47,000	55,000
Cash	46,000	15,000
Prepaid expenses	1,000	5,000
	9,65,000	7,49,000
Liabilities:		
Share capital	4,65,000	3,15,000
Reserve and surplus	1,40,000	1,32,000
Bonds	2,95,000	2,45,000
Accounts payable	50,000	43,000
Accrued liabilities	12,000	9,000
Income taxes payable	3,000	5,000
	9,65,000	7,49,000

Analysis of selected accounts and transactions during 1996-97:

1. Purchased investments for ₹ 78,000
2. Sold investments for ₹ 1,02,000, these investments cost ₹ 90,000.
3. Purchased plant assets for ₹ 1,20,000
4. Sold plant assets that cost ₹ 10,000 with as simulated depreciation of ₹ 2,000 for ₹ 5,000.
5. Issued ₹ 1,00,000 of bonds at face value in an exchange for plant assets on 31st March 1997.
6. Repaid ₹ 50,000 of bonds at face value at maturity.
7. Issued 15,000 shares of ₹ 10 each.
8. Paid cash dividends of ₹ 8000.

Prepare Cash flow statement as per AS-3 using the indirect method.

QUESTION NO 11

The Balance Sheet of Sun Limited for the years ended 31st March 1996 and 1997 were summarized thus:

	1997 (₹)	1996 (₹)
Equity share capital	60,000	50,000
Reserves:		
Profit and Loss account	5,000	4,000
Current liabilities:		
Creditors	4,000	2,500
Taxation	1,500	1,000
Proposed dividend	2,000	1,000
	72,500	58,500
Fixed assets (at w.d.v.)		
Premises	10,000	10,000
Fixtures	17,000	11,000
Vehicles	12,500	8,000
Short-term investments	2,000	1,000
Current assets:		
Stock	17,000	14,000
Debtors	8,000	6,000
Bank and cash	60,000	8,500
	72,500	58,500

And the Profit and Loss account for the year ended 31st March 1997 disclosed

Profit before tax	4,500
Taxation	(1,500)
Profit after tax	3,000
Proposed dividend	(2,000)
Retained profit	1,000

Further information is available:

	Vehicles (₹)	Fixtures (₹)
Depreciation for year	1,000	2,500
Disposals:		
Proceeds on disposal		1,700
Written down value		(1,000)
Profit on disposal		700

Prepare a Cash Flow Statement for the year ended 31st March 1997.

QUESTION NO 12

Given below are Profit and Loss account of ABC Limited and relevant Balance Sheet information. Prepare cash flow from operating activities:-

Profit and Loss Account for the year ended 31.12.2000 of ABC Limited	₹ in lacs.
Revenues:	
Sales	4150
Interest and dividends	100
Stock adjustment	20
Total	**4270**
Expenditure:	
Purchases	2400
Wages and salaries	800
Other expenses	200
Interest	60
Depreciation	100
Total	**3560**
Profit before tax	710
Tax provision	200
Profit after tax	**510**
Balance of Profit and Loss Account	50
Profit available for distribution	560

Appropriation	
Transfer to general reserve	200
Proposed dividend	300
Distribution tax	30
Total	**530**
Balance	30

Relevant information of Balance Sheet	31.12.2000	31.12.1999
Debtors	400	250
Inventories	200	180
Creditors	250	230
Outstanding wages	50	40
Outstanding expenses	20	10
Advance tax	195	180
Tax provision	200	180

QUESTION NO 13

The Balance Sheets of Western Manufacturers Limited as on 1st January 2002 and 31st December,2002 are as follows:

Liabilities	1.1.2002	31.12.2002	Assets	1.1.2002	31.12.2002
Share capital	2,50,000	2,50,000	Land and building	1,50,000	1,50,000
5% debentures	1,00,000	80,000			
Sundry creditors	1,15,000	1,08,000	Machinery	82,000	90,000
			Stock	1,00,000	1,14,000
Profit and Loss account	20,000	27,000	Debtors	85,000	81,000
Depreciation fund	40,000	44,000	Cash and bank	60,000	55,000
Reserve for contingencies	70,000	55,000	Temporary investments	1,31,000	95,000
Outstanding expenses	15,000	24,000	Prepaid expenses	2,000	3,000
	6,10,000	5,88,000		6,10,000	5,88,000

The following additional information is also available:

1. New machinery was purchased for ₹ 30,000 but old machinery costing ₹ 15,000 was sold for ₹ 5,000 accumulated depreciation was ₹ 8,000.
2. ₹ 20,000, 5% debentures were redeemed by purchase from open market @ ₹ 96.
3. ₹ 36,000 investment were sold at book value.
4. 12% dividend was paid in cash.
5. ₹ 15,000 was debited to contingency reserve for settlement of previous tax liability.

You are required to prepare the cash flow statement by indirect method.

NOTE:

QUESTION NO 14 (MAY 2003)

From the following Balance Sheet and information, prepare Cash Flow statement of Ryan Limited for the year ended 31.3.2003:-

Balance Sheet

	31.03.2003	31.03.2002
Liabilities:		
Equity Share Capital	6,00,000	5,00,000
10% Redeemable Preference 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	—
Sundry Creditors	95,000	80,000
Bills Payable	20,000	30,000
Liabilities for expenses	30,000	20,000
Provision for Taxation	95,000	60,000
Proposed Dividend	90,000	60,000
	15,00,000	12,50,000
Assets:		
Land and building	1,50,000	2,00,000
Plant and machinery	7,65,000	5,00,000
Investment	50,000	80,000
Inventory	95,000	90,000
Bills receivable	65,000	70,000
Sundry debtors	1,75,000	1,30,000
Cash and bank	65,000	90,000
Preliminary Expenses	10,000	25,000
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 ₹ 1,50,000 (cost- ₹ 1,20,000) and the balance land was revalued. Capital reserve consisted of profit on sale and profit on revaluation.

(ii) On 1st April, 2002 a plant was sold for ₹ 90,000 (original cost – ₹ 70,000 and W.D.V – ₹ 50,000) and debentures worth ₹ 1 lakh was issued at par as part consideration for plant of ₹ 4.50 lakhs acquired.

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

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

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

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

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

(viii) Depreciation @ 15% has been written off from plant account but no depreciation has been charged on land and building.

NOTE:

QUESTION NO 15

From the following information prepare Cash flow statement by indirect method.

COMPARATIVE BALANCE SHEET

Excellent Limited.

Liabilities	31.3.2002	31.3.2001		31.3.2002	31.3.2001
Share capital	50,00,000	40,00,000	Fixed assets	31,00,000	30,00,000
Reserves and surplus	15,00,000	5,00,000	Investments	1,50,000	—
			Cash and bank	2,50,000	1,25,000
Secured loans	35,00,000	40,00,000	Stocks and stores, work in progress	75,00,000	78,75,000
Current liabilities	50,00,000	60,00,000	Sundry debtors	40,00,000	35,00,000
	1,50,00,000	1,45,00,000		1,50,00,000	1,45,00,000

(a) The net profit for the year after adjustment in respect of provisions for dividends and taxation was ₹ 10,00,000.

(b) There was addition to fixed assets during the year amounting to ₹ 4,00,000 and depreciation for the year was ₹ 3,00,000.

QUESTION NO 16

From the following Balance Sheets prepare a cash flow statement of AA Limited for the year-ended 31.3.1999:

Liabilities	97-98	98-99	Assets	97-99	98-99
Share capital:			Sundry fixed assets:		
Equity shares of ₹ 10 each	1000	1200	Gross block	1600	2000
General reserve	700	750	Less: depreciation	320	720
Profit and Loss a/c	200	220	Net block	1280	1280
Share premium	20	40			
14% debentures	400	450	Investment	600	700
Cash credits	90	120	Inventories	500	700
Sundry creditors	180	220	Sundry debtors	320	450
Provisions for taxation	10	20	Cash and bank	50	130
Proposed dividend	150	240			
	2750	3260		2750	3260

Other information:

1. It discarded fixed assets costing ₹ 2 lacs, accumulated depreciation ₹ 40,000 at ₹ 20,000 only.
2. It paid advance tax ₹ 70 lacs for 1998-99, apart from payment of balance tax liability of ₹ 8Lakhs for 1997-98.
3. It transferred excess tax provisions for 1997-98 to General reserve.

NOTE:

QUESTION NO 17 (MAY 2005)

THE following figures have been extracted from the books of X Ltd. for the year ended on 31.3.2004. You are required to prepare a cash flow statement:

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

a. Depreciation on fixed assets ₹ 5lakhs

b. Discount on issue of Debentures written off ₹ 30,000.

c. Interest on debentures paid ₹ 3,50,000.

d. Books value of investments ₹ 3lakhs (sale of investment for ₹ 3,20,000)

e. Interest received on investments ₹ 60,000.

f. Compensation received ₹ 90,000 by the company in a suit filed.

(b) Income tax paid during the year ₹ 10,50,000

(c) 15,000, 10% Preference shares of ₹ 100 each were redeemed on 31.3.2004 at a premium of 5%. Further the company issued 50,000 equity shares of ₹ 10 each at a premium of 20% on 2.4.2003. dividend on Preference shares were paid at the time of redemption.

(d) Dividends paid for the year 2002-2003 ₹ 5lakhs and interim dividend paid ₹ 3 lakhs for the year 2003-04.

(e) Land was purchased on 2.4.2003 for ₹ 2,40,000 for which the company issued 20,000 equity shares of ₹ 10 each at a premium of 20% to the land owner as consideration.

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

	31.3.2003	31.3.2004
Stock	12,00,000	13,18,000
Debtors	2,08,000	2,13,100
Cash in hand	1,96,300	35,300
Bills receivable	50,000	40,000
Bills payable	45,000	40,000
Creditors	1,66,000	1,71,300
Outstanding expenses	75,000	81,800

NOTE:

QUESTION NO 18 (MAY 2004)

ABC Ltd. gives you the following information. You are required to prepare cash flow statement by using indirect method as per AS 3 for the year 31.03.2004:

BALANCE SHEETS

Liabilities	31.3.2003	31.3.2004	Assets	31.3.2003	31.3.2004
Capital	50,00,000	50,00,000	Plant and mach.	27,30,000	40,70,000
Retained earnings	26,50,000	36,90,000	Less: depreciation		
9% Debentures	—	9,00,000		6,10,000	7,90,000
Creditors	8,80,000	8,20,000		21,20,000	32,80,000
Bank loan	1,50,000	3,00,000	Debtors	23,90,000	28,30,000
Liability for exp.	3,30,000	2,70,000	Less: Provisions	1,50,000	1,90,000
Dividend payable	1,50,000	3,00,000		22,40,000	26,40,000
			Cash	15,20,000	18,20,000
			Marketable sec.	11,80,000	15,00,000
			Inventories	20,10,000	19,20,000
			prepaid expenses	90,000	1,20,000
	91,60,000	1,12,80,000		91,60,000	1,12,80,000

Additional information:

(a) Net profit for the year ended 31st March, 2004, after charging depreciation ₹ 1,80,000 is ₹ 22,40,000.

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

(c) ABC Ltd. declared dividend of ₹ 12,00,000 for the year 2003-2004.

NOTE:

QUESTION NO 19 (NOV 2003)

The Balance Sheet of New Light Ltd. for the years ended 31st March, 2001 and 2002 are as follows:

BALANCE SHEETS

Liabilities	31.3.2003	31.3.2004	Assets	31.3.2003	31.3.2004
Equity share			Fixed Assets	32,00,000	38,00,000
capital	12,00,000	16,00,000	Less:		
10% Preference			depreciation	9,20,000	11,60,000
share capital	4,00,000	2,80,000		22,80,000	26,40,000
Capital Reserve	—	40,000			
General Reserve	6,80,000	8,00,000	Investment	4,00,000	3,20,000
Profit and loss			Cash	10,000	10,000
account	2,40,000	3,00,000	Other		
9% Debentures	4,00,000	2,80,000	current		
Current			assets	11,10,000	13,10,000
Liabilities	4,80,000	5,20,000	Preliminary		
Provision for			expenses	80,000	40,000
tax	1,20,000	1,44,000			
Prop. Dividend	3,60,000	3,40,000			
Unpaid dividend	—	16,000			
	38,80,000	43,20,000		38,80,000	43,20,000

Additional information:

(a) The company sold one fixed asset for ₹ 1,00,000, the cost of which was ₹ 2,00,000 and the depreciation provided on it was ₹ 80,000.

(b) The company also decided to write off another fixed asset costing ₹ 56,000 on which depreciation amounting to ₹ 40,000 has been provided.

(c) Depreciation on fixed assets provided ₹ 3,60,000.

(d) Company sold some investment at a profit of ₹ 40,000 which was credited to capital reserve.

(e) Debentures and Preference share capital redeemed at 5% premium.

(f) Company decided to value stock at cost, whereas previously the practice was to value stock at cost less 10%. The stock according to books on 31.3.2003 was ₹ 2,16,000. The stock on 31.3.2004 was correctly valued at ₹ 3,00,000.

Prepare cash flow statement as per revised accounting standard 3 by indirect method.

NOTE:

QUESTION NO 20 (CA FINAL NOV 1998)

The following are the changes in the account balances taken from the Balance Sheets of PQ Ltd. as at the beginning and end of the year:

	Changes in Rupees in debit or (credit)
Equity share capital 30,000 shares of ₹ 10 each issued and fully paid	0
Capital reserve	(49,200)
8% debentures	(50,000)
Debentures discount	1,000
Freehold property at cost/revaluation	43,000
Plant and machinery at cost	60,000
Depreciation on plant and machinery	(14,400)
Debtors	50,000
Stock and work in progress	38,500
Creditors	(11,800)
Net profit for the year	(76,500)
Dividend paid in respect of earlier year	30,000
Provision for doubtful debts	(3,300)
Trade investments at cost	47,000
Bank	(64,300)
	0

You are informed that:

(a) Capital reserve as at the end of the year represented realized profits on sale of one freehold property together with surplus arising on the revaluation of balance of freehold properties.

(b) During the year plant costing ₹ 18,000 against which depreciation provision of ₹ 13,500 was lying, was sold for ₹ 7,000.

(c) During the middle of the year ₹ 50,000 debentures were issued for cash at a discount of ₹ 1,000.

(d) The net profit for the year was after crediting the profit on sale of plant and charging debentures interest.

You are required to prepare a statement which will explain, why bank borrowing has increased by Rs64,300 during the year end. Ignore taxation.

QUESTION NO 21 (MAY 2006)

Raj Ltd. gives you the following information for the year ended 31.3.2006:

(i) Sales for the year ₹ 48,00,000. The company sold goods for cash only.

(ii) Cost of goods sold was 75% of sales.

(iii) Closing inventory was higher than opening inventory by ₹ 50,000.

(iv) Trade creditors on 31.3.2006 exceed the outstanding on 31.03.2005 by 1,00,000.

(v) Tax paid during the year amounts to ₹ 1,50,000.

(vi) Amounts paid to trade creditors during the year ₹ 35,50,000.

(vii) Administrative and selling expenses paid ₹ 3,60,000.

(viii) One new machinery was acquired in December 2005, for ₹ 6,00,000.

(ix) Dividend paid during the year ₹ 1,20,000.

(x) Cash in hand and at bank on 31.3.2006 ₹ 70,000

(xi) Cash in hand and bank on 31.3.2005 ₹ 50,000

Prepare cash flow statement for the year ended 31.3.2006 as per the prescribed accounting standard.

QUESTION NO 22 (MAY 2006)

What all are the differences between cash flow statement and fund flow statement?

SOLUTION:

Fund Flow Statements	Cash flow statement
It ascertains the changes in the financial position between two accounting periods.	It ascertains the changes in balance of cash in hand and cash at bank between two dates.
It analyses the reasons for changes in financial position between two Balance Sheets.	It analyses the reasons for changes in cash and bank balances on a particular date.
It reveals the sources and application of funds.	It shows the Inflows and Outflows of cash.
It helps to test whether working capital has been effectively used or not.	It is an important tool for short term analysis. The two significant areas of analysis are cash generating efficiency and free cash flow.

QUESTION NO 23

Following are the summarized balance sheets of Growell Limited as on 31st March 2000 and 2001.

Particulars	2000	2001
Liabilities:		
Share capital	2,00,000	2,50,000
General reserve	50,000	60,000
Profit and loss account	30,500	30,600
Bank loan (Long term)	70,000	-
Sundry creditors	1,50,000	1,35,200
Provision for taxation	30,000	35,000
	5,30,500	5,10,800

Particulars	2000	2001
Assets:		
Land and Building	2,00,000	1,90,000
Machinery	1,50,000	1,69,000
Stock	1,00,000	74,000
Sundry debtors	80,000	64,200

Cash	500	800
Bank	—	7,800
Goodwill	—	5000
	5,30,500	5,10,800

Additional information:

(i) Dividend of ₹ 23,000 was paid.

(ii) Assets of another company were purchased for a consideration of ₹ 50,000 payable in shares. The following assets were purchased:

(a) Stock ₹ 20,000

(b) Machinery ₹ 25,000

(iii) Machinery was further purchased for ₹ 8,000.

(iv) Depreciation written off on machinery ₹ 12,000 and

(v) Income tax provided during the year ₹ 33,000; Loss on sale of machinery ₹ 200 was written off to general reserve .

You are required to make the statement of cash flow.

QUESTION NO 24 (NOV 2006)

The following are the summarized Balance Sheets of 'X' Ltd. as on March 31,2005 and 2006.

Liabilities	As on 31.03.2005 (₹)	As on 31.03.2006 (₹)
Equity share capital	10,00,000	12,50,000
Capital Reserves	—	10,000
General Reserve	2,50,000	3,00,000
Profit and Loss A/c	1,50,000	1,80,000
Long-term loan	5,00,000	4,00,000
Sundry Creditors	5,00,000	4,00,000
Provision for Taxation	50,000	60,000
Proposed Dividends	1,00,000	1,25,000
	25,50,000	27,25,000

Assets	Year 2005 (₹)	Year 2006 (₹)
Land and Building	5,00,000	4,80,000
Machinery	7,50,000	9,20,000
Investment	1,00,000	50,000
Stock	3,00,000	2,80,000
Sundry Debtors	4,00,000	4,20,000
Cash in Hand	2,00,000	1,65,000
Cash at Bank	3,00,000	4,10,000
	25,50,000	27,50,000

Additional Information:

- Dividend of ₹ 1,00,00 was paid during the year ended March 31,2006.
- Machinery during the year purchased for ₹ 1,25,000.
- Machinery of another company was purchased for a consideration of ₹ 1,00,00 payable in equity shares.
- Income-tax provided during the year ₹ 55,000.
- Company sold some investment at a profit of ₹ 10,000, which was credited to Capital reserve.
- There was no sale of machinery during the year.
- Depreciation written off on Land and Building ₹ 20,000.

From the above particulars, prepare a cash flow statement for the year ended March, 2006 as per AS-3 (Indirect method).

QUESTION NO 24 (B) (MAY 2007)

Answer the following :

Garden Ltd. acquired fixed assets viz. plant and machinery for ₹ 20 Lakhs. During the same year it sold its furniture and fixtures for ₹ 5 lakhs. Can the company disclose, net cash outflow towards purchase of fixed assets in the cash flow statement as per AS_3?

QUESTION NO 25 (NOV 2007)

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

		(₹ In Lacs)
(i)	Net Profit before tax provision	36,000
(ii)	Dividend paid	10,202
(iii)	Income Tax paid	5,100
(iv)	Book value of Assets sold	222
	Loss on sale of Asset	48
(v)	Depreciation debited in P&L Account	24,000
(vi)	Capital grant received –amortised in P&L A/c	10
(vii)	Book value of investment sold	33,318
	Profit on sale of Investment	120
(viii)	Interest income from investment credited in P&L A/c	3,000
(ix)	Interest expenditure debited in P&L A/c	12,000
(x)	Interest actually paid (Financing activity)	13,042
(xi)	Increase in working Capital Excluding cash and Bank Balance].	67,290
(xii)	Purchase of fixed assets	22,092
(xiii)	Expenditure on construction work	41,6881
(xiv)	Grant received for Capital projects	18
(xv)	Long-term borrowings from Banks	55,866
(xvi)	Provision for Income Tax debited in P&L A/c	6,000
	Cash and Bank Balance on 1.4.2006	6,000
	Cash and Bank Balance on 31.3.2007	8,000

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

QUESTION NO 26 (MAY 2009)

From the following summarized Cash account of S. Ltd. prepare cash flow statement for the year ended 31st March, 2009 in accordance with AS-3 (revised) using direct method. The company does not have any cash requirement.

Summarized Cash Account

			(₹ 000)
Opening Balance	50	Payment to suppliers	2,000
Issue of Share capital	300	Purchase of Fixed assets	200
Received from customers	2,800	Overhead expenses	200
Sale of Fixed asset.	100	Wages and salaries	100
		Tax paid	250
		Dividend paid	50
		Bank Loan	300
		Closing Balance	150
	3,250		3,250

QUESTION NO 27 (MAY 2010)

The following particulars relate to Bee Ltd. for the year ended 31 March, 2010. '.

(i) Furniture of book value of ₹ 15,500 was disposed off for ₹ 12,000.

(ii) Machinery costing ₹ 3,10,000 was purchased and ₹ 20,000 were spent on its erection.

(iii) Fully paid 8% preference shares of the face value of ₹ 10,00,000 were redeemed at a premium of 3%. In this connection 60,000 equity shares of ₹ 10 each were issued at a premium of ₹ 2 per share. The entire money being received with applications.

(iv) Dividend was paid as follows :

On 8% preference shares	₹ 40,000
On equity shares for the year 2009-10	₹ 1,10,000

(v) Total sales were ₹ 32,00,000 out of which cash sales were ₹ 11,50,000.

(vi) Total purchases were ₹ 8,00,000 including cash purchase of ₹ 60,000.

(vii) Total expenses were ₹ 12,40,000

(viii) Taxes paid including dividend tax of ₹ 22,500 were ₹ 3,30,000

(ix) Cash and cash equivalents as on 31st March, 2010 were ₹ 1,25,000.

You are requested to prepare Cash Flow Statement as per AS-3 for the year ended 31st March, 2010 after taking into consideration the following also:

	On 31st March, 2009 (₹)	On 31st March, 2010 (₹)
Sundry debtors	1,50,000	1,47,000
Sundry creditors	78,000	83,000
Unpaid expenses	63,000	55,000

NOTE:

QUESTION NO 28 (8 MARKS) (NOV. 2013)

Surya Ltd has provided you the following particulars. Prepare Cash Flow from Operating Activities by Indirect Method in accordance with AS 3:

Profit & Loss Account of Surya Ltd.

for the year ended 31st March, 2013

Particulars	Rs	Particulars	Rs
To Depreciation	86,700	By Operating profit before depreciation	11,01,600
To Patents written off	35,000	By profit on sale on Investments	10,000
To Provision for Tax	1,25,000	By Refund of Tax	3,000
To Proposed dividend	72,000	By Insurance Claim Major Fire Settlement	1,00,000
To Transfer to Reserve	87,000		
To Net Profit	8,08,900		
Total	12,14,600	Total	12,14,600

Additional information :

in ₹

	31.3.2012	31.3.2013
Stock	1,20,000	1,60,000
Trade Debtors	7,500	75,000
Trade Creditors	23,735	87,525
Provision for tax	1,18,775	1,25,000
Prepaid Expenses	15,325	12,475
Marketable Securities	11,775	29,325
cash balance	25,325	35,340

SOLUTION :

CASH FROM OPERATING ACTIVITIES

Particulars	Amount
Net profits	8,08,900
Transfer to Reserves	87,000
Proposed Dividends	72,000
Provision for Tax	1,25,000
Patents written off	35,000
Depreciation	86,700
Profit on sale on investment	(10,000)
Insurance claim major fire settlement	(1,00,000)
Tax paid for previous year	(1,18,775)
Working Capital Requirement:	
Increase in Stock	(40,000)
Increase in debtors	(67,500)
Decrease in prepaid expenses	2,850
Increase in creditors	63,790
Extra ordinary Activities:	
Insurance claim recovered for major fire settlement	1,00,000
CFOA	10,44,965

QUESTION NO 29 (8 MARKS) (MAY 2013)

On the basis of the following prepare a cash Flow Statement for the year ended 31th March, 2013:-

(i) Total sales for the year were ₹ 199 crore out of which cash sales amounted ₹ 131 crore.

(ii) Cash collection from credit customers during the year totaled ₹ 67 crore.

(iii) Cash paid to suppliers of goods and services and to the employees of the enterprises amounted to ₹ 159 crore.

(iv) Fully paid preference shares of the face value of ₹ 16 crore were redeemed and equity shares of the face value of ₹ 16 crore were allotted as fully paid up at a premium of 25%

(v) ₹ 13 crore were paid by way of income tax.

(vi) Machine of the book value of ₹ 21 crore was sold at a loss ₹ 30 lakhs and a new machine was installed was installed at a total cost of ₹ 40 crore.

(vii) Debenture interest amounting ₹ 1 crore was paid.

(viii) Dividends totaling ₹ 10 crore was paid on equity and preference shares. Corporate dividend tax @ 17% was also paid.

(ix) On 31st March, 2012 balance with bank and cash on cash hand totaled ₹ 9 Crore.

SOLUTION

CASH FLOW STATEMENT
FOR THE YEAR ENDING 31.03.2013
(DIRECT METHOD)

Particulars	Amounts	Amounts
Cash from Operating Activities:		
Cash sales	131	
Collection from debtors	67	
Payment to suppliers	(159)	
Income tax paid	(13)	26

Cash from investing Activities:		
Sale of machinery (21-.30)	20.70	
Purchase of machinery	(40)	
		(19.3)
Cash from financing Activities:		
Redemption of Preference share capital	(16)	
Issue of equity share capital	16	
Premium on issue	4	
Dividend paid on capitals	(10)	
Dividend distribution tax	(1.7)	
Interest paid	(1)	(8.7)
Total of all activities (O+I+F)		(2)
Add: opening balance of cash and bank		9
Closing balance of cash and bank(bal.fig)		**7**

Note : In the given question, we can not apply indirect method because net profit is not given as well as balance sheets for two years are not given due to which changes can not be calculated.

QUESTION NO 30 (10 MARKS) (NOV. 2011)

The following are the summarized Balance Sheets of Hero Ltd. As on 31st March, 2010 and 2011:

Liabilities	31-03-2010 (₹)	31-03-2011(₹)
Equity share capital (₹ 10 each)	10,00,000	11,50,000
Capital Reserve	-	10,000
Profit and Loss A/c	1,50,000	1,80,000
General reserve	2,50,000	3,00,000
Long term loan from the Bank	5,00,000	4,00,000
Sundry creditors	5,00,000	4,00,000
Provision for taxation	50,000	60,000
Proposed dividend	1,00,000	1,25,000
	25,50,000	26,25,000

Assets	31-03-2010 (₹)	31-03-2011(₹)
Land and building	5,00,000	4,80,000
Machinery	7,50,000	8,20,000
Investment	1,00,000	50,000
Stock	3,00,000	2,80,000
Sundry Debtors	4,00,000	4,20,000
Cash in hand	2,00,000	1,65,000
Cash at Bank	3,00,000	4,10,000
	25,50,000	26,25,000

Additional information:

(i) Dividend of ₹1,00,000 was paid during the year ended 31st march 2011

(ii) Depreciation written off on land and building ₹ 20,000.

(iii) The company sold some investment at a profit of ₹ 10,000 which was credited to Capital Reserve.

(iv) Income Tax provided during the year ₹ 55,000.

(v) During the year, the company purchased a machinery for ₹ 1,25,000.

You are required to prepare a cash flow statement for the year ended 31st March, 2011 as per AS-3, by using indirect method.

SOLUTION:

CASH FLOW STATEMENT

Of Hero Ltd.

FOR THE YEAR ENDING 31.12.2011

Particulars	Amounts	Amounts
Cash from Operating Activities:		
Closing balance in profit and loss a/c	1,80,000	
Transfer to Reserves	50,000	
Proposed/interim dividends	1,25,000	
Opening balance in profit and loss a/c	(1,50,000)	
Net profit for the year	2,05,000	
Depreciation on land & buildings	20,000	
Provision for tax	55,000	

Tax paid **(W.N#1)**	(45,000)	
Depreciation on machinery**(W.N#2)**	55,000	
Working capital adjustments:		
Decrease in stock	20,000	
Increase in debtors	(20,000)	
Decrease in creditors	(1,00,000)	1,90,000
Cash from investing Activities:		
Purchase of machinery (**(W.N#2)**	(1,25,000)	
Sale of investment (50,000+10,000)	60,000	(65,000)
Cash from financing Activities:		
Issue of shares	1,50,000	
Repayment of Bank loan	(1,00,000)	
Dividend paid	(1,00,000)	(50,000)
Total of all activities (O+I+F)		75,000
Add: opening balance of cash and bank		5,00,000
Closing balance of cash and bank		5,75,000

(W.N#1)

Provision for Tax Account

Particulars	Amount	Particulars	Amount
To bank **(bal. fig)**	**45,000**	By balance b/d	50,000
		By PL account **(given)**	55,000
To balance c/d	60,000		
	1,05,000		1,05,000

(W.N#2)

Machinery Account

Particulars	Amount	Particulars	Amount
To balance b/d	7,50,000	By Depreciation	55,000
To Cash	1,25,000	**(bal.fig)**	
		By Balance c/d	8,20,000
	8,75,000		8,75,000

₹ 3,000 only)

QUESTION NO 31 (16 MARKS) (MAY 2011)

The following are the summarized Balance Sheets of Lotus Ltd. As on 31st March, 2010 and 2011:

Liabilities	**31-03-2010 (₹)**	**31-03-2011(₹)**
Equity share capital (₹ 10 each)	10,00,000	12,50,000
Capital Reserve	–	10,000
Profit and Loss A/c	4,00,000	4,80,000
Long term loan from the Bank	5,00,000	4,00,000
Sundry creditors	5,00,000	4,00,000
Provision for taxation	50,000	60,000
	24,50,000	26,00,000
Assets	**31-03-2010 (₹)**	**31-03-2011(₹)**
Land and building	4,00,000	3,80,000
Machinery	7,50,000	9,20,000
Investment	1,00,000	50,000
Stock	3,00,000	2,80,000
Sundry Debtors	4,00,000	4,20,000
Cash in hand	2,00,000	1,40,000
Cash at Bank	3,00,000	4,10,000
	24,50,000	26,00,000

Additional information:

(1) Depreciation written off on land and building ₹ 20,000.

(2) The company sold some investment at a profit of ₹ 10,000 which was credited to Capital Reserve.

(3) Income Tax provided during the year ₹ 55,000.

(4) During the year, the company purchased a machinery for ₹ 2,25,000. They paid ₹ 1,25,000 in cash and issue 10,000 equity shares of ₹ 10 each at par.

You are required to prepare a cash flow statement for the year ended 31st March, 2011 as per AS-3, by using indirect method.

SOLUTION:

CASH FLOW STATEMENT

Of LOTUS Ltd.

FOR THE YEAR ENDING 31.12.2011

Particulars	Amounts	Amounts
Cash from Operating Activities:		
Closing balance in profit and loss a/c	4,80,000	
Transfer to Reserves	Nil	
Proposed/interim dividends	Nil	
Opening balance in profit and loss a/c	(4,00,000)	
Net profit for the year	80,000	
Depreciation on land & buildings	20,000	
Provision for tax	55,000	
Tax paid **(W.N#1)**	(45,000)	
Depreciation on machinery**(W.N#2)**	55,000	
Working capital adjustments:		
Decrease in stock	20,000	
Increase in debtors	(20,000)	
Decrease in creditors	(1,00,000)	

Cash from investing Activities:		
Purchase of machinery (**(W.N#2)**	(1,25,000)	
Sale of investment (50,000+10,000)	60,000	65,000
Cash from financing Activities:		(65,000)
Issue of shares (other than for machinery)	1,50,000	
Repayment of Bank loan	(1,00,000)	50,000
Total of all activities (O+I+F)		50,000
Add: opening balance of cash and bank		5,00,000
Closing balance of cash and bank		5,50,000

(W.N#1)

Provision for Tax Account

Particulars	Amount	Particulars	Amount
To bank	**45,000**	By balance b/d	50,000
(bal. fig)		By PL account	55,000
To balance c/d	60,000	**(given)**	
	1,05,000		1,05,000

(W.N#2)

Machinery Account

Particulars	Amount	Particulars	Amount
To balance b/d	7,50,000	By Depreciation	**55,000**
To Cash	1,25,000	**(bal.fig)**	
To ESC	1,00,000	By Balance c/d	9,20,000
	9,75,000		9,75,000

QUESTION NO 32

From the following Balance Sheet of Avinash Ltd., you are required to prepare Cash flow statement.

Balance Sheet

	1-1-01	31-12-01		1-1-01	31-12-01
Equity Share	3,00,000	4,00,000	Fixed Assets:	4,00,000	5,50,000
Capital			Less: Accumulated		
General Reserve	85,000	1,10,000	Deprecation	80,000	1,35,00
Bank Loan	1,00,000	75,000		3,20,000	4,15,000
Creditors	3,10,000	2,90,000	Investments	80,000	1,10,000
Bank overdraft	—	5,000	Stock	2,00,000	2,25,000
Proposed Dividend	45,000	60,000	Debtors	2,10,000	1,80,000
			Cash	30,000	10,000
	8,40,000	9,40,000		8,40,000	9,40,000

A piece of machinery costing ₹ 50,000 was sold for ₹ 30,000, accumulated deprecation thereon beings ₹ 10, 000.

SOLUTION:

Cash Flow Statement	
Cash from Operating Activities	1,50,000
Cash from Investing activities	(2,00,000)
Cash from Financing Activities	30,000
Total	(20,000)
(+) Opening cash and cash Equivalents	30,000
Closing cash and Cash Equivalents	10,000

Operating Activities	
Increase in General Reserve	25,000
+ Change in Debtors	30,000
+ Deprecation	65,000
+ Loss on Sale of Machinery	10,000
- Change in stock	(25,000)
- Change in Creditors	(20,000)
+ Proposed Dividend	**1,45,000**

Cash from Investing Activities	
Purchase of Fixed Assets	(2,00,000)
Sale of Machinery	30,000
Purchase of Investment	(30,000)
	(2,00,000)
Cash from Financing Activities	
Issue of Equity Share Capital	1,00,000
+ Bank Loan	5,000
- Payment of Bank Loan	(25,000)
- Dividend Paid	(45,000)
	35,000

QUESTION NO 33

From the following information prepare Cash flow statement:

Balance Sheet

	31-3-00	31-3-01		31-3-00	31-3-01
Share Capital	10,00,000	11,00,000	Goodwill	50,000	40,000
Debentures	5,00,000	3,00,000	Land	4,20,000	6,60,000
General Reserve	2,00,000	2,00,000	Machinery	6,00,000	8,00,000
Profit and Loss A/c	1,10,000	1,90,000	Stock	2,50,000	2,10,000
Provision for			Debtors (Good)	3,00,000	2,40,000
Income tax	40,000	1,00,000	Preliminary Exp.	30,000	20,000
Creditors	50,000	40,000	Cash	3,00,000	24,000
Bills payable	20,000	30,000			
Provision for					
Doubtful debts	30,000	24,000			
	19,50,000	19,94,000		19,50,000	19,94,000

Additional Information :

During the year, a part of machine costing ₹ 7,500 (accumulated deprecation thereon being ₹ 2,500) was sold for ₹ 3,000.

Income –tax of 1999-2000 paid in 2000-2001 was ₹ 40,000.

Depreciation on machinery provided for 2000-2001 was ₹ 50,000.

SOLUTION:

Cash Flow Statement	
Cash from operating Activities	3,16,000
Cash from Investing Activities	(1,00,000)
Cash from Financing Activities	(4,92,000)
Total	(2,76,000)
(+) Opening cash and Cash Equivalents	3,00,000
Closing Cash and Cash Equivalents	24,000
Operating Activities	
Change in Profit and Loss Account	80,000
+ Provision for tax	1,10,000
- Tax paid	(40,000)
- Change in Creditors	(10,000)
+ Change in Bills Payable	10,000
+ Goodwill Written off	10,000
+ Loss on Sales on Machine	2,000
+ Deprecation	50,000
+ Change in Stock	40,000
+ Change in Debtors	60,000
+ Preliminarily Expenses Written off	10,000
-Change in Provisions for Doubtful Debts	(6,000)
	3,16,000
Cash from Investing Activities	
Purchase of Land	(2,40,000)
Purchase of Machinery	(2,55,000)
Sale of Machinery	3,000
	4,92,000
Cash from Financing Activities	
Issue of Share Capital	1,00,000
Payment to Debenture holders	(2,00,000)
	1,00,000

QUESTION NO 34

From the following summarized Balance Sheet of a Company, as at 31st March, 2000 and 31st March, 2001 respectively, you are required to prepare cash flow statement All working should from part of your answer.

Balance Sheet

	31-3-00	31-3-01		31-3-00	31-3-01
Equity share capital	75,000	1,20,000	Fixed Assets at	2,40,070	2,53,730
10% redeemable			cost		
Preference Shares			Less: Deprecation	90,020	98,480
Capital	1,00,000	80,000		1,50,050	1,55,250
Reserve for			Investments	61,000	76,000
Replacement of			Stocks	98,000	1,04,000
Machinery	15,000	10,000	Trade Debtors	88,000	85,000
Long term loans	—	40,000	Bank	11,750	32,000
Bank Overdraft	22,000	—			
Trade Creditors	84,450	75,550			
Proposed dividends					
On equity shares	12,000	24,000			
Profit & Loss A/c	1,00,350	1,02,700			
	4,08,800	4,52,250		4,08,800	4,52,250

Additional Information :

1. During the year, additional equity capital was issued to the extent of ₹ 25,000 by way of bonus shares fully paid up.
2. Final dividend on preference shares and an interim dividend of ₹ 4,000 on equity shares were paid on 31st March, 2001.
3. Proposed dividends for the year ended 31st March, 2000 were paid in October, 2000.
4. Movement in Reserve for replacement of machinery account represents transfer to Profit and Loss Account.
5. During the year, one item plant was up valued by ₹ 3,000 and credit for this was taken in then Profit and Loss Account.
6. ₹ 1,700 being capital expenditure on fixed assets for the year ended 31st March, 2000 wrongly debited to Sundry Debtors then, was corrected in the next year.

7. Fixed assets costing ₹ 6,000 (accumulated depreciation ₹ 4,800) were sold for ₹ 250. Loss arising there from was written off.

8. Preference share redeemed in the year were out of a fresh issue of equity shares. Premium paid on redemption was 10%.

SOLUTION:

Cash Flow Statement	
CF OA (S-1)	57,960
CFIA (S-2)	(29,710)
CFFA (S-3)	(8,000)
Total	20,250
(+) Opening Cash & Cash Equivalent	11,750
Closing Cash Equivalent	32,000

CFOA (S-1)	
Change in P/L A/c	2,350
(-) Revaluation of Profits	3,000
(+) Deprecation charged	13,260
(+) Loss on sale	950
(-) Change in stock	6,000
(+) Change in debtors (86,300-85, 000) 1,300	
(+) Bonus out of Profits	25,000
(+) premium on red. Written off	2,000
(-) Movement in reserve in replacement	5,000
(-) change in creditors	8,900
(+) Dividend Proposed/ Pref. interest	36,000
	57,960

CFOA (S-2)	
Asset purchased	(14,960)
Sale of asset	250
	(15,000)
Purchased of Investment	**(29,710)**

CFOA (S-3)	
Issue of share capital	20,000
Redemption of Pref. Cap.	(22,000)
Loan raised	40,000
Bank O/D repaid	(22,000)
	(8,000)
	(8,000)

Working Notes:

Fixed assets Account

Particulars	₹	Particulars	₹
To Balance b/d	2,41,770	By Asset disposal	6,000
To P&L A/c	3,000	By Balance c/d	2,53,730
To bank (Purchase)	14,960		
	2,59,730		2,59,730

Accumulated Depreciation Account

Particulars	₹	Particulars	₹
To Assets deposal Account	4,800	By Balance b/d	90,020
To Balance c/d	98,480	By P & L A/c	13,260
	1,03,280		1,03,280

Asset Disposal A/c

Particulars	₹	Particulars	₹
To Fix Asset	6,000	By A Dep.	4,800
		By bank	250
		By P/L A/c	950
	6,000		6,000
	ESC	A/c	6,000
To Bal. c/d	1,20,000	By bal. b/d	75,000
		By P/L A/c	25,000
		By bank	20,000
	1,20,000	PSC A/c	1,20,000

To cash	22,000	By bal. b/d	1,00,000
To c/d	80,000	By P/L A/c	2,000
	1,02,000		1,02,000

Reserve for Replacement of Machinery A/c

Particulars	₹	Particulars	₹
To P/L A/c	5,000	By bal. b/d	15,000
To bal. c/d	10,000		
	15,000		15,000

Proposed Dividend A/c

Particulars	₹	Particulars	₹
To cash	8,000	By bal. b/d	12,000
To cash	4,000	By P/L A/c	36,000
To cash	12,000		
To bal. c/d	24,000		
	48,000		48,000

QUESTION NO 35

From the following information, prepare cash flow statement:

Balance Sheet

	1-1-01	31-12-01		1-1-01	31-12-01
Share Capital	2,00,000	2,00,000	Cash	8,000	10,000
Profit and Loss A/c	50,000	90,000	Bank	22,000	20,000
Bank Loan	10,000	—	Debtors	10,000	20,000
Creditors	15,000	20,000	Stock	25,000	15,000
Outstanding Exp.	5,000	1,000	Non-current Assets	2,35,000	2,75,000
Provision for Taxation	20,000	25,000			
Unclaimed Dividend		4,000			
	3,00,000	3,40,000		3,00,000	3,40,000

Net profit for the year 2001 after providing ₹ 20,000 depreciation was ₹ 60,000. During the 2001, Company declared equity dividend @ 10%, and paid ₹ 15,000 as income tax.

SOLUTION:

Cash Flow Statement	
Cash from operating Activities	86,000
Cash from Investing Activities	(60,000)
Cash from Financing Activities	(26,000)
Total	Nil
(+) Opening Cash and Cash Equivalents (8,000 + 22,000)	30,000
Closing cash and Equivalents (20,000 + 10, 000)	30,000
Operating Activities	
Increase in Profit and Loss Account	40,000
+ Depreciation	20,000
+ Proposed Dividend (2,00,000 x 10%)	20,000
- Income Tax paid	(15,000)
+ Provision for Tax	20,000
+ Change in Stock	10,000
- Change in Debtors	(10,000)
+ Change in Creditors	5,000
- Change in out Expenses	(4,000)
	86,000
Investing Activities	
Purchase of Assets	(60,000)
(2,78,000 +20,000-2,35,000)	
	60, 000
Financing Activities	
Bank Loan paid	(10,000)
Dividend Paid	(16,000)
	(26,000)

QUESTION NO 36

From the following comparative balance Sheet of M/s A Ltd. make out:

Cash flow statement

Liabilities	2001 ₹	2002 ₹	Assets	2001 ₹	2002 ₹
Equity share capital	3,00,000	4,00,000	Goodwill	1,15,000	90,000
Preference Share			Land & Building	2,00,000	1,70,000
Capital	1,50,000	1,00,000	Plant	80,000	2,00,000
General Reserve	40,000	70,000	Debtors	1,60,000	2,00,000
Profit and Loss A/c	30,000	48,000	Stock	77,000	1,09,000
Proposed Dividends	42,000	50,000	Bills Receivable	20,000	30,000
Creditors	55,000	83,000	Cash	15,000	10,000
Bills Payable	20,000	16,000	Bank	10,000	8,000
Provision for Taxation	40,000	50,000			
	6,77,000	8,17,000		6,77,000	8,17,000

Supplementary Data :

(1) Depreciation of ₹ 10,000 and ₹ 20,000 have been charged on plant and Lnad and Building respectively in 2002.

(2) An interim dividend of ₹ 20,000 has been paid in 2002.

(3) Income-tax ₹ 35,000 has been paid during the year 2002.

SOLUTION:

CASH FLOW STATEMENT	
Cash from operating Activities	83,000
Cash from Investing Activities	(1,20,000)
Cash from Financing activities	30,000
Total	(7,000)
(+) Opening Cash and cash equivalents	25,000
Closing Cash and Cash Equivalents	18,000

Operating Activities	
Increase in General Reserve	30,000
+ Increase in Profit & Loss	18,000
+ Goodwill written off	25,000
+ Depreciating of Plant	10,000
+ Depreciation on land & Building	20,000
+ Change in Creditors	28,000
+ Proposed Dividend	28,000
+ Provision for Taxation	45,000
- Change in Debtors	40,000
- Change in Stock	32,000
-Change in Bills Receivable	10,000
- Change in Bill Payable	4,000
-Tax. Paid	35,000
	83,000
Cash from Investing Activities	
Purchase of Plant	(1,30,000)
Sale of Land & Building (2,00,000-20,000-1,70,000)	10,000
	(1,20,000)
Cash from Financing Activities	
Issue of Equity Share Capital	1,00,000
Redemption of Preference Share Capital	(50,000)
Interim Dividend Paid	(20,000)
	30,000

QUESTION NO 37

From the following details relating to the accounts of Husmundi & Co. Ltd. Prepare Cash Flow Statement.

Liabilities	31-12-86 ₹	31-12-85 ₹
Share Capital	4,00,000	3,00,000
Reserve	1,00,000	80,000
Profit & Loss Account	50,000	30,000
Debentures	1,00,000	1,50,000
I.T. Provision	40,000	50,000
Trade Creditors	70,000	90,000
Proposed Dividend	40,000	30,000
	8,00,000	7,30,000

Assets	31-12-86 ₹	31-12-85 ₹
Goodwill	90,000	1,00,000
Plant & Machinery	4,29,250	2,98,000
Debenture Discount	5,000	8,000
Prepaid Expenses	5,750	4,000
Investments	60,000	1,00,000
Sundry Debtors	1,10,000	1,60,000
Stock	80,000	50,000
Cash and Bank	20,000	10,000
	8,00,000	7,30,000

1. 15% depreciation has been charged in the accounts on plant & Machinery.
2. Old machine costing ₹ 50,000 (WDV 20,000) have been sold for ₹ 35,000,
3. A machine costing ₹ 10,000 (WDV ₹ 3,000) has been discarded.
4. ₹ 10,000 profit has been earned by sale of investments.
5. Debentures have been redeemed at 5% premium.
6. ₹ 45,000 income tax has been paid and adjusted against Income Tax Provision Accounts.

(20 marks)

SOLUTION:

Cash Flow Statements	
Cash From Operating Activities	1,37,500
Cash From Investing Activities	(1,45,000)
Cash From Financing Activities	17,500
Total	10,000
Add opp CSCE	10,000
Closing C&CE	20,000

Cash From Operating Activities	
Interest in Pls	20,000
Interest in Profit & Loss Account	20,000
(+) G/W W/off	10,000
(-) Profit on sale of M/C	15,000
(+) Profit & machinery discarded	3,000
(+) Deprecation on machinery	75,750
(+) Discount on deb w/off	3,000
(-) change in PP exp	1,750
(+) change in debtors	50,000
- change in stock	30,000
(+) prevention on red of debtor	2,500
(+) provision fro tax	35,000
(-) interest tax paid	45,000
(-) change in creditors	20,000
(+) proposed dividend	40,000
(-) profit on sale	10,000
	1,37,500

Cash From Investing Activities	
Sale of Plant & machinery	35,000
Purchase of plant & machinery	(2,30,000)
Sale of invests	50,000
	(1,45,000)

Cash from Financing Activities	
Issue of S cap	1,00,000
Redemption of deb	(52,500)
Dividend paid	(30,000)
	17,500

Profit and Machinery Account			
To Balance b/d	2,98,000	By bank	35,000
To profit & Loss A/c	15,000	By profit & Loss discard	3,000
To Bank	2,30,000	By Depreciations	75,750
		By Balance c/d	4,29,250
	5,43,000		5,43,000

Investment Account			
To balance b/d	1,00,000	By bank	50,000
Profit & Loss	-10,000	By Balance c/d	60,000
	1,10,000		1,10,000

Provision & tax			
To cash	45,000	By Balance b/d	50,000
To balance c/d	40,000	By Profit & Loss Account	35,000
	85,000		85,000

QUESTION NO 38

From the following information, prepared a cash Flow Statement as per AS for Banjara Ltd. using direct method:

Balance Sheet as on March 31,2010 (₹ 000)

Assets:		2010		2009
Cash on hand and balances with bank		200		25
Marketable securities (having one month maturity)		670		135
Sundry debtors		1,700		1,200
Interest receivable		100		
Inventories		900		1,950

Investments		2,500		2,500
Fixed assets at cost	2,180		1,910	
Accumulated depreciation	(1,450)		(1,060)	
Fixed assets (net)		730		850
Total assets		6,800		6,660
Liabilities:		**2010**		**2009**
Sundry creditors		150		1,890
Interest payable		230		100
Income tax payable		400		1,000
Long term debt		1,110		1,040
Total liabilities		1,890		4,030
Shareholder's fund:				
Share capital		1,500		1,250
Reserves		3,410		1,380
		4,910		2,630
Total liabilities and shareholders' fund		6,800		6,660

Statement of Profit and Loss for the year ended 31.03.2010

	(₹ 000)
Sales	30,650
Cost of sales	(26,000)
Gross Profit	4,650
Depreciation	(450)
Administrative and selling expenses	(910)
Interest expenses	(400)
Interest income	300
Dividend income	200
Net profit before taxation and extraordinary	3,390
Extraordinary items :	
Insurance proceeds from earthquake disaster settlement	140
Net profit after extraordinary items	3,530
Income tax	(300)
	3,230

Additional information :

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

(ii) Interest expense was ₹ 400 of which ₹ 770 was paid during the period ₹ 100 relating to interest expense of the prior period was also paid during the period.

(iii) Dividends paid were ₹ 1,200.

(vi) Tax deducted at source on dividends received (including in the tax expense of ₹ 300 for the year) amounted to ₹ 40.

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

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

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

SOLUTION:

Cash Flow Statement (Direct Method)		
Cash flows from Operating Activities		
Cash receipts from customers (W.N. 2)	30,150	
Cash paid to suppliers, employees and for expenses (W.N. 3)	(27,600)	
Cash generated from operations	2,550	
Income tax paid (W. N 4)	(860)	
	1,690	
Cash flow before extraordinary item:		
Proceeds from earthquake disaster settlement	140	
Net cash from operating activities		1830
Cash flows from Investing Activities:		
Purchase of fixed assets	(350)	
Proceeds from sale and equipment	20	
Interest received (300-100)	200	
Dividends received (200-40)	160	
Net cash from investing activities		30
Cash flows from Financing Activities:		
Proceeds from issuance of share capital	250	
Proceeds from long term borrowings	250	
Repayment of long term borrowings (W. N 5)	(180)	
Interest paid (W.N. 6)	(270)	
Dividends paid	(1,200)	

Net cash used in financial activities		(1150)
Net increase in cash and cash equivalents		
Cash and cash equivalents at beginning of the period (W. N. 1)		710
Cash and cash equivalents at end of the period (W.N. 1)		160
		870

Working Notes :

(1) Cash and cash equivalents

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

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

(2) Cash receipts from customers

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

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

		₹ 000
Cost of sales		26,000
Administrative and selling expenses		910
		26,910
Add: Sundry creditors at the beginning of the year	1,890	
Inventories at the end of year	900	2,790
		(29700)
Less: Sundry creditors at the end of year Inventories at	(150)	
the beginning of the year	(1950)	2100
		27,600

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

	₹ 000
Income Tax expense for the year	300
Including tax deducted at sources from dividend received	
Add: Income Tax liability at the beginning of the year	1,000
Less: Income Tax liability at the end of the year	1,300
	(400)
	900

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

(5) Repayment of long term borrowings during the year

	₹ 000
Long term debts at the beginning of the year	1,040
Add: Long term borrowings made during the year	(250)
Less : Long term borrowing at the end of the year	1290
	1110

(6) Interest paid during the year

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

QUESTION NO 39

Explain Classification of activities (with two examples) as suggested in AS 3, to be used for preparing a cash flow statements.

SOLUTION

AS 3 (Revised) on cash Flow Statements requires that the cash flow statement should cash flows by operating, investing and financing activities.

Additional information :

(i) Operating activities are the principal revenue-producing activities of the enterprise and other activities that are not investing or financing activities. Cash receipts from sale of goods and cash payments to suppliers of goods are two examples of operating activities.

(ii) Investing activities are acquisition and disposal of long-term assets and other investments not included in cash equivalents. Payment made to acquire machinery and cash received for sale furniture are examples of investing activities.

(iii) Financial activities are those activities that result in changes in the size and composition of the owner's capital (including preference share capital in the case of a company) and borrowings of the enterprise. Cash proceeds from issue of shares and cash paid to redeem debentures are two examples of financing activities.

QUESTION 40

Explain the difference between direct and indirect methods of reporting cash flows from operating activities with reference to Accounting Standard 3, (AS 3) revised.

SOLUTION

As per Para 18 of AS 3 (Revised) on Cash Flow Statements, an enterprise should report cash flow from operating activities using either:

(a) The direct method, whereby major classes of gross cash receipts and gross cash payments are disclosed: or

(b) the indirect method, whereby net profit or loss is adjusted for the effects of transactions of a non-cash nature, any deferrals or accruals of past or future operating cash receipts or payments, and items of income or expense associated with investing or financing cash flows.

The direct method provides information which may be useful in estimating future cash flows and which is not available under the indirect method and is, therefore, considered more appropriate than the indirect method. Under the direct method, information about major classes of gross cash receipts and gross cash payments may be obtained either:

(a) from the accounting records of the enterprise; or

(b) by adjusting sales, cost of sales (interest and similar income and interest expenses and similar charges for a financial enterprise) and other items in the statement of profit and loss for :

(i) changes during the period in inventories and operating receivables and payables;

(ii) other non-cash items; and

(iii) other items for which the cash effects are investing or financing cash flows.

Under the indirect method, the net cash flow from operating activities is determined by adjusting net profit or loss for the effects of:

(a) changes during the period in inventories and operating receivables and payables;

(b) non-cash items such as depreciation, provisions, deferred taxes and unrealized foreign exchange gains and losses; and

(c) all other items for which the cash effects are investing or financing cash flows.

Alternatively, the net cash flow from operating activities may be presented under the indirect method by showing the operating revenues and expenses, excluding non-cash items disclosed in the statement of profit and loss and the changes during the period in inventories and operating receivables and payables.

QUESTION 41

From the following Balance Sheets of Mr. Zen, prepare a Cash flow statement as per AS-3 for the year ended 31.3.2015:

Balance Sheet of Mr. Zen

Liabilities	**As on 1.4.2014** ₹	**As on 1.4.2015** ₹
Zen's Capital A/c	10,00,000	12,24,000
Trade payables	3,20,000	3,52,000
Mrs. Zen's loan	2,00,000	--
Loan from Bank	3,20,000	4,00,000
	18,40,000	19,76,000

Assets	As on 1.4.2014 ₹	As on 1.4.2015 ₹
Land	6,00,000	8,80,000
Plant and Machinery	6,40,000	4,40,000
Inventories	2,80,000	2,00,000
Trade receivables	2,40,000	4,00,000
Cash	80,000	56,000
	18,40,000	19,76,000

Additional information:

A machine costing ₹80,000 (accumulated depreciation there on ₹24,000) was sold for ₹40,000. The provision for depreciation on 1.4.2014 was ₹2,00,000 and 31.3.2015 was ₹3,20,000. The net profit for the year ended on 31.3.2015 was ₹3,60,000.

SOLUTION

Cash Flow Statement of Mr. Zen as per AS 3
for the year ended 31.3.2015

			₹
(i)	**Cash flow from operating activities**		
	Net Profit (given)		3,60,000
	Adjustments for		
	Depreciation on Plant & Machinery	1,44,000	
	Loss on Sale of Machinery	16,000	1,60,000
	Operating Profit before working capital changes		5,20,000
	Decrease in inventories	80,000	
	Increase in trade receivables	(1,60,000)	
	Increase in trade payable	32,000	(48,000)
	Net cash generated from operating activities		4,72,000
(ii)	**Cash flow from investing activities**		
	Sale of Machinery	40,000	
	Purchase of Land	(2,80,000)	
	Net cash used in investing activities		(2,40,000)

(iii) **Cash flow from financing activities**		
Repayment of Mrs. Zen's Loan	(2,00,000)	
Drawings	1,36,000)	
Loan from Bank	80,000	
Net cash used in financing activities		(2,56,000)
Net decrease in cash		(24,000)
Opening balance as on 1.4.2014		80,000
Cash balance as on 31.3.2015		56,000

Working Notes:

1. **Plant & Machinery A/c**

	₹		₹
To Balance b/d	8,40,000	By Cash-Sales	40,000
(6,40,000+2,00,000)		By Provision for Depreciation A/c	24,000
		By Profit & Loss A/c- Loss on	16,000
		Sale (80,000-64,000)	
		By Balance c/d	
		(4,40,000+3,20,000)	7,60,000
	8,40,000		8,40,000

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

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

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

	₹
Opening Capital	10,00,000
Add: Net Profit	3,60,000
	13,60,000
Less: Closing Capital	(12,24,000)
Drawings	1,36,000

QUESTION 42

From the following information, prepare cash flow statement of A (P) Ltd. as at 31st March, 2015 by using indirect method:

Balance Sheet

	2014 ₹	2014 ₹
Liabilities:		
Share capital	12,00,000	12,00,000
Profit and loss account	8,50,000	10,00,000
Long term loans	10,00,000	10,60,000
Trade payables	3,50,000	4,00,000
	34,00,000	36,60,000
Assets:		
Fixed assets	17,00,000	20,00,000
Investment in shares	2,00,000	2,00,000
Inventory	6,80,000	7,00,000
Trade receivables	7,60,000	6,90,000
Cash	60,000	70,000
	34,00,000	36,60,000

Income Statement for the year ended 31st March, 2015

		₹
Sales		40,80,000
Less: Cost of sales		(27,20,000)
Gross profit		13,60,000
Less: Operating expenses:		
Administrative expenses	4,60,000	
Depreciation	2,20,000	(6,80,000)
Operating profit		6,80,000
Add: Non-operating incomes (dividend received)		50,000
		7,30,000
Less: Interest Paid		(1,40,000)
Profit before tax		5,90,000
Less: Income-tax		(2,60,000)
Profit after tax		3,30,000

Statement of Retained Earnings

	₹
Opening balance	8,50,000
Add: Profit	3,30,000
	11,80,000
Less: Dividend paid	(1,80,000)
Closing balance	10,00,000

SOLUTION

Cash Flow Statement of A (P) Ltd.
for the year ended 31st March, 2015

		₹	₹
(i)	Cash flows from operating activities		
	Profit before tax	5,90,000	

	Adjustments for		
	Depreciation	2,20,000	
	Interest paid	1,40,000	
	Dividend received	(50,000)	
	Operating profit before working capital changes	9,00,000	
	Add:		
	Decrease in trade receivables	70,000	
	Increase in trade payables	50,000	
		10,20,000	
	Less: Increase in inventory	(20,000)	
	Cash generated from operations	10,00,000	
	Less: Tax paid	(2,60,000)	
	Cash flow operating activities		7,40,000
(ii)	**Cash flows from investing activities**		
	Purchase of fixed assets	(5,20,000)	
	[20,00,000+2,20,000-17,00,000]		
	Dividend on investments	50,000	
	Cash used in investing activities		(4,70,000)
(iii)	**Cash flows from financing activities**		
	Long term loan taken	60,000	
	Interest paid	(1,40,000)	
	Dividend paid	(1,80,000)	
	Cash used in financing activities		(2,60,000)
Net increase in cash during the year			10,000
Add: Opening cash balance			60,000
Closing cash balance			70,000

QUESTION 43

The Balance Sheets of X Ltd. as on 31st March, 2014 and 31st March, 2015 are as follows:

Liabilities	2014 Amount (₹)	2015 Amount (₹)	Assets	2014 Amount (₹)	2015 Amount (₹)
Share Capital	5,00,000	7,00,000	Land and Building	80,000	1,20,000
General Reserve	50,000	70,000	Plant and Machinery	5,00,000	8,00,000
Profit and Loss A/c	1,00,000	1,60,000	Inventory	1,00,000	75,000
Trade payable	1,93,000	240,000	Trade receivables	1,50,000	1,60,000
			Cash	20,000	20,000
Outstanding Expenses	7,000	5,000			
	8,50,000	11,75,000		8,50,000	11,75,000

Additional Information:

(a) ₹ 50,000 depreciation has been charged to Plant and Machinery during the year 2015.

(b) A piece of Machinery costing ₹ 12,000 (Depreciation provided there on ₹ 7,000) was sold at 60% profit on book value.

You are required to prepare Cash flow statement for the year ended 31st March 2015 as per AS 3 (revised), using indirect method.

SOLUTION

Cash Flow Statement for the year ended 31st March, 2015

	Amount ₹	Amount ₹
I. Cash Flows from Operating Activities		
Closing Balance as per Profit & Loss A/c		1,60,000
Less: Opening Balance as per Profit & Loss A/c		(1,00,000)
		60,000

Add:	Transfer to General Reserve		20,000
	Net Profit before taxation and extra-ordinary items		80,000
Add:	Depreciation on Plant and Machinery		50,000
Less:	Profit on sale of machinery (Refer W.N.)		(3,000)
	Operating Profit		1,27,000
Add:	Decrease in Inventory	25,000	
	Increase in trade payable	47,000	72,000
			1,99,000
Less:	Increase in trade receivables	(10,000)	
	Decrease in Outstanding expenses	(2,000)	(12,000)
	Net Cash from Operating Activities		1,87,000
II.	**Cash Flows from Investing Activities**		
	Purchase of Land & Building	(40,000)	
	Proceeds from Sale of Machinery (Refer W.N.)	8,000	
	Purchases of Plant & Machinery (Refer W.N.)	(3,55,000)	
	Net Cash used in Investing Activities		(3,87,000)
III.	**Cash Flows from Financing Activities**		
	Proceeds from Issuance of Share Capital	2,00,000	
	Net Cash from Financing Activities		2,00,000
	Net Increase / Decrease in Cash & Cash Equivalents		0
Add:	Cash in hand at the beginning of the year		20,000
Cash in hand at the end of the year			20,000

Working Note:

Plant and Machinery Account

	₹		₹
To Balance b/d	5,00,000	By Bank	8,000*
To Profit and Loss A/c (Profit on sale)	3,000	By Depreciation	50,000
To Purchase (Bal. fig.)	3,55,000	By Balance c/d	8,00,000
	8,58,000		8,58,000

QUESTION 44

The following are the summarized Balance Sheet Star Ltd. as on 31st March, 2014 and 2015:

		(₹ '000)
	2014	2015
Equity share capital of ₹10 each	3,400	3,800
Profit and Loss A/c	400	540
Securities Premium	40	80
14% Debentures	800	900
160% of (12,000-7,000) = ₹ 8,000		
Long term borrowings	180	240
Trade payables	360	440
Provision for Taxation	20	40
Dividend payable	300	480
	5,500	6,520
Sundry Fixed Assets:		
Gross Block	3,200	4,000
Less: Depreciation	(640)	(1,440)
Net Block	2,560	2560
Investment	1,200	1,400
Inventories	1,000	1,400
Trade receivables	640	900
Cash and Bank Balance	100	260
	5,500	6,520

The Profit and Loss account for the year ended 31st March, 2015 disclosed:

	(₹ '000)
Profit before tax	780
Less: Taxation	(160)
Profit after tax	620
Less: Dividend payable	(480)
Retained Profit	140

The following information are also available:

(1) 40,000 equity shares issued at a premium of ₹ 1 per share

(2) The Company paid taxes of ₹ 1,40,000 for the year 2014-15.

(3) During the period, it discarded fixed assets costing ₹ 4 lacs, (accumulated depreciation ₹ 80,000) at ₹ 40,000 only.

You are required to prepare a cash flow statement as per AS 3 (Revised), using indirect method,

SOLUTION

Cash Flow Statement for the year ended 31st March, 2015

			(₹ '000)
(A)	**Cash flow from operating activities**		
	Net profit before tax	780	
	Add: Adjustment for depreciation	880	
	Loss on sale of fixed assets	280	
	Interest on debentures	126	
	Operating profit before changes in working capital	2,066	
	Less: Increase in trade receivables	(260)	
	Less: Increase in Inventories	(400)	
	Add: Increase in trade payables	80	
	Cash generated from operations	1,486	
	Less: Income tax paid W.N.1)	140	
	Net cash from operating activities		1,346
(B)	**Cash flow from investing activities**		
	Purchase of fixed assets	(1,200)	
	Sale of fixed assets	40	
	Purchase of investments	(200)	
	Net cash used in investing activities		(1,360)
(C)	**Cash flow from financing activities**		
	Proceeds from issue of shares including premium (400+40)	440	

	Proceeds from issue of 14% debentures (900-800)	100	
	Proceeds from long term borrowings	60	
	Interest on debentures	(126)	
	Payment of dividend	(300)	
	Net cash from financing activities		174
	Net increase in cash and cash equivalents (A+B+C)		160
	Cash and cash equivalents at the beginning of the year		100
	Cash and cash equivalents at the end of the year		260

Working Notes:

1.	**Calculation of Income tax paid during the year**	(₹ '000)
	Income tax expense for the year	160
	Add: Income tax liability at the beginning of the year	20
		180
	Less: Income tax liability at the end of the year	(40)
	Income tax paid during the year	140
2	**Calculation of Fixed assets purchased during the year**	
	Closing balance of gross block of fixes assets	4,000
	Add: Cost assets discarded during the year	400
		4,400
	Less: Opening balance of gross block of fixed assets	(3,200)
	Fixed assets purchased during the year	1,200
3.	**Calculation of Depreciation charged during the year**	
	Closing balance of accumulated depreciation	1,440
	Add: Depreciation charged on assets discarded during the year	80
		1,520
	Less: Opening balance of accumulated depreciation	(640)
	Depreciation charged during the year	880

QUESTION 45

Intelligent Ltd., a non-financial company has the following entries in its Bank Account. It has sought your advice on the treatment of the same for preparing Cash Flow Statement.

(i) Loans and Advances given to the following and interest earned on then:

(1) To suppliers

(2) To employees

(3) To its subsidiaries companies

(ii) Investment made in subsidiary Smart Ltd. and dividend received

(iii) Dividend paid for the year

(iv) TDS on interest income earned on investments made

(v) TDS on interest earned on advance given to suppliers

(vi) Insurance claim received against loss of fixed asset by fire

Discuss in the context of AS 3 Cash Flow Statement.

SOLUTION

(i) **Loans and advances given and interest earned**

(1)	to suppliers	Operating Cash flow
(2)	to employees	Operating Cash flow
(3)	To its subsidiary companies	Investing Cash flow

(ii) **Investment made in subsidiary company and dividend received**

Investing Cash flow

(iii) **Dividend paid for the year**

Financing Cash Outflow

(iv) **TDS on interest income earned on investments made**

Investing Cash Outflow

(v) **TDS on interest earned on advance given to suppliers**

Operating Cash Outflow

(vi) **Insurance claim received of amount loss of fixed asset by fire**

Extraordinary item to be shown under a separate heading as 'Cash inflow from Operating activities.

QUESTION 46

Prepare cash flow statement of M/'s MNT Ltd. for the year ended 31st March, 2015 with the help of the following information:

(1) Company sold goods for cash only.

(2) Gross Profit Ratio was 30% for the year, gross profit amounts to ₹ 3,82,500.

(3) Opening inventory was lesser than closing inventory by ₹ 3,500.

(4) Wages paid during the year ₹ 4,92,500.

(5) Office and selling expenses paid during the year ₹ 75,000.

(6) Dividend paid during the year ₹ 30,000 (including dividend distribution tax.)

(7) Bank loan repaid during the year ₹ 2,15,000 (included interest ₹ 15,000)

(8) Trade payables on 31st March, 2014 exceed the balance on 31st March, 2015 by ₹ 25,000.

(9) Amount paid to trade payables during the year ₹ 4,60,000.

(10) Tax paid during the year amounts to ₹ 65,000 (Provisions for taxation as on 31.03.2015 ₹ 45,000).

(11) Investments of ₹ 7,00,000 sold during the year at a profit of ₹ 20,000.

(12) Depreciation on fixed assets amounts to ₹ 85,000.

(13) Plant and machinery purchased on 15th November, 2014 for ₹ 2,50,000.

(14) Cash and Cash Equivalents on 31st March, 2014 ₹ 2,00,000.

(15) Cash and Cash Equivalents on 31st March, 2015 ₹ 6,07,500.

SOLUTION

M/s MNT Ltd.

Cash Flow Statement for the year ended 31st March, 2015

(Using direct method)

Particulars	₹	₹
Cash flows from Operating activities		
Cash sales (3,82,500/30		12,75,000
Less: Cash payments for trade payables	(4,60,000)	
Wages paid	(4,92,500)	
Office and selling expenses	(75,000)	(10,27,500)

Cash generated from operations before taxes		2,47,500
Income tax paid		(65,000)
Net cash generated from operating activities (A)		1,82,500
Cash flows from investing activities		
Sale of investments	7,20,000	
Payments for purchase of Plant Y Machinery	(2,50,000)	
Net cash used in investing activities (B)		4,70,000
Cash flows from financing activities		
Bank loan repayment (including interest)	(2,15,000)	
Dividend paid (including dividend distribution tax)	30,000)	
Net cash used in financing activities (C)		(2,45,000)
Net increase in cash (A+B+C)		4,07,500
Cash and cash equivalents at beginning of the period		2,00,000
Cash and cash equivalents at end of the period		6,07,500

QUESTION 47 (CA INTER NOV 2019 EXAMS) (5 MARKS)

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

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

SOLUTION:

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

Cash generated from investing activities	₹	₹
Interest on loan received	70,000	
Pre-acquisition dividend received on investment made	52,600	
Unsecured loans given to subsidiaries	(5,00,000)	
Interest received on investments (gross value)	82,000	
TDS deducted on interest	(8,200)	
Sale of Plant & Machinery ₹ (90,000 – 9,600)	80,400	
Cash used in investing activities (before extra-ordinary item)		(2,23,200)
Extraordinary claim received for loss of machinery		55,000
Net cash used in investing activities (after extra-ordinary item)		(1,68,200)

Note:

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

QUESTION 48 (CA INTER NOV 2020) (10 MARKS)

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

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

(a) Depreciation on Property, Plant & Equipment ₹ 7.50 lakhs.

(b) Discount on issue of Debentures written off ₹ 45,000.

(c) Interest on Debentures paid ₹ 5,25,000.

(d) Book value of investments ₹ 4.50 lakhs (Sale of Investments for ₹ 4,80,000).

(e) Interest received on investments ₹ 90,000.

(ii) Compensation received ₹1,35,000 by the company in a suit filed.

(iii) Income tax paid during the year ₹ 15,75,000.

(iv) 22,500, 10% preference shares of ₹ 100 each were redeemed on 02-04-2019 at a premium of 5%.

(v) Further the company issued 75,000 equity shares of ₹10 each at a premium of 20% on 30.3.2020 (Out of 75,000 equity shares, 25,000 equity shares were issued to a supplier of machinery)

(vi) Dividend for FY 2018-19 on preference shares were paid at the time of redemption.

(vii) Dividend on Equity shares paid on 31.01.2020 for the year 2018-2019 ₹ 7.50 lakhs (including dividend distribution tax) and interim dividend paid ₹ 2.50 lakhs for the year 2019-2020.

(viii) Land was purchased on 02.4.2019 for ₹3,00,000 for which the company issued 22,000 equity shares of ₹ 10 each at a premium of 20% to the land owner and balance in cash as consideration.

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

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

SOLUTION:

Manan Ltd.

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

	₹	₹
Cash flow from Operating Activities		
Net profit before income tax and extraordinary items:		30,00,000
Adjustments for:		
Depreciation on Property, plant and equipment	7,50,000	
Discount on issue of debentures	45,000	
Interest on debentures paid	5,25,000	
Interest on investments received	(90,000)	
Profit on sale of investments	(30,000)	12,00,000
Operating profit before working capital changes		42,00,000
Adjustments for:		
Increase in inventory	(1,77,000)	
Decrease in trade receivable	7,350	
Increase in trade payables	450	
Increase in outstanding expenses	10,200	(1,59,000)
Cash generated from operations		40,41,000
Income tax paid		(15,75,000)

Cash flow from ordinary items		24,66,000
Cash flow from extraordinary items:		
Compensation received in a suit filed		1,35,000
Net cash flow from operating activities		26,01,000
Cash flow from Investing Activities;		
Sale proceeds of investments	4,80,000	
Interest received on investments	90,000	
Purchase of land (3,00,000 less 2,64,000)	(36,000)	
Net cash flow from investing activities		5,34,000
Cash flow from Financing Activities		
Proceeds of issue of equity shares at 20% premium	6,00,000	
Redemption of preference shares at 5% premium	(23,62,500)	
Preference dividend paid	(2,25,000)	
Interest on debentures paid	(5,25,000)	
Dividend paid (7,50,000 + 2,50,000)	(10,00,000)	
Net cash used in financing activities		(35,12,500)
Net decrease in cash and cash equivalents during the year		(3,77,500)
Add: Cash and cash equivalents as on 31.3.2019		3,94,450
Cash and cash equivalents as on 31.3.2020		16,950

QUESTION 49 (CA INTER JAN 21) (12 MARKS)

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

(1) Net profit before talking into account income tax and after talking into account the following items was ₹30 lakhs;

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

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

(iii) Interest on debentures paid ₹4,35,000

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

(v) Interest received on Investments ₹70,000

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

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

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

(5) Dividend paid during the year amounted to ₹11 Lakhs (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 ₹8 Lakhs but the vendor took over the old plant at a value of ₹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 ₹ 13,50,000.

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

	As on 1st April,2019 (₹)	As on 31st March,2020 (₹)
Inventory	13,50,000	14,76,000
Trade Receivables	3,27,000	3,13,200
Cash &Bank Balances	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 changes		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.

QUESTION 50 (CA INTER JULY 21)(5 MARKS)

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

Cash summary Account

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

equipment		Taxation	6,561
		Dividends	2,160
		Repayment of Bank Overdraft	6,750
		Interest paid on Bank overdraft	1,350
		Closing Balance	4,374
	87,642		87,642

SOLUTION:

Gama Limited

Cash Flow Statement

For the Year Ended 31st March 2021

Particulars	Amount (₹'000)	Amount (₹'000)
Cash flow from Operating Activities:		
Cash receipts from customers	74,682	
Cash payments to suppliers	(54,918)	
Cash payments for wages & salaries	(1,863)	
Cash payments of overheads	(3,105)	
Cash Generated from Operations	14,796	
Payment of Taxation	(6,561)	
Net Cash from Operating Activities		8,235
Cash Flow from Investing Activities:		
Proceeds from sale of investments	459	
Proceeds from sale of Property, Plant and Equipment	3,456	
Purchase of Investments	(351)	
Purchase of Property, Plant and Equipment	(6,210)	
Net Cash Used in Investing Activities		(2,646)

Cash Flow from Financing Activities:		
Proceeds from issue of shares	8,100	
Payment of Dividend	(2,160)	
Repayment of Bank Overdraft	(6,750)	
Interest paid on Bank Overdraft	(1,350)	
Net Cash Used in Financing Activities		(2,160)
Net Increase in Cash & Cash Equivalent		3,429
Cash and Cash Equivalent in the Beginning of the year		945
Cash and Cash Equivalent in the end of the year		4374

QUESTION 51 (CA INTER DEC. 2021 EXAMS : 5 MARKS)

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

Liabilities	31.3.2020	31.3.2021
	(₹)	(₹)
Equity Share Capital	25,00,0000	35,60,000
10% Preference Share Capital	7,00,000	6,00,000
Securities Premium Account	5,00,000	5,50,000
Profit & Loss A/c	20,00,000	28,00,000

Equity Share Capital for the year ended 31st March, 2021 includes ₹ 60,000 of equity shares issued to Grey Ltd. at par for supply of Machinery of ₹ 60,000.

Profit & Loss account on 31st March, 2021 includes ₹ 50,000 of dividend received on Equity shares invested in X Ltd.

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

SOLUTION :

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

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

Note:

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

QUESTION 52 (CA INTER MAY 2022 EXAMS : 5 MARKS)

The following information is provided by Alpha Limited, for the year ended 31st March, 2022:

(i) Net profit before taking into account income tax and income from law suits but after taking into account the following items was ₹ 40 lakhs.

(ii) Depreciation on Fixed Assets ₹ 10 lakhs.

(iii) Discount on issue of Debentures written of ₹ 60,000.

(iv) Interest on Debentures paid ₹ 7,00,000.

(v) Book value of investments ₹ 6 lakhs (Sale of Investments for ₹ 6,40,000).

(vi) Interest received on investments ₹ 1,20,000.

(vii) Compensation received ₹ 1,80,000 by the company in a suit filed.

(viii) Income tax paid ₹ 21,00,000

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

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

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

SOLUTION :

Alpha Ltd.

Cash Flow Statement (from Operating Activities)

for the year ended 31st March, 2022

	₹	₹
Cash flow from Operating Activities		
Net profit before income tax and extraordinary items:		40,00,000
Adjustments for:		
Depreciation on Property, plant and equipment	10,00,000	
Discount on issue of debentures	60,000	
Interest on debentures paid	7,00,000	
Interest on investments received	(1,20,000)	
Profit on sale of investments	(40,000)	16,00,000
Operating profit before working capital changes		56,00,000
Adjustments for:		
Increase in inventory	(2,36,000)	
Increase in Sundry Debtors	(10,200)	

Decrease in Bills receivables	20,000	
Increase in Sundry Creditors	10,600	
Increase in Bills payables	(10,000)	
Increase in outstanding expenses	13,600	(2,12,000)
Cash generated from operations		53,88,000
Income tax paid		(21,00,000)
Cash flow from ordinary items		32,88,000
Cash flow from extraordinary items:		
Compensation received in a suit filed		1,80,000
Net cash flow from operating activities		34,68,000

QUESTION 53 (CA INTER NOV. 2022 EXAMS : 5 MARKS)

Ridgeway Limited, a Non-Financial company has the following activities:

(i) Dividend paid for the year.

(ii) TDS on interest income earned on investments made.

(iii) Loans and advances given to suppliers and interest earned from them.

(iv) Deposit with bank for a term of two years.

(v) Highly liquid Marketable Securities (without risk of change in value).

(vi) Investments made and dividends earned on them.

(vii) Insurance claims received against loss of stock or loss of profits.

(viii) Loans and advances given to subsidiaries and interest earned from them.

(ix) Issue of Bonus Shares.

(x) Term loan repaid.

You are required to classify the above activities in Cash Flow Statement as per 'AS-3'.

SOLUTION :

No.		Activities
(i)	Dividend paid for the year	Financing
(ii)	TDS on interest income earned on investments made	Investing
(iii)	Loans and advances given to suppliers and interest earned from them	Operating
(iv)	Deposit with bank for a term of two years	Investing

(v)	Highly liquid Marketable Securities (without risk of change in value)	Cash Equivalent
(vi)	Investments made and dividends earned on them	Investing
(vii)	Insurance claims received against loss of stock or loss of profits	Operating
(viii)	Loans and advances given to subsidiaries and interest earned from them	Investing
(ix)	Issue of Bonus Shares	No Cash Inflow/Cash outflow
(x)	Term Loan repaid	Financing

ACCOUNTING STANDARD:2

VALUATION OF INVENTORIES

QUESTION NO 1 (AUDIT PAPER 2009)

Grow More Private Limited a Wholesaler in Food and Other Agro Products has valued the year end Inventory of Net Realizable Value on the ground that AS-2 does not apply to inventory of Agriculture Products Comment.

SOLUTION

1. Principle: AS-2 does not apply to Producers Inventories of Livestock, Forest Product and Mineral Ores and Gases. These can be valued at Net Realizable value as per established practices.
2. Analysis and Conclusion:

   (a) However, the above principle does not apply in Trader's Inventory of Food and Agro Products. In the above case, Grow More Ltd. is only a Trader (Wholesaler) and not the producer. Hence, they cannot value their inventory at Net Realizable Value.

   (b) As AS-2, the Company should value the Inventory at lower of cost or Net Realisable Value. If the Management of M/s. Grow More Ltd. does not agree, the Auditor should qualify the Report.

QUESTION NO 2 (MAY 2006 4 MARKS)

Varada Ltd. purchased goods at the cost of ₹ 40 Lakhs in October. Till the end of the Financial year, 75% of the Stocks were sold. The Company wants to disclose Closing Stock at ₹ 10 Lakhs. The expected Sale value is ₹ 11 Lakhs and a commission at 10% on sale is payable to the Agent. What is the correct value of Closing Stock.

SOLUTION

Principle: Inventories are valued at – (a) Cost or (b) Net Realisable Value, whichever is lower.

Particulars	Amount (₹)
1. Cost Inventory (₹ 40 Lakhs x 25% Unsold)	10.00 Lakhs
2. NRV (Expected Sales Value ₹11 Lakhs Less cost to make the sale 10% ₹ 1.10 Lakh)	9.90 Lakhs
3. Value of Inventory under AS 2 = Least of the above	9.90 Lakhs

QUESTION NO 3

Gajanan Ltd. manufacturing garments and fancy terry towels has valued at the year end, its Closing Stock of Inventories of Finished Goods, (for which firm contracts have been received and goods are packed for export, but the ownership of which has not been transferred to the foreign buyers) at the Realisable Value inclusive of Profit and the export cash Incentives. Give your views on the above.

SOLUTION

1. General Principle: AS-2 requires that inventories should be valued at lower of cost and NRV. A departure from the general principle can be made if – (a) the AS is not applicable, or (b) having regard to the nature of industry say, plantations, inventories may be valued at market prices or price subsequently realized.
2. Special Items (Para 2) :AS-2 also states that Producers' Inventories of Livestock, Agriculture Crops, etc. are measured at NRV based on established practices if – (a) sale is assured under a Forward Contract or a Government Guarantee, or (b) where market is homogenous, and there is a negligible risk of failure to sell.
3. Analysis: In the given case the sale is assured under a Forward Contract but the goods are not of a nature covered by exceptions under Para 2. Hence, the Closing Stock of Finished Goods should have been valued at cost, as it is lower than the realizable value (as it includes profit). Also, Export Cash Incentives should not be included for valuation purposes.
4. Conclusion: Hence, the Company's policy of valuation is not correct.

QUESTION NO 4

State with reference to AS, how will you value the inventories in the following case. For kilogram of Finished Goods consisted of Material cost ₹ 100 per kg. Direct Labour Cost ₹ 20 per kg. and Direct Variable Production Overhead ₹10per kg. Fixed Production charges for the year on normal capacity of 1,00,000 kg. is ₹10 Lakhs. 2,000 kg. of Finished Goods are on stock at the year end.

SOLUTION

Computation of Value of stock (2000 kgs)

Particulars	₹
Direct Material (2,000 kgs. x ₹ 100 per kg.)	2,00,000
Direct Labour Cost (2,000 kgs. x ₹ 20 per kg.)	40,000
Direct Variable Production Overhed (2,000 kgs. x ₹10 per kg.)	20,000

Fixed Production Overheads (₹10 Lakhs x 2,000 Kgs) 1 Lakh Kgs.	20,000
Value of Closing Stock	2,80,000

QUESTION NO 5 (FIXED OVERHEADS)

Lambodar Ltd's normal production volume is 50,000 units and the Fixed Overheads are estimated at ₹ 5,00,000 Give the treatment of Fixed Production. OH under AS-2 if actual production during a period was – (a) 42,000 units (b) 50,000 units and (c) 60,000 units.

SOLUTION

Fixed Production OH Recovery Ratio (based on Normal Capacity) =

₹ 5,00,000 = ₹ 10 per unit.
50,000 units

The treatment of Fixed OH in different cases is as under:-

Particulars	Situation (a)	Situation (b)	Situation (c)
1. Normal Production	50,000 units	50,000 units	50,000 units
2. Actual Production	42,000 units	50,000 units	60,000 units
3. Difference in Production (1-2)	8,000 units (Short) Actual < Normal	Nil Actual = Normal	10,000 units (Excess) Actual > Normal
4. Recovery Rate to be used as per AS-2	Normal Rate = ₹10 per unit	Normal Rate = ₹ 10 per unit	Revised Rate = ₹500,000 60,000 units = ₹ 8.3 pu
5. Inventoriable Costs i.e. Recovered Costs	42,000 units = ₹10 = ₹4,20,000	50,000 units x ₹10 = ₹5,000,000	60,000 units x ₹ 8.33 = ₹ 5,00,000
6. Balance treated as Period Costs	₹ 80,000	Nil	Nil

QUESTION NO 6 (SALES AT SEPARATION POINT: JOINT COST)

Vaiabh Industries produces four Joint Products L,M, N and P from a joint process, incurring a cost of ₹ 571,200. Allocate the Joint Costs with the following information.

Particulars	L	M	N	P
Quantity Produced (in '000s)	10000 Kgs.	12000 Kgs.	14000 Kgs.	16000 Kgs.
Sales Price per Kg.	₹13	₹ 17	₹19	₹22
Stock Qty. at the end of year	1,625 Kgs.	400 Kgs.	Nil	1,550 Kgs.

Also determine the value of Closing Stock in respect of the above products.

SOLUTION

As per AS-2, costs of Joint Products should be apportioned on a rational and consistent basis

The Sales Value at Split off Point may be used for apportionment in the given case.

Particulars	L	M	N	P
1. Production Quantity	10000 Kgs.	12000 Kgs.	14000 Kgs.	16000 Kgs.
2. Sale Price per Kg	₹13	₹ 17	₹19	₹22
3. Total Sale Value (1x2)	₹130,000	₹2,04,000	₹2,66,000	₹3,52,000
4. Joint Costs apportioned (based on Sale value) (Based on 3)	₹ 78,000	₹ 1,22,400	₹159,600	₹2,11,200
5. Average Joint Costs per Kg. (4/1)	₹ 7.80	₹ 10.20	₹11.40	₹13.20
6. Closing Stock Qty. (given)	1,625 Kg.	400 Kg.	Nil	1,550 Kg.
7. Value of Closing Stock (5x6)	₹ 12,675	₹ 4,080	Nil	₹ 20,460

Note: It is presumed that the NRV of the products as at the Balance Sheet date are higher than the respective costs.

QUESTION NO 7 (TREATMENT OF BY PRODUCT)

In a manufacturing proves of Vijaya Limited, one by-product BP emerges besides two main products MP1 and MP2 apart from scrap. Details of Cost of production process is here under:-

Items	Units	Amount (₹)	Output (Unit)	Closing Stock on 31st March
Raw Material	15000	1,60,000	MP1-6,250	800
Wages	-	82,000	MP2-5,000	200
Fixed Overhead	-	58,000	BP-1,600	-
Variable Overhead	-	40,000	-	-

Average Market Price of MP1 and MP2 is ₹ 80 per unit and ₹ 50 per unit respectively. By-Product is sold at ₹ 25 per unit. There is a Profit of ₹ 5,000 on sale of By-Product after incurring Separate Processing Charges of ₹ 4,000 and Packing Charges of ₹ 6,000, ₹ 6,000 was realized from Sale of Scrap, Calculate the value of Closing Stock of MP1 and MP2 as on 31st March.

SOLUTION

1. Joint Cost = ₹1,60,000 + ₹ 82,000 + Rs 58,000 + ₹ 40,000
   = ₹3,40,000

2. Estimated NRV Charges of By Product = Final Sales value (-) Separate Processing Charges(-)Packing
   = (1,600 Units x ₹25(-)₹4,000 (-) ₹6,000 = ₹ 30,000

3. Net Joint Cost = Total Joint Cost (-) NRV of By Product (-) Proceeds from Sale of Scrap
   = ₹ 3,40,000 (-) ₹ 30,000 (-) ₹ 6,000 = ₹ 3,04,000

4. Value of Inventory:

Particulars	MP1	MP2
(a) Production Quantity	6,250 units	5,000 units
(b) Sale Value of Production Quantity	80x6250 = ₹ 5,00,000	50x5,000 = ₹ 2,50,000
(c) Joint Cost apportioned based on Sale value 2-1	₹ 2,02,667	₹ 1,01,333
(d) Average Joint Cost per unit (c/a)	₹ 32.43	₹ 20.60
(e) Closing Stock Units (given)	800 units	200 units
(f) Value of Closing Stock (dxe)	₹ 25,944	₹ 4,054

Note: It is assumed that Net Realisable Value is more than Cost.

QUESTION NO 8 (TREATMENT OF ABNORMAL LOSS)

Akshay Pharma Ltd. ordered 16,000 kg. of certain material at ₹ 160 per unit. The Purchase Price includes GST ₹ 10 per kg. in respect of which full GST Credit is admissible. Freight incurred amounted to ₹ 1,40,160. Normal Transit Loss is 2%. The Company actually received 15,500 kg. and consumed 13,600 kg. of Material. Compute the Cost of Inventory under AS-2 and the amount of Abnormal Loss.

SOLUTION

1. **Quantity Reconciliation:**

   Total Purchase Quantity = (given) = 16,000 kg.

   Normal Loss 2% on 16,000 = 320 kg.

   Balance Effective Quantity = 16,000(-) 320 = 15,680 kg.

   Actually Received (given) = 15,500 kg.

   Balance Abnormal Loss 15,680 (-) 15,500 = 180 kg.

   Consumption Quantity = (given) = 13,600 kg.

   Closing Stock (bal.fig) = 15500(-)13,600 = 1900 kg.

2. **Computation of Effective Cost per kg.**

Particulars	₹
Net Cost Per unit (excluding Excise Duty for which CENVAT Credit is available) = 160(-) 10 =	150
Total Purchase Cost for 16,000 kg. ordered Add: Freight Charges	24,00,000 1,40,000
Total Cost of Inventory	25,40,050
Effective Quantity (i.e. Gross Ordered Quantity Less Normal Loss) = 16,000 (-) 320 =	15,680
Effective Cost Per Kg. ₹ 25,40,160 15,680 Kg.	₹ 162.00

3. **Valuation of Inventory and Abnormal Loss**

Particulars	₹	Treatment
(a) Cost of Material Consumed = 13,600 Kg. at ₹162	22,03,200	Shown in Income Statement as Expense

(b) Cost of Abnormal Loss = 180 Kg. at ₹162	29,160	Shown in Income Statement as Expense/Loss
(c) Cost of Closing Stock = 1,900 Kg. at ₹162	3,07,800	Shown in Balance Sheet

QUESTION NO 9

In a production process, normal waste is 5% of input, 5,000 MT of input wee put in process resulting in a wastage of 3% MT. Cost per MT of input is ₹ 1,000. The entire quantity of waste is on stock at the year – end. State with reference to how you will value the inventories in the above case.

SOLUTION

1. Principle: Abnormal Amounts of Waste Materials, Labour or other Production Costs are excluded from cost of inventories and such costs are recognized as expenses in the period in which they are incurred.
2. Analysis and Conclusion: In this case, Normal Waste is 5% of 5000 MT = 250 MT and Abnormal Waste is 300 MT (-) 250 MT = 50 MT.
   (a) Cost of Normal Waste 250 MT will be absorbed and included in determining the cost of inventories (Finished Goods) at the year end.
   (b) Cost of Abnormal Waste = ₹ 50,000 (50 MT x ₹1,000) will be charged in the P&L Statement.

QUESTION NO 10 (INTEREST ON BANK OVERDRAFT)

Can PT Ltd. a Wire Netting Company, while valuing its Finished Stock at the year end include interest on Bank Overdraft as an element of cost, for the reason that Overdraft has been taken specifically for the purpose of financing Current Assets like Inventory and for meeting day to day working expenses?

SOLUTION

1. Nature of Interest: As per AS-2, "Interest and other Borrowing Costs are usually considered as not relating to bringing the inventories to their present location & condition, and hence usually, excluded in the cost of inventories".
2. Qualifying Assets: AS-16 identifies inventories which require a substantial period of time to bring them to a saleable condition as a Qualifying Assets, and permits capitalization of borrowing costs directly attributable to the asset as part of the Cost of the Asset.

3. Conclusion: In the given case, PI Ltd. can capitalize the interest cost on Bank Overdraft, only if its Inventories are is the nature of a Qualifying Asset as per AS-16. Otherwise, the entire amount will be treated as expense.

QUESTION NO 11 (REFER COST ACCOUNTS)

From the following data, find out value of Inventory as on 30th April using (a) LIFO Method, and (b) FIFO Method –

(a)	Purchased on 1st April	10 units at ₹ 70 per unit
(b)	Sold on 6th April	6 units at ₹ 90 per unit
(c)	Purchased on 9th April	20 units at ₹ 75 per unit
(d)	Sold on 18th April	14 units at ₹ 100 per unit

SOLUTION

1. Closing Stock (in Units) : 10 (-) 6 + 20 (-)14 = 10 units.
2. Valuation –

Value of Inventory under LIFO Basis	Value of Inventory under FIFO Basis
4 units from 1st April – 4 x ₹70 = ₹280	10 Units from 9th April – 10 x ₹75 = ₹750
6 units from 9th April – 6 x ₹75 =₹450	
Total Cost = ₹ 730	Total Cost = ₹ 750

QUESTION NO 12

In order to value the inventory of Finished Goods HR Ltd. has adopted the Standard

Cost of Raw Materials, Labour and Overheads. The Income Tax Officer wants to know the method, as per AS-2 for the valuation of Raw Material. Comment.

SOLUTION

1. The use of Standard Cost of Production has been suggested by AS-2 as a matter of convenience only. AS-2 suggests that Standard Cost system may be used for convenience if the results approximate the actual cost.
2. For Inventory Valuation, AS-2 recognises the use of absorption costing based on normal capacity. If the Company can adopt absorption costing for value of inventory, then the Standard Cost system need not be adopted.

QUESTION NO 13 (RETAIL VALUE METHOD)

HP is a leading distributor of Petrol. A detail Inventory of Petrol in hand is taken when the books are closed at the end of each month. At the end of the month, the following information is available.

Sales – ₹ 47,25,000, General Overheads Cost – ₹1,25,000, Inventory at beginning – 1,00,000 Litres at ₹ 15 per Litre.

Purchases: (a) June 1 Two Lakh Litres at 14.25 (b) June 30 One Lakh Litres at 15.15 (c) Closing Inventory 1.30 Lakh Litres Compute the following by the FIFO as per AS-2.

(a) Value of Inventory on June 30.

(b) Amount of Cost of goods sold for June.

(c) Profit/Loss for the month of June.

SOLUTION

1. Value of Inventory as on June 30:

Particulars	₹
0.30 Lakh Litres from June 1 Purchase Lot (0.30 Lakh Litres x ₹14.25 Per Litre)	4,27,500
1 Lakh Litres from June 30 Purchase Lot (1 Lakh Litres x ₹15.515 Litre)	15,15,000
Value of Inventory s on June 30	19,42,500

2. Cost of Goods Sold:

Particulars	₹
Opening Stock (1 Lakh Litres x ₹15)	15,00,000
Add: Purchases (2 Lakh Litres x ₹14.5) + (1 Lakh Litres x ₹15.15)	43,65,000
Less: Closing Stock	19,42,000
Cost of Gods Sold	39,22,500

3. Profit/Loss for June:

Sales (₹ 47,25,000) – Cost of Goods Sold (₹39,22,500) – General Overheads Cost (₹ 1,25,000) = Profit ₹ 6,77,500

QUESTION NO 14 (RETAIL VALUE)

Shri Ganesh operates a retail business. For a financial year, the following data is given -

Particulars	At Retail Price	At cost
Value of Opening Inventory	₹ 80,000	₹ 60,000
Value of Purchases	₹ 1,40,000	₹ 1,20,000

Calculate the cost of Closing Stocks, if the Sales made during the period is ₹2,00,000 (APPLY WEIGHTED AVERAGE METHOD)

SOLUTION

Value of Closing Inventory at Retail Prices	= Opening Stock + Purchases (-) Sales = ₹80,000 + ₹1,40,000 (-) ₹2,00,000 = ₹ 20,000
Average Percentage of Cost to Retail Prices	$= \frac{\text{Total Average Cost}}{\text{Total Average Retail Value}}$ $= \frac{60,000 + 1,20,000}{80,000 + 1,40,000}$ = 81.82%
Value of Closing Inventory at Cost Prices	= Retail values Less Margin of 18.18% = ₹20,000 (-) 18.18% thereon = ₹16,364.

QUESTION NO 15

Inventories of a Car Manufacturing Company include the value of items, required for the manufacture of a model, which was removed from the production line five years back, at Cost Price. As an Auditor, give your comments.

SOLUTION

1. AS-2 provides that the cost of inventories may not be recoverable if those inventories which are damaged, have become partially/fully obsolete, or if their selling prices have declined.
2. The Auditor should examine whether appropriate allowance has been made for the defective/obsolete/damaged inventories in determining the NRV. Having regard to this, NRV of inventory items, whichever was removed from the production line 5 years back, is likely to be much lower than the cost, as shown in the books of account. Thus, it becomes necessary to write down the inventories to NRV.

3. Since the Company has valued these inventories at cost, it has resulted in over statement of inventory and profits. Hence, the Auditor should qualify his report.

QUESTION NO 16 (SIMPLE VALUATION OF STOCK)

Best Ltd. deals in 5 products – P Q, R, S & T which are neither similar nor interchangeable. While closing its accounts for the year ending 31st March, the Historical Cost and NRV of the items of Closing Stock are determined as follows:-

Items	P	Q	R	S	T
Historical Cost (₹)	5,70,000	9,80,000	4,25,000	4,25,000	1,60,000
Net Realizale Value (₹)	4,75,000	10,32000	2,89,000	4,25,000	2,15,000

What is the Value of Closing Stock for the year ending 31st March as per AS-27.

Note: Refer Principle relating to item-by-item write-down given above.

SOLUTION

In the given case, since Inventories are not interchangeable, they are to be valued independently.

Item	Historical Cost (₹)	NRV (₹)	Valuation (₹) = Least of (2) or (3)
P	5,70,000	4,75,000	4,75,000
Q	9,80,000	10,32,000	9,80,000
R	3,16,000	2,89,000	2,89,000
S	4,25,000	4,25,000	4,25,000
T	1,60,000	2,15,000	1,60,000
			Inventory Value = 23,29,000

QUESTION NO 17

Closing Inventory at Cost of a Company amounted to ₹ 956,700. The following items were included at cost in the total –

(a) 350 Shirts, which had cost ₹ 380 each and normally sold for ₹ 750 each. Owing to a defect in manufacture, they were all sold after the Balance Sheet date at50% of their normal price. Selling expenses amounted to 5% of the proceeds.

(b) 700 Trousers, which had cost ₹ 520 each. These too were found to be defective. Selling expenses for the batch totaled ₹ 3800. They were sold for ₹ 950 each.

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

QUESTION NO 18 (VALUATION OF RAW MATERIAL)

A Raw Material costing ₹ 150 has Net Realisable Value (which can be the Replacement Cost) ₹130. The Finished Goods for which this Raw Material is used, has other cost to incur ₹60. At what Price should the Raw Material be valued, if Finished Goods has a Net Realizable Value – (1) ₹ 210 or above (2) less than ₹ 190

SOLUTION

Note: In all cases given above Cost of Finished Goods (RM at actuals 150+ Conversion 60) = ₹ 210.

1. SP ₹ 210 or above: If Sale Price is ₹ 210 or above the cost of FG can be recovered/realized fully. Hence, there is no need to write down RM Inventory to ₹ 130. So, Raw Material will be valued at ₹ 150.
2. SP less than ₹190: In this case, since cost of finished goods is not realizable fully, the Raw Material Inventory should be written down to Replacement Cost, i.e. ₹130

QUESTION NO 19 (VALUATION OF WIP)

On 31st March, a Business Firm finds that cost of a partly finished unit on that date is ₹530. The unit can be finished in its next financial year, by an additional expenditure of ₹ 310. The Finished Unit can be sold for ₹750 subject to payment of 4% brokerage on Selling Price The firm seeks your advice regarding -

(a) The amount at which the unfinished Unit should be valued as at 31st March for preparation of Final Accounts, and

(b) The desirability or otherwise of producing the Finished unit.

SOLUTION

Particulars	Amount
1. Estimated Net Realisable Value of Final Product = Sale value 750 less 4% Brokerage 30 less Further Processing Costs 310 = 750 – 30 – 310	410
2. Actual Cost incurred till date on the partly finished unit (including RM cost therein)	530

3. Since the entire actual cost of ₹530 is not recovered by use in finished production, the partly finished unit should be valued at its value in use, i.e. NRV ₹410. So Inventory should be written down by	530-410 =
4. Considering actual costs till date ₹530 + additional expected cost ₹ 310 it is not worthwhile to process this item further.	120

QUESTION NO 20 (VALUATION OF RAW MATERIAL)

Hari Ltd. purchased Raw Material at ₹ 400 per kg. The Company does not sell Raw Material but uses it in the production of Finished Goods. The Finished Gods in which Raw Material is used are expected to be sold at below cost. At the end of the accounting year, the Company is having 10,000 kg. of Raw Material in Stock as the Company never sells the Raw Material, does not know the Selling Price of Raw Material and hence cannot calculate the Realizable Value of the Raw Material for valuation of Inventories at the end of the year. However, Replacement cost of Raw Material is ₹300 per kg. How will you value the Inventory of Raw Material?

SOLUTION

Hind: Refer principle relating to RM valued at NRV given above.

Inventory should be valued at Replacement Cost of 10,000 Kgs. x ₹300 per Kg. = ₹ 30,00,000.

QUESTION NO 21

Himavan Pvt. Ltd. carries on the business of distribution of stationery goods on retail basis in a town area. It has obtained a dealership of toilet goods manufactured by a large manufacturing concern.

On account of keen competition from other Companies, this Company was forced to sell the goods with the consent of the Manufacturer, at 25% below the cost price of their goods. Almost about the end of the financial year, the Manufacturer has supplied to the Distributor Company, goods (free of cost), of such quantity and value so as to enable it to recover the loss of 25% and to leave an overall surplus of 10% on the total value of goods sold by the Distributor.

Before finalizing the accounts of the Distributor Company, the Directors seek your advice as to the price at which Closing Stock of goods should be valued as supplied by Manufacturer free of Cost, since the entire volume of stock has remained unsold.

QUESTION NO 22

Nidhi Ltd. purchased Raw Materials at a basic price of ₹ 10,000 on which GST of ₹ 1,500 is paid. Cost of Inventory (of Raw Materials at this stage would be ₹ 11,500). The material is thereafter processed. For this purpose, Conversion Costs (Labour and Direct Overheads, and other Fixed Production Overheads) amounting to ₹ 1,800 are incurred. Excise Duty Liability on Finished Goods amounting ₹1,700 is being paid by the Company. The Company is entitled for a GST credit of ₹ 1500. Compute the value of Inventory.

SOLUTION

1. Raw Materials: Since Materials have been fully consumed, there is no inventory as such. In case of Inventory Raw Material, it will be valued net of Excise Duty since the Company is entitled to CENVAT Credit thereon.
2. Finished Goods: Valuation of Finished Goods will be as under:-

Particulars	₹
Cost of Materials (net of GST, since GST Credit is available)	10,000
Cost of Conversion (given)	1,800
GST on Finished Product (given)	1,700
Total value of FG Inventory	13,500

QUESTION NO 23 (EMPTY BOTTLES)

Night Ltd. sells beer to customers. Some of the customers consume the beer in the bars run by Night Limited. While leaving the bars, the Consumers leave the empty bottles in the bars and the Company takes possession of these empty bottles. The Company has laid down a detailed internal record procedure for accounting for these empty bottles which are sold by the Company by calling for tenders. Keeping this in view:-

(a) Decide whether the Stock of Empty Bottles is an Asset of the Company.

(b) If so, whether the Stock of Empty Bottles existing as on the date of Balance Sheet is to be considered as Inventories of the Company and valued as per AS-2, or to be treated as scrap and shown at realizable value with corresponding credit to 'Other Income'?

SOLUTION

EAC Opinions – Stock of Empty Bottles – Nov. 07 – CA Journal Page 776

1. Asset: Where the enterprise takes possession of the empty bottles left behind by the customers at its bar, it constitutes an Asset for the enterprise, being a resource controlled by the Company as a result of past events from which future economic benefits are expected to flow to it.

2. Inventory: It is in the nature of Inventory, as it is consumed in the production process (i.e. primary packing of beer).
3. Conclusion: Since the bottles are acquired by the Company without incurring any cost, they (the total inventory) should be recorded at a Nominal Value of ₹ 1 which is the value at which they should figure in the Balance Sheet and should not be recognized as Income.

QUESTION NO 24

A Ltd. produces chemical, X which has following production cost per unit.

Raw Material = ₹ 5

Direct Labor = ₹ 2

Direct Expenses = ₹ 3

Normal capacity = 5,00 units per annum

Actual production = 4,000 units

Fixed Production Overhead =₹ 20,000 per annum.

The Company has 2,000 units of unsold stock lying with it at the end of year. You are required to value the closing Stock.

(Ans; ₹ 28,000)

QUESTION NO 25

The Company incurred ₹ 20,00,000 as fixed production overhead per year. It normally produces 1,00,000 units in a year. In 2009-10 how ever its production has been only 40,000 units. At the year end 31.3.2010 the closing stock was 10,000 units. The cost of unit is below:

Material	=	₹ 500 per unit
Labour	=	₹ 250 per unit
Fixed Production overhead	=	₹ 20,00,000 p.a.
Fixed administration	=	₹ 10,00,000 p.a.

Calculate the value of closing stock

(Ans:₹ 77,00,000)

QUESTION NO 26

The Company deals in three products X, Y and Z, which are neither similar nor interchangeable. at the time of closing of its account for the year 2001-2002. The historical cost and net realizable values of the items of closing stock are determined as below:

Items	Historical cost (₹ in Lakhs)	Net realizable value (₹ in Lakhs)
X	20	14
Y	16	16
Z	8	12
	44	42

What will be the value of closing Stock?
(Ans: ₹ 38)

QUESTION NO 27

Y Ltd. purchased 500 units of raw material @ ₹ 150 per unit gross less 10% Trade discount sales tax is chargeable @ 5% on the net price. The excise duty element on product is ₹ 12 per unit against which MODVAT can be claimed. The company spent ₹ 1,000 on transportation and ₹ 500 for loading and unloading Calculate the cost of purchase of raw material.

(Ans: ₹72,375)

QUESTION NO 28

XYZ Ltd produced 10,00,000 units of product A during 2009-10 per unit cost is as follows:

Raw Material	₹	100
Direct Wages	₹	50
Direct Expenses	₹	2
	₹	152

Production overhead is ₹ 20,00,000 of which 40% is fixed. The company sold 8,00,000 units and 2,00,000 units were in stock as on 31st March, 2010. Normal capacity is 5,00,000 units.

Calculate the value of closing stock

(Ans: ₹ 3.08 Crores)

QUESTION NO 29

Cost of Production of product X is given below:

Raw Material per unit	₹	120
Wages per unit	₹	80
Overhead per unit	₹	50
	₹	250

As on the balance sheet date the replacement cost of raw material is ₹ 110 per unit There were 1000 units of raw material on 31.3.2011.

Calculate the value of closing stock of raw material in following conditions.

(a) If finished product is sold at the rate of ₹275 per unit, what will be value of closing stock of raw material.

(b) If finished product is sold at the rate of ₹230 per unit, what will be value of closing stock of raw material.

(Ans: (a) ₹ 1,20,000 (b) ₹1,10,000)

QUESTION NO 30

Induga Ltd. imports raw materials of ₹ 10,00,000, which are kept in bonded warehouse till import duty on the same is paid. When the goods are ex-bonded, the duty is paid at the rate prevailing at that time. If goods are re-exported directly from bonded warehouse, no import duty is payable. On 31.3.2010 raw material of value of ₹ 5,00,000 was in the bonded warehouse. The rate of import duty was 10% of value of raw materials.

It is also noticed that where any goods remain in the bonded warehouse beyond a specified period, interest becomes payable on the duty for the period from the expiry of the specific period till the date of clearance of goods at the rate 2% of he custom duty payable. Raw materials lying on 31.3.2010 crossed the specified period by 100 days.

Calculate the value closing stock of raw material on 31.3.2010. Ans: ₹ 5,50,000

(NOTE: interest on duty is not a part of cost of inventory)

QUESTION NO 31

A company does not value it's W.I.P. because the quantity of work-in-progress cannot be determined accurately and in any case, there is not much variation between the opening and closing W.I.P. quantities. Comment on the above statement of the company.

Ans: Statement of company is not in accordance with AS-2.

QUESTION NO 32

A company is engaged in the manufacturing of organic chemicals Production of one intermediate product (say X) is in excess of its immediate requirement for captive consumption. Further factors are:

(i) X is not marketable and therefore, the market price is not known.

(ii) The estimated expenditure the further processing of X is ₹ 6000 per ton.

(iii) The company has been valuing the stock of X by theoretically converting it into equivalent units of finished products and then valuing the same on the principle of cost or net realizable value, whichever is lower.

Comments:

(a) Whether the present practice of valuating the X at the lower of cost and net realizable value of the end-product by theoretically converting it into equivalent finished product is in order.

(b) Whether the company can value at cost the stock X since X will have to undergo further processing to become marketable and net realizable value of X in its present form cannot be ascertained.

(c) If the answer of above (a) & (b) is negative, suggest the correct method for valuation of X. Ans: (a) NO

(b) NO – If net realizable after processing of X is ascertainable. (c) At cost

QUESTION NO 33 (NOV.2014 5 MARKS)

Capital Cables Ltd. has normal wastage of 4% in the production process. During the year 2013-14 the Company used 12,000 MT of Raw Material costing ₹150 per MT. At the end of the year 630 MT of Wastage was in Stock. The Accountant wants to know how this wastage is to be treated in the books. Explain in the context of AS-2 the treatment of Normal Loss and Abnormal Loss and also find out the amount of Abnormal Loss if any.

SOLUTION

1 Principle: Abnormal Amounts of Waste Material, Labour or other Production costs are excluded from cost of inventories and such costs are recognized as Expenses in the period in which they are incurred.

2 Analysis and Conclusion: Normal Waste is 4% of 12,000 MT = 480 MT & Abnormal Waste is 630 MT (-) 480 MT = 150MT.

(a) Cost of Normal Waste 480 MT wil be absorbed in the cost of Production and included in determining the Cost of Inventories (Finished Goods) at the year end.

(b) Cost of Abnormal Waste will be charged in the Profit and Loss Statement.

3. Computation

(a) Effective Material Cost of Output $= \frac{12{,}000\text{ MT} \times ₹150}{12{,}000\text{ MT} - 4\%\text{ Normal Waste}}$

$= \frac{18{,}00{,}000}{11{,}520}$

= ₹156.25 Per MT

(b) Cost of Abnormal Waste = 150 MT x ₹156.25 = ₹23,437.50

Alternatively, this may be taken at 150 MT x ₹150 = ₹22,500

QUESTION NO 34 (MAY 2014 5 MARKS)

Calculate the value of Raw Materials and Closing Stock based on the following information:

Particulars	Raw Material X	Particulars	Finished Goods Y
Closing Balance	500 Units	Closing Balance	1200 Units
Cost Price including GST	₹200 per unit	Material Consumed	₹220 per unit
GST Credit is receivable	₹10 per unit	Direct Labour	₹ 60 per unit
Freight Inward	₹20 per unit	Direct Overhead	₹ 40 per unit
Unloading Charges	₹10 per unit		
Replacement Cost	₹150 per unit		

Total Fixed Overhead for the year was ₹ 2,00,000, on normal capacity of 20,000 units.

Calculate the value of the Closing Stock when –

(i) Net Realizable Value of the Finished Goods Y is ₹400

(ii) Net Realizable Value of the Finished Goods Y is ₹300

SOLUTION

1. Principle:

   (a) Raw Materials and Supplies held for use in production are valued at cost. However, they can be valued below cost (i.e. NRV) in the following peculiar situations.

   - Sale below cost : When the Finished Products in which the Raw Material is incorporated, are expected to be sold below cost.
   - Price Decline: When there is a decline in the price of materials, and it is estimated that the cost of Finished Goods will be exceed NRV.

   (b) Finished Goods will be valued at Cost (or) Net Realisable Value, whichever is lower.

2. Valuation of Finished Goods Stock: In the given case the Valuation of FG Stock will be as under:-

   (a) Cost per unit of Finished Goods: (Material +Direct Labour + Direct Overhead + Fixed Production OH)

   $= 220 + 60 + 40 + \frac{2{,}00{,}000}{20{,}000} =$ ₹330 per unit

   (b) Valuation of FG will be –

Particulars	If NRV is rs.400 p.u.	If NRV is rs.300 p.u.
Value p.u. (Lower of cost ₹330 & NRV)	330	300
Total Value of Finished Goods Stock	₹330 x 1200 units = ₹3,96,000	₹300 x 1200 units = ₹3,60,00

3. Valuation of Raw Material Stock: In the given case, the Valuation of RM Stock will be as under:-

   (a) Cost p.u. of Raw Material:

Particulars	Cost p.u.
Purchase Price net of GST (since GST eligible for Credit) 200-10	190
Add: Freight Charges	20
Add: Unloading cost p.u.	10
Total Cost p.u.	220

(b) Total Value of Raw Material Closing Stock:

Particulars	Finished Goods of valued at Cost	Finished Goods of valued at NRV
* Raw Material cost p.u.	₹ 220	₹220
* Replacement cost p.u.	₹ 150	₹150
* Relevant Value p.u.	₹220 (since FG is valued at Cost)	₹ 150 (since FG is valued NRV)
* Total value for 500 units	500x ₹220 = ₹1,10,000	500x ₹150 = ₹ 75,000

Note: Replacement Cost of the Raw Material is assumed as its Net Realisable value.

QUESTION NO 35 NOV 2015 5 MARKS

In the books of Prashant Ltd., Closing Inventory as on 31stMarch2015 amount to ₹1,62,000 (on the basis of FIFO Method).

The Company decides to change from FIFO Method to Weighted Average Method for ascertaining the Cost of Inventory from the year 2014-15. On the basis of Weighted Average Method, Closing Inventory as on 31st March 2015 amounts to ₹ 1,47,000. Realisable Value of the Inventory as on 31st March 2015 amounts to ₹ 1,95,000.

Discuss the disclosure requirements of change in accounting policy as per AS-1.

SOLUTION

1. Principle: Change in an Accounting Policy should be disclosed -
   (a) When such change has a material effect in the current period, and
   (b) When such change is reasonably expected to have a material effect in later Periods.
2. Analysis and Conclusion: Due to the change in valuation of Inventory from FIFO to Weighted Average Method, the Inventory has been valued at ₹ 147,000, which is lower by ₹ 16,000 than the old method (₹ 1, 63,000). Consequently, the Profit is lower by ₹ 16,000. Hence the change in Accounting Policy should be disclosed in Notes to Accounts.

QUESTION NO 36 MAY 2015 5 MARKS

Mr. Mehul gives the following information relating to items forming part of inventory as on 31.03.2015. His Factory produces Product X using Raw Material A.

1. 600 units of Raw Material A (Purchased at ₹120). Replacement Cost of Raw Material A as on 31.03.2015 is ₹ 90 per unit.
2. 500 units of Partly Finished Goods in the process of producing X and Cost incurred till date ₹260 per unit. These units can be finished next year by incurring Additional Cost of ₹ 60 per unit.
3. 1,500 units of Finished Product X and Total Cost incurred ₹ 320 per unit. Expected Selling price of Product X is ₹ 300 per unit.

Determine how each item of inventory will be valued on 31.03.2015. Calculate the Value of Total Inventory as on 31.03.2015.

SOLUTION

Item	**Valuation Principle**	**Result**
Raw Material	Since the Finished Product using this Raw Material is expectable be sold below cost, Raw Material may be valued of NRV, i.e. Replacement cost of ₹90.	600 x ₹90 = ₹ 54000
WIP	• Cost ₹ 260 • Estimated NRV = Sale Price ₹300 – Cost to Complete ₹60 = ₹240 • Hence, valued at least of the above, i.e. ₹240 p.u.	500 x ₹240 = ₹1,20,000
Finished Goods	Cost ₹320 or Net Realisable Value ₹300, whichever is lower. Hence valued at ₹300 p.u.	1500 x ₹300 = ₹ 4,50,000
	Total	₹ 6,24,000

QUESTION NO 37 MAY 2015 FINAL 5MARKS

From the following information, value the Inventories as on 31st March, 2015.

Raw Material has been purchased at ₹125 per Kg. Prices of Raw Material are on the decline. The Finished Goods being manufactured with the Raw Material is also being sold at below Cost. The Stock of Raw Material is of 15,000kg. and the Replacement Cost of Raw Material is ₹100 Per Kg.

Cost of Finished Goods per Kg. is as under:-

Particulars	₹ per Kg.
Material cost	125
Direct Labour Cost	20
Direct Variable Production Overhead	10

Fixed Production Overhead for the year for a normal capacity of 1,00,000 kgs. of production is rs.10 Lakhs. At the year end, there were 2,000 Kgs. of Finished Goods in stock. Net Realisabale value of Finished gods is rs.140 Per Kg.

SOLUTION

1. Conversion Cost Per Kg. of Finished Product

= Direct Labour + Direct Variable Production OH + Fixed Production OH

$= ₹\ 20 + ₹\ 10 + \frac{₹\ 10\ \text{Lakhs}}{1\ \text{Lakh Kgs.}} = ₹\ 40$ Per Kg.

2. Inventory Valuation is as under: - (A) For Finished Goods

(a)	Cost per Kg. for Finished Product = Material + Conversion	125+40 = ₹ 165 Per Kg.
(b)	Net Realizable value of Finished Product if sold after Conversion	Given = ₹ 140 per kg.
(c)	Hence, Valuation Rate for finished goods = (a) or (b), whichever is lower.	₹140 Per kg.
(d)	Value of Inventory 2,000 kg. of Finished Product	2,000 Kg. x ₹140 = ₹2,80,000

(B) For Raw Materials

(a)	Cost of Raw Material	Given = ₹ 125 Per kg.
(b)	Replacement Cost of Material, i.e. Sale without Conversion	Given = ₹100 Per Kg.
(c)	Valuation Rate for Raw Material (i.e. least o Cost or NRV, least of (a) and (b)	₹ 100 per Kg.
(d)	Value of Inventory 15,000 kg. of Raw Material	15,000 kgs x ₹100 = ₹15,00,000

Note: When the Finished Products in which the Raw Material is incorporated, are expected to be sold below Cot (NRV rs.140 Vs. Cost ₹165), it is preferable to sell the product without Conversion. In such case, the Raw Materials will be valued below cost, i.e. at NRV, being the Replacement cost.

QUESTION 39

JATIN Ltd. purchased *raw* materials for 1,25,000 less a rebate of 2%. It paid 25,000 as import duty, including ₹ 10,000 towards a special duty. According to local tax laws, it will get a credit of the amount paid towards the special duty, while determining its customs liability. It spent ₹ 8,000 on ocean freight, clearing agent's charges of 2,000, 4,000 on warehouse rent and 1,500 on the watchman's salary.

QUESTION 40

Per kg. of finished goods consisted of:

Material cost	Rs 100 per kg.
Direct labour cost	20 per kg.
Direct variable production overhead	10 per kg.

Fixed production charges for the year on normal capacity of one lakh kg. is 10 lakhs. 2,000 kg. of finished goods are on stock at the year end. Calculate value of inventories.

(Nov. 2000 - 4 Marks)

QUESTION 41

Total Unit	: 10,000 (closing stock)
Contract sales	: 6,000 units
Normal units	: 4,000 units
Cost per unit	: 150
Contract selling price	: 200
Market Price	: 90

QUESTION 42 (NOV 2002:3MARKS)

Inventories of a Car manufacturing company include the value of items, required for the manufacture of model which was removed from the production line five years back, at cost price. As an Auditor Comment.

SOLUTION

(1) Provision of AS 2

The cost of inventories may not be recoverable if those inventories are damaged, have become wholly or partially obsolete, or if their selling prices have declined. Accordingly, the auditor should examine whether appropriate allowance has been made for the defective, damaged, obsolete and slow-moving inventories in determining the net realizable value.

(ii) Analysis and Conclusion

In this case, items required be the manufacture of a model which has been withdrawn from the production line five veal's ago are included in the stock at cost price resulting in overstatement of inventory and profit. As it appears from the facts given that the net realizable value of these items is likely to much lower than the cost at which these are being shown in the books of account. Accordingly, it becomes necessary to write down the inventory to 'net realizable value' if the items of inventories become wholly or partially obsolete. Under the circumstance, the auditor should qualify the report appropriately.

QUESTION 43 *(NOV. 1995)*

The company deals in purchase and sale of timber and has included notional interest charges (calculated on the paid-up share capital and free reserves) in the value of stock of timber as at the Balance Sheet date as part of cost of holding the timber.

SOLUTION

1) Provision of AS 2

An item of expenditure will be included in the cost of inventories, if it has been incurred in bringing the inventories to their present condition and location. An expenditure can't be included in the valuation of closing stock if it has not been actually incurred. In other words, notional expenses are excluded from inventory valuation.

2) Analysis and Conclusion

Thus, in the present cases, inclusion of notional interest in valuing the closing stock of timber can't considered to be fair, reasonable or in conformity with GAAP. As an auditor, we need to ensure that the basis of valuation of inventory is clearly stated in the form of a note. We also need to ensure that the basis of valuation is followed consistently.

QUESTION 44

The management tells you that the WIP is not valued since it is difficult to ascertain the same, in view of the multiple processes involved and in any case, the value of opening and closing WIP would be more or less the same. Advise.

SOLUTION

(i) Provision of AS 2 (May 2001)

Inventory includes raw material, work-in-progress and finished goods and should be valued at cost or NRV whichever is lower.

(ii) Analysis and Conclusion

In this case work-in-progress is also a component of inventory and should be valued at cost or NRV whichever is lower.

QUESTION 45

CC Ltd. a Pharmaceutical Company, while valuing its finished stock at the year end wants to include interest on Bank Overdraft as an element of cost, for the Reason that overdraft has been taken specifically for the purpose of financing curl-cut assets like inventory and for meeting day to day working expenses.

SOLUTION

(i) Provision of AS 2

Cost of inventories comprises all costs of purchase, costs of conversion and other costs incurred in bringing the inventories to their present location and condition. However, it makes clear that interest and othet- borrowing costs are usually not included in the cost of inventories because generally such costs at-c not related in bringing the inventories to their present location and condition.

(ii) Conclusion

Therefore, the proposal of CC Ltd. to include interest on bank overdraft as an element of cost is not acceptable because it does not form part of cost of production.

QUESTION 46 (RTP MAY, 2012)

A company is engaged in the manufacture of electronic products and systems. As per Chief Accountant a prototype system was installed at one of the customer's locations in June 2010 for getting acceptance on the performance of the system. The Chief Accountant has stated that as the ownership of the system installed for field trials was vested with the company, for accounting & control purposes, the prototype system installed at customer's location in 2010 was capitalised in the accounts for the year 20 10-1 1 at its bought-out cost. State whether the accounting treatment adopted by the company is correct or not?

SOLUTION:

(i) Provision of AS 2

inventories mean assets held for sale in the ordinary course of business, or in the process of production for such sale, or for consumption in the production of goods or services for sale, including maintenance supplies and consumable other than machinery spares.

(ii) Provision of AS 10

Fixed asset is an asset held with the intention of being used for the purpose of producing or providing goods or services and is not held for sale in the normal course of business.

(iii) Analysis and Conclusion

Accordingly, the system installed by the company at customer's site for his acceptance, based on the field trials of the system, is an item of inventory, it is not a fixed assets. installation of such prototype system at customer's sites for their acceptance is akin to sale of goods on approval basis. Therefore, the capitalization of such prototype system at its bought out cost is not correct.

QUESTION 47

(Study Material) A Ltd. purchased 1,00,000 MT for 100 each MT of raw material and introduced in the production process to get 85,000 MT as output. Normal wastage is 15%. In the process, company incurred the following expenses:

Direct Labour	10,00,000
Direct Variable Overheads	1,00,000
Direct Fixed Overheads	1,00,000
(including interest 40,625)	

On the above 80,000 MT was sold during the year and remaining 5,000 MT remained in closing stock. Due to fall in demand iii market the selling price for the finished goods on the closing day was estimated to be 105 per MT. Calculate the value of closing stock.

QUESTION 48

(Study Material) Ambica Stores is a departmental store, which sell goods on retail basis. It makes a gross profit of 20% on net sales. The following figures for the year-end are available:

Opening Stock	₹50,000
Purchases	₹3,60,000
Purchases Returns	₹10,000
Freight Inwards	₹10,000
Gross Sales	₹4,50,000
Sales Returns	₹11,250
Carriage Outwards	Rs 5,000

Compute the estimated cost of the inventory on the closing date.

SOLUTION.

Calculation of Cost for Closing Stock

Particulars	**Rs**
Opening Stock	50,000
Purchase less return (3,60,000-10,000)	3,50,000
Freight Inwards	10,000
	4,10,000
Less:COGS (4,50,000 -11,250) – profit @ 20%	3,51,000
Closing Stock	59,000

QUESTION 49 (STUDY MATERIAL)

Particular	**Kg.**	**Rs**
Opening Stock: Finished Goods	**1,000**	25,000
Raw Materials	**1,100**	11,000
Purchase	**10,000**	1,00,000
Labour		76,500
Overhead (Fixed)		75,000
Particular	**Kg.**	**Rs**
Sales	10,000	2,80,000
Closing Stock: Raw Materials	900	
Finished Goods	1,200	

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 20 per kg. and the replacement cost for the raw metatarsal was 9.50 per kg. n the closing day. You are required to calculate the closing stock as on that *date.*

SOLUTION

(i) Calculation of Cost per Unit

Particulars	Rs
Raw Material consumed (1100+10000-900) @10 per unit	1,02,000
Director Labour	76,500
Fixed Overhead $\frac{(75{,}000 \times 10{,}200)}{15{,}000}$	51,000
Cost of production	2,29,500
Cost of closing stock per unit (2,29,500 ÷ 10,200)	22.50

(ii) Conclusion

Since NRV is lower than cost hence Finished goods is valued at 20 *i.e.* NRV and raw material is valued at replacement cost *i.e.* 9.5.

Finished Goods (1,200 X 20)	24,000
Raw Materials (900 X 9.50)	8,550
	32,550

QUESTION 50 (STUDY MATERIAL)

The closing inventory at cost of a company amounted to 2,84,700. The following items were included at cost in the total:

(a) 400 coats, which had cost 80 each and normally sold for 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 20 each. These too were found to be defective. Remedial work in April cost 5 per skirt, and selling expenses for the batch totalled 800. They were sold for 28 each.

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

SOLUTION

Valuation of Closing Stock

Particulars	Rs	Rs
Closing Stock at Cost		2,84,700
Less: Cost of 400 coats (400x 80)	32,000	
Less: Net Realisable Value (400 X 75) - 5%	(28,500)	(3,500)
Value of closing Stock		**2,81,200**

NOTE: THERE IS NO LOSS ON SKIRTS DUE TO WHICH WE HAVE NOT CONSIDERED ANY DECLINE.

QUESTION 51 (MAY 2013) 4 MARKS

On 31St March, 2013 a business firm finds that cost of a partly finished unit on that date is 530. The unit can be finished in 2013-14 by an additional expenditure of 310. The finished unit can be sold for 750 subject to payment of 4% brokerage on selling price. The firm seeks your advice regarding:

(i) The amount at which the unfinished unit should be valued as at 31st March, 2013 for preparation of final accounts and

(ii) The desirability or otherwise of producing -the finished unit.

(May, 2010 & 2013-4 Marks)

SOLUTION

(i) Statement showing value at which unfinished unit should be presented in final account:

Cost of partial processed goods	530
NRV {(750-4%)-310}	410
Whichever Is lower	410

(ii) **Desirability of producing finished unit**

On the basis of above calculation, it can be said production should not be continued due to loss on goods manufactured.

QUESTION 52 (MAY 2011)

Best Ltd. deals in Five Products - P, Q, R, Sand T which are neither similar nor interchangeable. At the time of closing of its Accounts for the year ending 31st March 2011, the Historical Cost and Net Realizable Value of the items of the Closing Stock are determined as follows :-

Items	Historical Cost (R)	Net Realizable Value (R)
P	5,70,000	4,75,000
Q	9,80,000	10,32,000
R	3,16,000	2,89,000
S	4,25,000	4,25,000
T	1,60,000	2,15,000

What will be the Value of Closing Stock for the year ending 31St March 2011 as per AS-2 "Valuation of Inventories"?

SOLUTION

Statement of Valuation of Inventory

Particulars	Rs
Item P	4,75,000
Item Q	9,80,000
Item R	2,89,000
Item S	4,25,000
Item-T	1,60,000
Total	**23,29,000**

QUESTION 53

XY Ltd. was making provisions for non-moving stocks based on no issues for the last L2 months upto 31.3.11. Based on technical evaluation the company wants to make provisions during year 3 1.3.12.

Total value of stock - 100 lakhs.

Provisions required based on 12 months issue 3.5 Iakhs

Provisions required based on technical evaluation ' 2.5 lakhs.

Does this amount to change in accounting policy ? Can the company change the method of provision? *(Nov., 2009, May 2003 & 2012 - 4 Marks)*

SOLUTION

(i) Provision of AS

The decision of making provisions for non-moving stocks 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 stocks should be made. The method of estimating the amount of provision may be changed in case a more prudent estimate can !ie made.

(ii) Analysis and Conclusion

In the given case, considering the total value of stock, the change in the amount of required provision of non-moving stock from ₹ 3.5 lakhs to 2.5 Iakhs is 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 2011-12.

“The company has provided for non-moving stocks 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 higher by Rs 1 Lakh.

QUESTION NO 54 (NOV 2012) (4MARKS)

“ In determining the cost of inventories, it is appropriate to exclude certain costs and recognize them as expenses in the period in which they are incurred. “ provide example of such costs as per AS-2: Valuation of Inventories.

SOLUTION

“In determining the cost of inventories, it is appropriate to exclude certain cost and recognize them as expenses in the period in which they are incurred. “ Provide example of such costs as per AS-2: valuation of Inventories.]

Answer: As per Paragraph 13 of Accounting standards-2, “Valuation of Inventories” in determining the cost of inventories, it is appropriate to exclude following costs and recognize them as expenses in the period in which they are incurred:

(a) Abnormal amounts of wasted materials, labour, or other production cost:

(b) Storage cost, unless the production process requires such storage,

(c) Administrative overheads that do not contribute to bringing the inventories to their present location and condition.

(d) Selling and distribution cost:

QUESTION 55 (CA INTER NOV 2019) (5MARKS)

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

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

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

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

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

SOLUTION:

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

Hence the valuation will be done as under:

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

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

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

Valuation of Total Inventory as on 31.03.2019:

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

*It has been assumed that the partly finished unit cannot be sold in semi-finished form and its NRV is zero without processing it further.

QUESTION 56 (CA INTER JAN 21) (5 MARKS)

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

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

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

(iii) 800 units of Finished goods P and total cost incurred is ₹ 295 per unit.

Expected selling price of product P is ₹280 per unit, subject to a payment of 5% brokerage on selling price.

Determine how each item of inventory will be valued as on 31.03.2019. Also calculate the value of total Inventory as on 31.03.2019.

SOLUTION

As per AS 2 (Revised) "Valuation of Inventories", materials and other supplies held for use in the production of inventories are not written down below cost if the finished products in which they will be incorporated are expected to be sold at cost or above cost. However, when there has been a decline in the price of materials and it is estimated that the cost of the finished products will exceed net realizable value, the materials are written down to net realizable value. In such circumstances, the replacement cost of the materials may be the best available measure of their net realizable value. In the given case, selling price of product P is ₹ 266 and total cost per unit for production is ₹ 295.

Hence the valuation will be done as under:

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

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

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

Valuation of Total Inventory as on 31.03.2019:

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

QUESTION 57 (CA INTER JULY 21) (5 MARKS)

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

Particulars	Units	Amount (₹)
Opening Inventory:		
Finished Goods	2,000	1,00,000
Raw Materials	2,200	44,000
Direct Labour		3,06,000
Fixed Overheads		3,00,000
Sales	20,000	11,20,000
Closing Inventory:		
Finished Goods	2,400	
Raw Materials	1,800	

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

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

SOLUTION

Statement Showing the Computation of Value of Closing Inventory

Value of Closing Finished Goods

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

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

Value of Closing Raw Materials

As NRV of finished goods is less than its cost, the relevant raw material will be valued at its replacement cost, which is the best available measure of its NRV i.e. @ ₹ 19 per kg.

Therefore, value of closing inventory would be as under:

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

Working Note:

Calculation of raw material consumed during the year

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

QUESTION 58 (CA INTER MAY 2022 EXAMS: 5 MARKS)

SM Enterprises is a leading distributor of petrol. A detailed inventory of petrol in hand is taken when the books are closed at the end of each month. For the month ending on June 2021 following information is available:

(i) Sales for the month of June 2021 was ₹ 30,40,000.

(ii) General overheads cost ₹ 4,00,000.

(iii) Inventory at beginning 10,000 litres @ ₹ 92 per litre.

(iv) Purchases-June 1, 2021, 20,000 litres @ ₹ 90 per litre, June 30, 2021, 10,000 litres @ ₹ 95 per litre.

(v) Closing inventory 13,000 litres.

You are required to compute the following by FIFO method as per AS 2:

(i) Value of Inventory on 30th June, 2021.

(ii) Amount of cost of goods sold for June,2021.

(iii) Profit/Loss for the month of June,2021.

SOLUTION :

	₹
Cost of closing inventory for 13,000 litres as on 30th June 2021	
10,000 litres @ ₹ 95	9,50,000
3,000 litres @ ₹ 90	2,70,000
Value of inventory (determined at cost in absence of NRV)	12,20,000
Calculation of cost of goods sold	
Opening inventories (10,000 litres @ ₹ 92)	9,20,000
Purchases June – 1 (20,000 litres @ ₹ 90)	18,00,000
June – 30 (10,000 litres @ ₹ 95)	9,50,000
	36,70,000
Less: Closing inventories	(12,20,000)
Cost of Goods Sold	24,50,000
Calculation of Profit	
Sales (Given) (A)	30,40,000
Cost of Goods Sold	24,50,000

Add: General Overheads	4,00,000
Total Cost (B)	28,50,000
Profit (A-B)	1,90,000

QUESTION 59 (CA INTER NOV. 2022 EXAMS : 5 MARKS)

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).

NOTES

ACCOUNTING STANDARD: 17
SEGMENT REPORTING

SCOPE AND OBJECTIVE

Nowadays a company cannot survive running with single product. Diversification is a necessity in today's market, to secure itself from the attacks and counter attacks of the competitors on any product. Specially in a multi product company or a company operating in different geographical areas traditional method of financial disclosures to the shareholders could not depict the complete picture regarding the risk and returns. Hence, there arises a need for segmental reporting.

The significance of Segment Reporting is as under:

- Evaluation and understanding of the overall performance of the Company.
- Identification of loss making and profit making units.
- How various products/various areas are exposed to various risk and returns.
- To effectively assess the underlying risks and returns of an enterprises and make more informed decisions relating to the enterprise.
- To know the return on Capital employed for a segment.
- The shareholders can make correct decisions based on the segmental performance reported to them.

Types of segments

i) Business Segment:

If a company is dealing in various products/services having different risk-return profile then we say that the enterprise is having Business segments. A BS is a distinguishable component of an enterprise that is engaged in providing an individual product or service or a group of related products or services and that is subjected to risks and returns that are different from those of other business segments. A coaching classes is running 3 divisions Commerce, Science and School. Risk and returns of individual division might be different. This is an example of Business Segment.

Factors to be considered for BS:

i) Nature of product ii) Different process involved iii) Type or class of customers, iv) Methods of distribution, v) Nature of regularity environment (laws, regulations).

Meaning of Risks and rewards:

If a segment includes two products having different risks and rewards factors then they are two different segments. For Example: Risk and rewards profile of doing Broking business is different compared to trading on one's own account; therefore they fail under two different segments.

The two factors are very important in the context of interpreting 'risks and rewards' under AS-17 for defining BS. The word significant which is added before the term risks and rewards is very important. The risk and reward of doing business in jeans would not be significantly different compared to doing business in shirts. Also manufacturing chairs and tables carry similar risks and returns. If we take the example of hair oil and cooking oil, they would fall under two different segments, because their nature is different, the production process is different, the customers are different, channels are different.

ii) **Geographical Segment:**

If a Company is providing products/services catering geographically exposed to different risk and returns then it is a Geographical segment. Again Geographical Segment is divided as per Location of Assets and Location of Customers.

Geographical Segment can be within a region or within a city, within a country or scattered in different countries.

Factors to be considered for GS:

(i) Economic and political conditions, (ii) Proximity between operations (iii) Special risks involved. (iv) Currency risks (v) Exchange control risks.

Advantage of having geographical segment:

Shehnaaz Global products has been in the business of beauty products. The products were sold in Asia, London and France. Previously the business was doing well. However, in the last three years there has been a decline in the profitability of the company. The Company is not able to know the exact reason for the decline in the profitability because the company use to prepare a consolidate income statement (combining all the locations). After preparing segment wise profit and loss statement, the company came to know that the sales in France was declining in the last few years. Now the company can take corrective actions based on this information.

SOME DEFINITIONS

i) **Reportable Segment:** An enterprise may be engaged in 'n' number of products/areas. But only some of the segments need to be compulsorily disclosed in the financial statements. Such mandatory disclosed segments are known as Reportable Segment.

ii) **Segment Revenues:** If represents revenue of a particular segment.

Segment Revenue = (Direct revenues from outside customers + Inter segment sales + Allocated income). As segment revenue includes allocable income the basis for sharing common income between the segments can be agreed between the segments, internal MIS, transfer-pricing policy.

What about other income: Other income should be included as a part of segment revenue if they do not fall under the exclusion definition (discussed below) and if it is essentially operating in nature. For Example: Export incentives are price subsidies for achieving exports which is indirectly a component of export turnover and should be included in segment revenue. Some times segment assets are idle, and these may be used to earn rentals. Such income would be operating income and consequently form part of segment revenue.

Exclusions: (i) Income like interest, dividend earned unless the operations of the segment are primarily of a financial nature; (ii) Gains on sale of investments; (iii) Extraordinary items.

iii) **Enterprise Revenues:**

Enterprise Revenue = Revenues from eternal customers only as reported in profit and loss account.

iv) **Segment Expenses:** It represents expenses of a particular segment.

Segment Expenditure =(Direct expenses related to the unit + Expenses incurred on dealing with other department +Allocated expenses). It excludes (i) interest expense, (ii) Capital loss on Sale of Investments, (iii) Corporate expenses like selling and distribution expenses, office expenses (iv) Tax expenses (v) Extraordinary items.

Why interest is not included in segment expenses: As per ASI-22, interest expense relating to overdrafts/other borrowings identified to a particular segment should not be included as a part of segment expense unless the operations of the segment is of financial nature or unless interest is included as a part of cost of inventories as per AS-16. Segment results are net of operating results rather than net of financing.

v) **Segment Result:** (Segment Revenue – Segment Expenses)

vi) **Segment Assets:** Segment's own assets used for its operating activities + Allocable assets including allocable Goodwill. For Example: Milk powder purchased to make chocolates is a segment asset if not consumed before the reporting period for the Dairy product segment. Segment revenue generally includes debtors, inventories, advances, fixed assets.

> If item of expense (say depreciation) is included in P&L A/c. for a particular segment, then the corresponding asset will also go to that segment assets head.

vii) **Segment Liabilities:** Segment's own operating liabilities + Share of Common liabilities. It excludes; (i) Provision for Taxes (ii) Liabilities incurred at Head Office level for general purpose.

vii) **Segment Accounting Policies:** AS-1 prescribes accounting policies at the total company level as a whole. But segment accounting policies are specific accounting policies for the concerned segment to be reported. Even accounting policies at the enterprise level may be passed on (allocated to) the segment. For ex. If all the segments use one particular Asset commonly then, depreciation charged on the enterprise level will be allocated to different segments.

Examples of segment policies:

Policies relating to (i) Basis of allocation of revenues/expenses between segments, (ii) Transfer pricing policies.

Identification of Segments:

Identification of Segments mostly depends upon the Organizational and Management structure. The internal financial reporting to the BOD and CEO provides the best evidence for the basis of identification of segments.

Deciding between Primary or Secondary Segments

If an enterprise has both business as well as geographical segment then the question arises as to which is primary and which is secondary segment. This is because the intensity of disclosures being low for secondary segments and high in the case of primary segments. Following points are worth noting for such differentiation:

1) Largely it depends upon the information provided by the internal financial reporting to the BOD and CEO.

2) The important factor for differentiation is "dominant source and nature of risks and return".

3) If risks and returns of enterprises are largely affected by the products and services then business segment will be the primary reporting segment. Here business segment is the dominant factor.

4) If risks and returns of an enterprise are largely affected by the operations in different areas then geographical segment will be the primary reporting segment Here geographical segment is the dominant factor.

5) If suppose the risks and returns of both the business as well as geographical segment is equally dominant then business segment will be primary segment.

However, if confusion arises as to differentiation between primary and secondary segment, one has to undertake the facts and circumstances of the case. Ultimately the financial disclosure should depict true and fair view.

Segment in CFS

There is no such rule that a subsidiary company would constitute a reportable segment. Segments reportable in the stand-alone financial statements may not be reported at the CFS level. If there are similar segments in parent and subsidiary then they are treated as one segment for CFS purpose. Example: If HO and Subsidiary have a common segment say FMCG, then they are merged of the CFS level.

Reportable Segments

An enterprise may be engaged in 'n' number of products/areas. But only some of the segments need to be compulsorily disclosed in the financial statements. Such mandatory disclosed segments are known as Reportable Segment.

However following are the tests applied to decide the Reportable Segment:

Test 1: REVENUE TEST

As per Revenue test Reportable Segment is :

Segment Revenue > 10% (Total Revenue of all segments)

Test 2 : RESULT TEST

As per Revenue test Reportable Segment is :

Segment Result > 10% of Higher of (Total Results of profitable segments OR Total Results of loss making segments) Loss making segments will be considered in absolute terms.

Test 3: ASSETS TEST

As per Revenue test Reportable Segment is :

Segment Assets > 10% (Total Segment Assets)

ADDITIONAL CONDITIONS TO BE CONSIDERED

(1) 75% TEST

As per 75% test Reportable Segment is :

If External Revenue of Reportable Segments < 75% (Enterprise Revenue), then

Add more and more segments such that:

External Revenue of Reportable Segments > 75% (Enterprise Revenue)

(2) MANAGEMENTS CHOICE:

As per Management Test Reportable Segment is :

If any of the above tests are not satisfied then management at its discretion choose Reportable Segment.

(3) If 'X' is a Reportable Segment last year, then 'X' will continue to be a Reportable Segment every year irrespective of the above tests gets satisfied or not.

What about Non-Reportable Segments?

Non-Reportable Segments are not reported as such but they are shown as reconciling segments.

- Disclosure Requirements

  Two styles of formats are required for reporting purposes:

Primary Reporting Format

Every enterprises has to report the following as Primary Reporting:

1) Revenue items:

a) Revenues from external customers b) Inter-segment Revenues. c) Depreciation/ impairments/amortizations d) Non-cash expenses other than 'c' above e) Segment Results.

2) Balance Sheet Items:

a) Total Carrying amounts of Segment assets b) Total amounts of Segment Liabilities c) Tangible and Intangible assets acquired.

3) Other Items:

a) Reconciliation between (Different Segments Vs. Whole Enterprise's) of Segment Revenues/Results/Assets/Liabilities.

Secondary Reporting Format

(i) If Business Segment is Primary Segment: Then Geographical segment will be Secondary. Following is to be reported by the Secondary Segments:

- Segment Revenues form external customers of geographical segment of only those segments who's External Revenues is 10% > Total Enterprises Revenues.
- Carrying amount of segment assets, of those segment assets whose assets > total assets of geographical segments.
- Tangible and intangible assets acquired.

(ii) If Geographical Segment is Primary Segment: Then Business will be Secondary. Following is to be reported by the Secondary Segments.

- Segment Revenues from external customers of business segment of only those segments whose External Revenue is 10% > Total Enterprises Revenues.
- Carrying amount of segment assets, of those segment assets whose assets is 10 > total assets of business segments.
- Tangible and Intangible assets acquired.

(iii) If Geographical Segment based on location of assets is Primary Segment: Then Geographical Segment based on location of customers will be Secondary.

Following is to be reported by the Secondary Segments:

- Segment Revenues from external customers of business segment of only those segments who's External Revenues is 10% > Total Enterprises Revenues.

(iv) If Geographical Segment based on location of customers is Primary Segment: Then Geographical Segment based on location of assets will be Secondary.

Following is to be reported by the Secondary Segments:

- Carrying amount of segment assets, of those segment assets whose assets is 10% > total assets of business segments.
- Tangible and Intangible assets acquired.

Other Optional Disclosures

1. Transfer pricing basis.
2. Changes in segment accounting policies.
3. For Business Segments types of products and services.
4. Composition of each Geographical Segment.

Additional disclosures required in respect of secondary segments.

In addition to reporting the aforementioned segment information in respect of primary segments, enterprises are required to make additional disclosures in respect of secondary segments. The disclosure required depends on type of primary segment. The principal disclosure requirements are as below:

Where primary segments are business segments (Para 48)

a) segments revenue from external customers by geographical area based on the geographical location of its customers, for each geographical segment whose revenue from sales to external customers is 10% or more of enterprise revenue;

b) the total carrying amount of segment assets by geographical location of assets, for each geographical segment whose segment assts are 10% or more of the total assets of all geographical segment; and

c) the total cost incurred during the period to acquire segment assets that are expected to be used during more than one period (tangible and intangible fixed assets) by geographic allocation of assets, for each geographical segment whose segment assets are 0% or more of the total assets of all geographical segments.

Where Primary segments are geographical segments (Para 49).

Where primary segment is geographical segment (whether based on location of assets or location of customers), the following segment information should be disclosed for each business segment whose revenue from sales to external customers is 10% or more of the total assets of all business segments:

a) segment revenue from external customers;

b) the total carrying amount of segment assets; and

the total cost incurred during the period to acquire segment assets that are expected to be used during more than one period (tangible and intangible fixed assets).

Where Primary segments are geographical segments based on location of assets (Para 50).

If locations of customers are different from location of assets, in addition to disclosures required pursuant to paragraph 49 above, an enterprise is required to report revenue from sales to external customers for each customer-based geographical segment whose revenue from sales to external customers is 10% more of enterprise revenue.

Where Primary segments are geographical segments based on location of customers (Para 51).

If location of assets are different from location of customers, in addition to disclosures required pursuant to paragraph 49 above, an enterprise is required to report the following segment information for each asset based geographical segment whose revenue from sales to external customers is 10% or more of enterprise revenue or whose segment assets is 10% or more of total enterprise assets.

a) the total carrying amount of segment assets by geographical location of the assets, and

b) The total cost incurred during the period to acquire segment assets that are expected to be used during more than one period (tangible and intangible fixed assets) by location of the assets.

Some Examples of Segmental Disclosure (For Your Knowledge)

Name of the Co.	Industry	Segments
Dabur India Ltd.	Pharma	FMCG Ayurvedic products Others
SAIL	Steel	Geographical segment Bhilai Steel Plant Durgapur Steel Plant Rourkela Steel Plant Bokaro Steel Plant IISCO Steel Plant Alloy Steel Plant Salem Steel Plant Visvesaraya Steel Plant Others
Indian Hotels Ltd.	Hotel	Hotel Services Air Catering

Lifetree Convergence Ltd.	IT	Primary reporting Business segment Software products, Software development products, Software maintenance Secondary reporting Geographical segment India Europe South Asia Other part of the world
Tata Chemical Ltd.	Fertilizers and Chemical	Inorganic Chemical Fertilizers
Barclays PLC	Banking	UK Banking Barklay Card Barklays Capital Barclays Wealth Retail and Commercial Banking Insurance activities HO and other operations
Axis Bank	Banking	Treasury Corporate Banking Retail Banking Others
Tech Mahindra	IT and technical services	Telecom Service provider Telecom equipment manufacturer BPO Others
Sonata Software	IT	Geographical Segment Domestic Services (Sales and Services) International Services (Sales and Services)

Religare Ltd.	Financial Services	Investments and Finance Financial Advisory Services Broking Support Services Fees Custodian Fees Life Insurance
ITC	Conglomerate	Tobacco Hotels Agri products Toilet products

QUESTION NO 1

Rajesh Ltd. has ten segments. The share of revenue, profit/loss and assets of each of these ten segments is given below. The company has identified segments H,I and J for reporting. Comment the adequacy of reporting, assuming there are no inter segment revenues.

Segments	Revenues	Profit (Loss)	Assets
A,B,C,D,E,F,G,	5% each=35%	5% each=35%	8%each=56%
H,I,	20% each=40%	25% each=50%	20% each=40%
J	25%	15%	4%

QUESTION NO 2

Information relating to five segments of Sharma Ltd. is as under: (₹ in lakhs)

Segment	A	B	C	D	E	Total
Segment revenue	150	200	200	50	300	900
Segment results	50	(70)	80	10	(25)	45
Segment assets	40	65	140	20	35	200

The company wishes to know which of the segments need to be reported. Advise.

QUESTION NO 3

ICS Ltd. has the following business / geographical segments. Examine which of these are reportable Segments under AS-17. (information in ₹'000)

Segments	Revenue	Profit and loss	Assets
A	9,600	1,750	4,100
B	300	180	450
C	100	70	450

QUESTION NO 4

Larson Ltd. has eight Segments A,B,C,D,E,F,G and H. The following information is available in relation to these Segments. (information in ₹ lakhs)

Particulars	A	B	C	D	E	F	G	H	Total
Segment Revenue:									
External	Nil	510	30	20	30	100	40	70	800
Internal	200	120	60	10	nil	nil	10	nil	400
Total revenue	200	630	90	30	30	100	50	70	1200
Segment result:									
profit(Loss)	10	(180)	30	(10)	16	(10)	10	14	(120)
Segment Assets	45	141	15	33	9	15	15	27	300

Identify which of the above constitute reportable Segment if you were informed that A,B,C and E were the reported Segments in the last financial year.

QUESTION NO 5

Following is the data regarding six Segments of Garg Ltd. (Rs in lakhs)

Segment	A	B	C	D	E	Total
Segment revenue	150	310	40	30	40	30
Segment results	25	(95)	5	5	(5)	15
Segment assets	20	40	15	10	10	5

The finance director is of the view that it is sufficient that Segments A and B alone are reported. Advice.

QUESTION NO 6

From the following information of Kristen Ltd. having two primary Segments, prepare a statement classifying the same under appropriate heads: (₹ in lakhs)

Particulars	Segment Alpha	Segment Beta	Others
Segment revenue (See note)	27,100	3,280	
Segment profit	4,640	(197)	
Capital expenditure	1,300	16	
Non cash expense excluding depreciation	114	16	
Liabilities	3,430	770	2,200
Assets	19,450	2,700	6,550
Depreciation	110	15	

Dividend income 285

Interest expenses 35

Tax provision 1675

Note: Segment revenue for Alpha includes inter Segment revenue of 50.

QUESTION NO 7

V Ltd. group has three divisions A,B and C. Details of their turnover, results and net assets are given below (in ₹'000) prepare a Segmental report.

Division A:

(a) Sales to division B ₹3050

(b) Local sales ₹60

(c) Export sales ₹4090

Division B:

(a) sales to division C ₹30

(b) export sales to Europe ₹200

Division C:

(a) Export sales to USA ₹180

Other information:

Particulars	Head office	A	B	C
Profit or loss before tax		160	20	(8)
Re allocated cost from Head office		48	24	24
Interest costs		4	5	1
Fixed assets	50	200	40	120
Net current assets	48	120	40	90
Long term liabilities	38	20	10	120

QUESTION NO 8

Prepare a Segmental report for publication in Diversifiers Ltd. fro the following details of the company' Segment three divisions and he head office.

	₹'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	Forging shop division ₹'000	Bright bar division ₹'000	Fitting division ₹'000
Pre tax operating results		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

QUESTION NO 9

Following details are given for Cheer Ltd. for the year ended 31.3.2003:

	₹'000	₹ '000
Sales:		
Food products	5650	
Plastic and packaging	625	
Health and scientific	345	
Others	162	6782
Expenses:		
Food products	3335	
Plastic and packaging	425	
Health and scientific	222	
Others	200	4182
General corporate expenses		562
Income from investments		132
Interest expenses		65
Identifiable Assets:		
Food products	7320	
Plastic and packaging	1320	
Health and scientific	1050	
Others	665	10355
General corporate Assets		722

Other information:

(a) Inter Segment sales are as below:

a. Food products	55000
b. Plastic and packaging	72000
c. Health and scientific	21000
d. Others	7000

(b) Operating profit included ₹33000 on inter Segment sales.

(c) Information about inter Segment expenses are not available.

You are required to prepare a statement showing financial information about Cheer Ltd. operations in different industry segments.

QUESTION NO 10

Microtech Ltd. produces batteries for scooters, cars, trucks and specialized batteries for invertors and UPS. Are these products different business segments or a part of the same business segment.

SOLUTION:

As per AS-17 segments are identified based on different risk/rewards factors. The company is basically producing batteries. But the batteries are further meant for (i) auto/ vehicle and (ii) invertors/ UPS mostly useful for household purposes i.e. indoors. The risk and rewards in auto and invertors are significantly different. Auto batteries are affected by governed policy, road conditions, number of accidents etc. and batteries for invertors/ UPS depends upon number of power suppliers, standard of living corporate use or household use etc. Hence there are two business segments for Microtech Ltd. 'Auto batteries' and 'batteries for invertors/UPS'.

QUESTION NO 11

If by applying the 10% thresholds, one reportable segment is identified but there are 5 other business/geographical segments which do not meet individually any of the 10% thresholds what should the enterprise do in this case.

SOLUTION:

In such case the decision regarding reportable segment lies with the management. As per TEST 5 (Management Choice) if any of the previous tests are not satisfied then management as its discretion choose reportable segment. Such segments are disclosed under unallocated column.

QUESTION NO 12

M Ltd. Group has three divisions A, B and C. Details of their turnover, results and net assets are given below:

	₹ ('000)
Division A	
Sales to B	3050
Other Sales (Home)	60
Export Sales	4090
	7200
Division B	
Sales to C	30
Export Sales to Europe	200
	230
Division C	
Export Sales to America	180

	Head Office	Division		
		A	B	C
	₹ ('000)	₹('000)	₹ ('000)	₹ ('000)
Operating Profit or Loss before Tax		160	20	(8)
Re-allocated cost from Head Office		48	24	24
Interest Costs		4	6	1
Fixed Assets	59	200	40	120
Net Current assets	48	120	40	90
Long term liabilities	38	20	10	120

* Long term liabilities does not include interest bearing liabilities.

Prepare a Segmental Report for publication in M Ltd. Group.

SOLUTION:

M Ltd.

Segmental Report

	Division			Inter-Segment	Consolidated
	A	B	C	Eliminations	Total
Segment Revenue					
Sales:					
Domestic	60	-	-	-	60
Export	4,090	200	180	-	4,470
External Sales	4,150	200	180	-	4,530
Inter-Segment Sales	3,050	30	-	(3,080)	--
Total Revenue	7,200	230	180	(3,080)	4,530

Segment result (given)	160	20	(8)		172
Head Office expenses					(96)
Operating Profit					76
Interest expenses					(10)
Net Profit					66
Other Information					
Fixed assets	200	40	120		360
	120	40	90		250
Segment Assets	320	80	210		610
Unallocated corporate Assts					98
Segment liabilities	20	10	120		150

Sales Revenue by Geographical Market

Home Sales	Export Sales	Export to Europe	Export to America	Consolidated Total
60	4090	200	180	4,530

QUESTION NO 13

The management of Airways Ltd. provides you the information related to one of its segment. You are required to calculate Segment assets from the given information Plant, Property, equipments = ₹ 24,00,000, investments = ₹ 7,00,000, Loans to employees = ₹ 4,00,000. Accounts receivable =₹ 5,00,000. DTA = ₹ 45000

SOLUTION:

Segment assets = 24,00,000 + 5,00,000 = 29,00,000

Segment assets includes the operating assets employed for the operations of the segments. Any loan even to employees also should not be considered segment assets. Investments and DTA are also not considerable.

QUESTION NO 14

From the following information of a Company having two primary segments, prepare a statement classifying the same under appropriate heads.

Particulars	A (₹ in Lakhs)	B (₹ in Lakhs)	Particulars	(₹ in Lakhs)
Segment Revenue	27,050	3,280	Dividend Income	285
Inter Segment Revenue	50	-	Interest Expenses	35
Segment Profit	4,640	Loss 107	Tax Provision	1,675
Capital Expenditure	1,300	16		
Non-Cash Exp. (excl. Dep.)	114	16		
Segment Liabilities	3,430	770	Other Liabilities	2,200
Segment Assets	19,450	2,700	Other Assets	6,550
Depreciation on Assets	110	15		

SOLUTION

Particulars	A (₹ in Lakhs)	B (₹ in Lakhs)	Total (₹ in Lakhs)
I. Segment Revenue	27,050	3,280	30,330
Inter Segment Revenue	50	-	50
Sub Total	27,100	3,280	30,380
Less: Inter Segment Revenue			(50)
Total			30,330
II. Segment Result	4,640	(197)	4,443
Interest Expenses			(35)
Dividend Income			285
Tax Provision			(1,675)
Profit after Tax			3,018
III. Other Information			
(a) Segment Assets	19,450	2,700	22,150
Unallocated Assets			6,550
(b) Segment Liabilities	3,430	770	5,200
Unallocated Liabilities			6,400
(c) Capital Expenditure	1,300	16	1,316
(d) Depreciation	110	75	185
Non Cash Expenses	114	16	130

STUDY MATERIAL & PAST EXAMINATION QUESTIONS (SELF READING)

QUESTION 15 (CA INTER NOV 2020) (5MARKS)

The accountant of Parag Limited has furnished you with the following data related to its Business Divisions:

(₹ in Lacs)

Division	A	B	C	D	Total
Segment Revenue	100	300	200	400	1,000
Segment Result	45	-70	80	-10	45
Segment Assets	39	51	48	12	150

You are requested to identify the reportable segments in accordance with the criteria laid down in AS 17.

SOLUTION

As per AS 17 'Segment Reporting', a business segment or geographical segment should be identified as a reportable segment if:

Its revenue from sales to external customers and from other transactions with other segments is 10% or more of the total revenue- external and internal of all segments; or

Its segment result whether profit or loss is 10% or more of:

- The combined result of all segments in profit; or
- The combined result of all segments in loss,

Whichever is greater in absolute amount; or

Its segment assets are 10% or more of the total assets of all segments.

On the basis of revenue criteria, segments A, B, C and D - all are reportable segments.

On the basis of the result criteria, segments A, B and C are reportable segments (since their results in absolute amount is 10% or more of 125 Lakhs).

On the basis of asset criteria, all segments except D are reportable segments.

Since all the segments are covered in at least one of the above criteria, all segments have to be reported upon in accordance with Accounting Standard (AS) 17.

QUESTION 16

M/s XYZ Ltd. has three segments namely X, Y, Z. The total Assets of the Company are ₹ 10.00 crores. Segment X has ₹ 2.00 crores, segment Y has ₹ 3.00 crores and segment Z has ₹ 5.00 crores. Deferred tax assets included in the assets of each segments are X- ₹ 0.50 crores, Y— ₹ 0.40 crores and Z— ₹ 0.30 crores. The accountant contends that all the three segments are reportable segments. Comment.

SOLUTION:

According to AS 17 "Segment Reporting", segment assets do not include income tax assets. Therefore, the revised total assets are ₹ 8.8 crores [₹ 10 crores – (₹ 0.5 + ₹ 0.4 + ₹ 0.3)]. Segment X holds total assets of ₹ 1.5 crores (₹ 2 crores – ₹ 0.5 crores);

Segment Y holds ₹ 2.6 crores (₹ 3 crores – ₹ 0.4 crores); and Segment Z holds ₹ 4.7 crores (₹ 5 crores – ₹ 0.3 crores). Thus all the three segments hold more than 10% of the total assets, all segments are reportable segments.

QUESTION 17

Microtech Ltd. produces batteries for scooters, cars, trucks, and specialised batteries for invertors and UPS. How many segments should it have and why?

SOLUTION

In case of Microtech Ltd., the basic product is the batteries, but the risks and returns of the batteries for automobiles (scooters, cars and trucks) and batteries for invertors and UPS are affected by different set of factors. In case of automobile batteries, the risks and returns are affected by the Government policy, road conditions, quality of automobiles, etc. whereas in case of batteries for invertors and UPS, the risks and returns are affected by power condition, standard of living, etc. Therefore, it can be said that Microtech Ltd. has two business segments viz- 'Automobile batteries' and 'batteries for Invertors and UPS'.

QUESTION 18 (CA INTER JAN 21) (5 MARKS)

The Senior Accountant of AMF Ltd. gives the following data regarding its five segments: (₹ in lakhs)

Particulars	P	Q	R	S	T	Total
Segment Assets	80	30	20	20	10	160
Segment Results	(190)	10	10	(10)	30	(150)
Segment Revenue	620	80	60	80	60	900

The Senior Accountant is of the opinion that segment "P" alone should be reported. Is he justified in his view? Examine his opinion in the light of provision of AS-17 'Segment Reporting'.

SOLUTION:

As per AS 17 'Segment Reporting', a business segment or geographical segment should be identified as a reportable segment if:

(i) Its revenue from sales to external customers and from other transactions with other segments is 10% or more of the total revenue- external and internal of all segments; or

(ii) Its segment result whether profit or loss is 10% or more of:

(1) The combined result of all segments in profit; or

(2) The combined result of all segments in loss, whichever is greater in absolute amount; or

(iii) Its segment assets are 10% or more of the total assets of all segments. Accordingly,

(a) On the basis of revenue from sales criteria, segment P is a reportable segment.

(b) On the basis of the result criteria, segments P & T are reportable segments (since their results in absolute amount is 10% or more of ₹ 200 Lakhs).

(c) On the basis of asset criteria, all segments except T are reportable segments.

Since all the segments are covered in at least one of the above criteria, all segments have to be reported upon in accordance with AS 17. Hence, the opinion of chief accountant that only segment 'P' is reportable is wrong.

QUESTION 19 (CA INTER MAY 2022 EXAMS : 5 MARKS)

XYZ Ltd. has 5 business segments. Profit / Loss of each of the segments for the year ended 31st March,2022 has been provided below. You are required to identify from the following whether reportable segments or not reportable segments, on the basis of "profitability test" as per AS-17.

Segment	**Profit (Loss) ₹ in lakhs**
A	225
B	25
C	(175)
D	(20)
E	(105)

SOLUTION :

As per AS 17 'Segment Reporting', a business segment or geographical segment should be identified as a reportable segment if:

Its segment results whether profit or loss is 10% or more of:

- The combined result of all segments in profit; i.e. ₹ 250 Lakhs or
- The combined result of all segments in loss; i.e. ₹ 300 Lakhs

Whichever is greater in absolute amount i.e. ₹ 300 Lakhs.

Operating Segment	Absolute amount of Profit or Loss (₹ In lakhs)	Reportable Segment Yes or No
A	225	Yes
B	25	No
C	175	Yes
D	20	No
E	105	Yes

On the basis of the profitability test (result criteria), segments A, C and E are reportable segments (since their results in absolute amount is 10% or more of ₹ 300 lakhs i.e. 30 lakhs).

ACCOUNTING STANDARD 24: DISCONTINUING OPERATION

QUESTION NO 1

A healthcare goods producer has changed the product line as follows:

	Washing soap	Bathing soap
January 2004- September, 2004 per month	2,00,000	2,00,000
October 2004- December, 2004 per month	1,00,000	3,00,000
January 2005- March, 2005 per month	0	4,00,000

The company has enforced a gradual enforcement of change in product line on the basis of an overall plan. The Board of Directors of the Company has passed a resolution to this effect. The company follows calendar year as its accounting year. Should it be treated as discontinuing operation?

SOLUTION :

Business enterprises frequently close facilities, abandon products, or even product lines, and cane the size of their work force in response to market forces. These kinds of terminations, generally, are not in themselves discontinuing operations unless they satisfy the definition criteria. By gradually reducing the size of operations in the product line of Washing Soap, the company has increased its scale of operations in Bathing Soap. Such a change is a gradual or evolutionary, phasing out of a product line or class of services and does not meet definition criteria in paragraph 3(a) of AS 24 — namely, disposing of substantially in its entirety, a component of the enterprise. Hence, this change over is not a discontinuing operation.

QUESTION NO 2

A company has two divisions -, cement and steel. It has started negotiating for disposal of the steel division informally since May 2001, discussion has been held with the possible buyers, the labour union has demonstrated against this secret deal, the company has given a statement that there is no move to sell the steel division. The significant reduction in the production has taken place because of decline in the market demand for the company's product not as Planned strategy to dose down operation. During November 2001 the Board of Directors has announced that they are considering disposal of the steel division because of continuing loss suffered by that division. But no formal resolution was passed. Necessary formalities for disposal of a division were fulfilled only during January 2002 and the steel division was disposed of in the last week of January 2002. The company follows calendar year as accounting year. Does this event require disclosure?

SOLUTION :

Initial Disclosure event has not yet taken place in 2001, hence no disclosure required.

QUESTION NO 3

Changeover Ltd. is in the business of making cell phones. During the year ended 31.3.2002, it made 1,00,000 units of GSM phones and 50,000 units of CDMA phones. In the current year, the company has gradually cut down the production of GSM phones and is utilizing the spare, capacity released for manufacturing CDMA phones. During the last quarter of 2002-03, not even a single unit of GSM phones has been produced whereas 60,000 unit of CDM.A phones were manufactured in the same period. Should it be treated as a discontinuing operation.

Hint :No

QUESTION NO 4

A division of Trousers Ltd. has been classified as a discontinuing operation for the current year. Should the accounts of the enterprise as a whole be prepared assuming that the entire enterprise is no longer a going concern?

Hint: No

QUESTION NO 5

Goodwork Ltd. is engaged in the business of marketing shoes for Liberty Footwear. It has four different divisions - one each for Northern, Southern, Western and Eastern Region, which function independently. Revenue from each division lies between 15%-35% of the total revenue.

Goodwork Ltd. has decided to dispose of its Eastern Division pursuant to single plan. However, the assets will be sold in piecemeal manner and the liability will be settled individually. The entire process is likely to be completed in two years. Can the closure of this division be treated as a discontinuing operation?

Hint: Yes

QUESTION NO 6

Radhika Ltd. is a company engaged in the business of manufacturing liquor. It has 70% stake in Chetanaye Ltd. During the current year ending 31-3-2003, it sold its entire stake to Pankaj Ltd. Can it be treated as a discontinuing operation for Radhika Ltd.?

QUESTION NO 7

What are the initial disclosure requirements for discontinuing operations? (Advanced Auditing)

QUESTION NO 8

A Company belonging to the process industry carries out three consecutive processes. The output of the first process is taken as input of the second process, and the output of the second process is taken as input of the third process. The final product emerges out of the third process. It is also possible to outsource the intermediate products. It has been found that over a period a time cost of production process is 10% higher than the market price of the intermediate product available freely in the market. The company has decided to close down the first process as a measure of cost saving (vertical spin off) and outsource. Should this event be treated as discontinuing operation?

SOLUTION :

The change made by the company is focused on outsourcing of services, in respect of one single process - in a sequence of processes. The net effect of this change is closure of one facility relating to a process. This has been done by the company with a view to achieving productivity improvements and savings in costs.

Such a change does not meet definition criteria in paragraph 3(a) of AS 24 — namely, disposing of substantially in its entirety, such as by selling a component of the enterprise in a single ,transaction. The change is merely a cost-saving endeavor. Hence, this change over is not a discontinuing operation.

QUESTION NO 9

A Cosmetic articles producing company provides the following information:

	Cold Cream	Vanishing Cream
January, 2006- September, 2006 per month	2,00,000	2,00,000
October, 2006- December, 2006 per month	1,00,000	3,00,000
January,2007- September, 2007 per month	0	4,00,000

The company has enforced a gradual change in product-line on the basis of an overall plan. The Board of Directors of the company has passed a resolution to this effect. The company follows calendar year as its accounting year. Should this be treated as a discontinuing operation?

Give reasons in support of your answers.

SOLUTION :

In response to the market forces, business enterprises often abandon products or even product lines and reduce the size of their work-force. These actions are not in themselves discontinuing operations unless they satisfy the definition criteria.

In the instant case the company has been gradually reducing operation in the product line of cold creams, simultaneously increasing operation in the product line of vanishing creams. The company was not disposing of any of its components. Phasing out a product line as undertaken by the company does not meet. definition criteria in paragraph 3 of AS 24, namely, disposing of substantially in its entreaty a component of the enterprise. Therefore, this change over is not a discontinuing operation

STUDY MATERIAL & PAST EXAMINATION QUESTIONS

QUESTION 10 (CA INTER NOV 2018) (5 MARKS)

What are the initial disclosure requirements of AS 24 for discontinuing operations?

SOLUTION:

An enterprise should include the following information relating to a discontinuing operation in its financial statements beginning with the financial statements for the period in which the initial disclosure event occurs:

A. A description of the discontinuing operation(s)

B. The business or geographical segment(s) in which it is reported as per AS 17

C. The date and nature of the initial disclosure event.

D. The date or period in which the discontinuance is expected to be completed if known or determinable

E. The carrying amounts, as of the balance sheet date, of the total assets to be disposed of and the total liabilities to be settled

F. The amounts of revenue and expenses in respect of the ordinary activities attributable to the discontinuing operation during the current financial reporting period

G. The amount of pre-tax profit or loss from ordinary activities attributable to the discontinuing operation during the current financial reporting period, and the income tax expense related thereto

H. The amounts of net cash flows attributable to the operating, investing, and financing activities of the discontinuing operation during the current financial reporting period

QUESTION 11 (CA INTER JULY 21 EXAM) (5MARKS)

Rohini Limited is in the business of manufacture of passenger cars and commercial vehicles. The Company is working on a strategic plan to close the production of passenger cars and to produce only commercial vehicles over the coming 5 years. However no specific plans have been drawn up for sale of neither the division nor its assets. As part of its prospective plan it will reduce the production of passenger cars by 20% annually. It also plans to establish another new factory for the manufacture of commercial vehicles and transfer surplus employees in a phased manner. You are required to comment:

(i) If mere gradual phasing out in itself can be considered as a discounting operation' operation within the meaning of AS-24

(ii) If the Company passes a resolution to sell some of the assets in the passenger car division and also to transfer few other assets of the passenger can division to the new factory, does this trigger the application of AS-24?

(iii) Would your answer to the above be different if the Company resolves to sell the assets of the passenger car division in a phases but time bound manner?

SOLUTION:

(i) In response to the market forces, business enterprises often abandon products or even product lines and reduce the size of their work-force. These actions are not in themselves discontinuing operations unless they satisfy the definition criteria.

In the instant case the company has been gradually reducing operation in the product line of passenger vehicles, simultaneously increasing operation in the product line of commercial vehicles. The company was not disposing of any of its components. Phasing out a product line as undertaken by the company does not meet definition criteria in paragraph 3 of AS 24, namely, disposing of substantially in its entreaty a component of the enterprise. Therefore, this change over is not a discontinuing operation

(ii) The company is not selling its division in its entirety due to which it can not be considered as a discontinuing operation as per AS 24.

(iii) In this case, it can be considered as discontinuing operating because company is selling all assets of division. As per provision of AS 24, its not mandatory to sell all the assets at once but assets can also be sold on piecemeal basis.

QUESTION 12

(i) What are the disclosure and presentation requirements of AS 24 for discontinuing operations?

(ii) Give four examples of activities that do not necessarily satisfy criterion (a) of paragraph 3 of AS 24, but that might do so in combination with other circumstances.

SOLUTION

(i) An enterprise should include the following information relating to a discontinuing operation in its financial statements beginning with the financial statements for the period in which the initial disclosure event occurs:

(a) a description of the discontinuing operation(s);

(b) the business or geographical segment(s) in which it is reported as per AS 17 'Segment Reporting';

(c) the date and nature of the initial disclosure event;

(d) the date or period in which the discontinuance is expected to be completed if known or determinable;

(e) the carrying amounts, as of the balance sheet date, of the total assets to be disposed of and the total liabilities to be settled;

(f) the amounts of revenue and expenses in respect of the ordinary activities attributable to the discontinuing operation during the current financial reporting period;

(g) the amount of pre-tax profit or loss from ordinary activities attributable to the discontinuing operation during the current financial reporting period, and the income tax expense related thereto; and

(h) the amounts of net cash flows attributable to the operating, investing, and financing activities of the discontinuing operation during the current financial reporting period.

(ii) Para 3 of AS 24 "Discontinuing Operations" explains the criteria for determination of discontinuing operations. According to AS 24, examples of activities that do not necessarily satisfy criterion (a) of paragraph 3, but that might do so in combination with other circumstances, include:

(i) Gradual or evolutionary phasing out of a product line or class of service;

(ii) Discontinuing, even if relatively abruptly, several products within an ongoing line of business;

(iii) Shifting of some production or marketing activities for a particular line of business from one location to another; and

(iv) Closing of a facility to achieve productivity improvements or other cost savings.

An example in relation to consolidated financial statements is selling a subsidiary whose activities are similar to those of the parent or other subsidiaries.

NOTES

ANNEXURE

Schedule III to the Companies Act, 2013

(See section 129) Division I*

Financial Statements for a company whose Financial Statements are required to comply with the Companies (Accounting Standards) Rules, 2006.

GENERAL INSTRUCTIONS FOR PREPARATION OF BALANCE SHEET AND STATEMENT OF PROFIT AND LOSS OF A COMPANY

1. Where compliance with the requirements of the Act including Accounting Standards as applicable to the companies require any change in treatment or disclosure including addition, amendment, substitution or deletion in the head/sub-head or any changes *inter se*, in the financial statements or statements forming part thereof, the same shall be made and the requirements of this Schedule shall stand modified accordingly.

2. The disclosure requirements specified in this Schedule are in addition to and not in substitution of the disclosure requirements specified in the Accounting Standards prescribed under the Companies Act, 2013. Additional disclosures specified in the Accounting Standards shall be made in the notes to accounts or by way of additional statement unless required to be disclosed on the face of the Financial Statements. Similarly, all other disclosures as required by the Companies Act shall be made in the notes to accounts in addition to the requirements set out in this Schedule.

3. (i) Notes to accounts shall contain information in addition to that presented in the Financial Statements and shall provide where required (a) narrative descriptions or dis-aggregations of items recognized in those statements and (b) information about items that do not qualify for recognition in those statements.

   (ii) Each item on the face of the Balance Sheet and Statement of Profit and Loss shall be cross-referenced to any related information in the notes to accounts. In preparing the Financial Statements including the notes to accounts, a balance shall be maintained between providing excessive detail that may not assist users of financial statements and not providing important information as a result of too much aggregation.

* *As per syllabus, only Division I of Schedule III (excluding general instructions for the preparation of consolidated financial statements) has been reproduced here. In exercise of the powers conferred by sub-section (1) of section 467 of the Companies Act, 2013, the Central Government made certain amendments in Schedule III to the said Act with effect from 1st day of April, 2021 vide MCA notification dated 24th March, 2021. This Annexure incorporates these amendments.*

4. (i) Depending upon the total income of the company, the figures appearing in the Financial Statements shall be rounded off as given below:

Totalincome	Roundingoff
(a) less than one hundred crore rupees	to the nearest hundreds, thousands, lakhs or millions, or decimals thereof
(b) one hundred crore rupees or more	to the nearest, lakhs, millions or crores, or decimals thereof.

(ii) Once a unit of measurement is used, it should be used uniformly in the Financial Statements.

5. Except in the case of the first Financial Statements laid before the Company (after its incorporation) the corresponding amounts (comparatives) for the immediately preceding reporting period for all items shown in the Financial Statements including notes shall also be given.

6. For the purpose of this Schedule, the terms used herein shall be as per the applicable Accounting Standards.

Note: This part of Schedule sets out the minimum requirements for disclosure onthe face of the Balance Sheet, and the Statement of Profit and Loss (hereinafter referred to as "Financial Statements" for the purpose of this Schedule) and Notes. Line items, sub-line items and sub-totals shall be presented as an addition or substitution on the face of the Financial Statements when such presentation is relevanttoanunderstandingofthecompany'sfinancialpositionorperformance or to cater to industry/sector-specific disclosure requirements or when required for compliance with the amendments to the Companies Act or under the Accounting Standards.

PART I – BALANCE SHEET

Name of the Company…………………….

Balance Sheet as at………………………

(Rupees in ....)

			Particulars	Note No.	Figures as at the end of current reporting period	Figures as at the end of previous reporting period
			1	2	3	4
			EQUITY AND LIABILITIES			
1.			**Shareholders' funds**			
	a		Share capital			
	b		Reserves and Surplus			
	c		Money received against share warrants			
2.			**Share application money pending allotment**			
3.			**Non-current liabilities**			
	a		Long-term borrowings			
	b		Deferred tax liabilities (Net)			
	c		Other long term liabilities			
	d		Long-term provisions			
4.			**Current liabilities**			
	a		Short-term borrowings			
	b		Trade Payables			
			(A) total outstanding dues of micro enterprises and small enterprises; and			
			(B) total outstanding dues of creditors other than micro enterprises and small enterprises.			
	c		Other current liabilities			
	d		Short-term provisions			
			Total			

			Particulars	Note No.	Figures as at the end of current reporting period	Figures as at the end of previous reporting period
			ASSETS			
1.			**Non-current assets**			
	a	i	Property, plant and Equipment			
		ii	Intangible assets			
		iii	Capital Work-in-progress			
		iv	Intangible assets under development			
	b		Non-current investments			
	c		Deferred tax assets (Net)			
	d		Long-term loans and advances			
	e		Other non-current assets			
2			**Current assets**			
	a		Current investments			
	b		Inventories			
	c		Trade receivables			
	d		Cash and cash equivalents			
	e		Short-term loans and advances			
	f		Other current assets			
			Total			

See accompanying notes to Financial Statements.

Notes

GENERAL INSTRUCTIONS FOR PREPARATION OF BALANCE SHEET

1. An asset shall be classified as current when it satisfies any of the following criteria:

   (a) it is expected to be realized in, or is intended for sale or consumption in, the company's normal operating cycle;

   (b) it is held primarily for the purpose of being traded;

   (c) it is expected to be realized within twelve months after the reporting date; or

   (d) it is cash or cash equivalent unless it is restricted from being exchanged or used to settle a liability for at least twelve months after the reporting date.

   All other assets shall be classified as non-current.

2. An operating cycle is the time between the acquisition of assets for processing and their realization in cash or cash equivalents. Where the normal operating cycle cannot be identified, it is assumed to have a duration of 12 months.

3. A liability shall be classified as current when it satisfies any of the following criteria:

   (a) it is expected to be settled in the company's normal operating cycle;

   (b) it is held primarily for the purpose of being traded;

   (c) it is due to be settled within twelve months after the reporting date; or

   (d) the company does not have an unconditional right to defer settlement of the liability for at least twelve months after the reporting date. Terms of a liability that could, at the option of the counterparty, result in its settlement by the issue of equity instruments do not affect its classification.

   All other liabilities shall be classified as non-current.

4. A receivable shall be classified as a 'trade receivable' if it is in respect of the amount due on account of goods sold or services rendered in the normal course of business.

5. A payable shall be classified as a 'trade payable' if it is in respect of the amount due on account of goods purchased or services received in the normal course of business.

6. A company shall disclose the following in the notes to accounts:

A. SHARE CAPITAL

For each class of share capital (different classes of preference shares to be treated separately):

(a) the number and amount of shares authorized;

(b) the number of shares issued, subscribed and fully paid, and subscribed but not fully paid;

(c) par value per share;

(d) a reconciliation of the number of shares outstanding at the beginning and at the end of the reporting period;

(e) the rights, preferences and restrictions attaching to each class of shares including restrictions on the distribution of dividends and the repayment of capital;

(f) shares in respect of each class in the company held by its holding company or its ultimate holding company including shares held by or by subsidiaries or associates of the holding company or the ultimate holding company in aggregate;

(g) shares in the company held by each shareholder holding more than 5 percent shares specifying the number of shares held;

(h) shares reserved for issue under options and contracts/commitments for the sale of shares/disinvestment, including the terms and amounts;

(i) for the period of five years immediately preceding the date as at which the Balance Sheet is prepared:

(A) Aggregate number and class of shares allotted as fully paid up pursuant to contract(s) without payment being received in cash.

(B) Aggregate number and class of shares allotted as fully paid up by way of bonus shares.

(C) Aggregate number and class of shares bought back.

(j) terms of any securities convertible into equity/preference shares issued along with the earliest date of conversion in descending order starting from the farthest such date.

(k) calls unpaid (showing aggregate value of calls unpaid by directors and officers)

(l) forfeited shares (amount originally paid up)

(m) A company shall disclose Shareholding of Promoters* as below:

Shares held by promoters at the end of the year				**% Change during the year*** **
S. No	Promoter name	No. of Shares**	% of total shares**	
Total				

B. RESERVES AND SURPLUS

(i) Reserves and Surplus shall be classified as:

(a) Capital Reserves;

(b) Capital Redemption Reserve;

(c) Securities Premium;

(d) Debenture Redemption Reserve;

(e) Revaluation Reserve;

(f) Share Options Outstanding Account;

(g) Other Reserves – (specify the nature and purpose of each reserve and the amount in respect thereof);

(h) Surplus i.e. balance in Statement of Profit & Loss disclosing allocations and appropriations such as dividend, bonus shares and transfer to/from reserves etc.

***Promoter here means promoter as defined in the Companies Act, 2013.*

***Details shall be given separately for each class of shares*

****Percentage change shall be computed with respect to the number at the beginning of the year or if issued during the year for the first time then with respect to the date of issue.*

(Additions and deductions since last balance sheet to be shown under each of the specified heads)

(ii) A reserve specifically represented by earmarked investments shall be termed as a 'fund'.

(iii) Debit balance of statement of profit and loss shall be shown as a negative figure under the head 'Surplus'. Similarly, the balance of 'Reserves and Surplus', after adjusting negative balance of surplus, if any, shall be shown under the head 'Reserves and Surplus' even if the resulting figure is in the negative.

C. LONG-TERM BORROWINGS

(i) Long-term borrowings shall be classified as:

(a) Bonds/debentures.

(b) Term loans

(A) From banks.

(B) From other parties

(c) Deferred payment liabilities.

(d) Deposits.

(e) Loans and advances from related parties.

(f) Long term maturities of finance lease obligations

(g) Other loans and advances (specify nature).

(ii) Borrowings shall further be sub-classified as secured and unsecured. Nature of security shall be specified separately in each case.

(iii) Where loans have been guaranteed by directors or others, the aggregate amount of such loans under each head shall be disclosed.

(iv) Bonds/debentures (along with the rate of interest and particulars of redemption or conversion, as the case may be) shall be stated in descending order of maturity or conversion, starting from farthest redemption or conversion date, as the case may be. Where bonds/debentures are redeemable by instalments, the date of maturity for this purpose must be reckoned as the date on which the first instalment becomes due.

(v) Particulars of any redeemed bonds/ debentures which the company has power to reissue shall be disclosed.

(vi) Terms of repayment of term loans and other loans shall be stated.

(vii) Period and amount of continuing default as on the balance sheet date in repayment of loans and interest, shall be specified separately in each case.

D. OTHER LONG TERM LIABILITIES

Other Long-term Liabilities shall be classified as:

(a) Trade payables

(b) Others

E. LONG-TERM PROVISIONS

The amounts shall be classified as:

(a) Provision for employee benefits.

(b) Others (specify nature).

F. SHORT-TERM BORROWINGS

(i) Short-term borrowings shall be classified as:

  (a) Loans repayable on demand

    (A) From banks

    (B) From other parties

  (b) Loans and advances from related parties.

  (c) Deposits.

  (d) Other loans and advances (specify nature).

(ii) Borrowings shall further be sub-classified as secured and unsecured. Nature of security shall be specified separately in each case.

(iii) Where loans have been guaranteed by directors or others, the aggregate amount of such loans under each head shall be disclosed.

(iv) Period and amount of default as on the balance sheet date in repayment of loans and interest shall be specified separately in each case.

(v) Current maturities of Long term borrowings shall be disclosed separately.

FA. Trade Payables

The following details relating to Micro, Small and Medium Enterprises shall be disclosed in the notes:

(a) the principal amount and the interest due thereon (to be shown separately) remaining unpaid to any supplier at the end of each accounting year;

(b) the amount of interest paid by the buyer in terms of section 16 of the Micro, Small and Medium Enterprises Development Act, 2006, along with the amount of the payment made to the supplier beyond the appointed day during each accounting year;

(c) the amount of interest due and payable for the period of delay in making payment (which have been paid but beyond the appointed day during the year) but without adding the interest specified under the Micro, Small and Medium Enterprises Development Act, 2006;

(d) the amount of interest accrued and remaining unpaid at the end of each accounting year; and

(e) the amount of further interest remaining due and payable even in the succeeding years, until such date when the interest dues above are actually paid to the small enterprise, for the purpose of disallowance of a deductible expenditure under section 23 of the Micro, Small and Medium Enterprises Development Act, 2006.

FB. Trade payables due for payment

The following ageing schedule shall be given for Trade payables due for payment:-

Trade Payables ageing schedule

(Amount in ₹)

Particulars	Outstanding for following periods from due date of payment#				
	Less than 1 year	1-2 years	2-3 years	More than 3 years	Total
(i) MSME					
(ii) Others					
(iii) Disputed dues – MSME					
(iv) Disputed dues–					
(v) Others					

# similar information shall be given where no due date of payment is specified in that case disclosure shall be from the date of the transaction.

Unbilled dues shall be disclosed separately;

Explanation: The terms 'appointed day', 'buyer', 'enterprise', 'micro enterprise', 'small enterprise' and 'supplier', shall have the same meaning assigned to those under clauses (b), (d), (e), (h), (m) and (n) respectively of section 2 of the Micro, Small and Medium Enterprises Development Act, 2006.

G. OTHER CURRENT LIABILITIES

The amounts shall be classified as:

(a) Current maturities of finance lease obligations;

(b) Interest accrued but not due on borrowings;

(c) Interest accrued and due on borrowings;

(d) Income received in advance;

(e) Unpaid dividends

(f) Application money received for allotment of securities and due for refund and interest accrued thereon. Share application money includes advances towards allotment of share capital. The terms and conditions including the number of shares proposed to be issued, the amount of premium, if any, and the period before which shares shall be allotted shall be disclosed. It shall also be disclosed whether the company has sufficient authorized capital to cover the share capital amount resulting from allotment of shares out of such share application money. Further, the period for which the share application money has been pending beyond the period for allotment as mentioned in the document inviting application for shares along with the reason for such share application money being pending shall be disclosed. Share application money not exceeding the issued capital and to the extent not refundable shall be shown under the head Equity and share application money to the extent refundable i.e., the amount in excess of subscription or in case the requirements of minimum subscription are not met, shall be separately shown under 'Other current liabilities'

(g) Unpaid matured deposits and interest accrued thereon

(h) Unpaid matured debentures and interest accrued thereon

(i) Other payables (specify nature);

H. SHORT-TERM PROVISIONS

The amounts shall be classified as:

(a) Provision for employee benefits.

(b) Others (specify nature).

I. Property, Plant and Equipment

(i) Classification shall be given as:

(a) Land.

(b) Buildings.

(c) Plant and Equipment.

(d) Furniture and Fixtures.

(e) Vehicles.

(f) Office equipment.

(g) Others (specify nature).

(ii) Assets under lease shall be separately specified under each class of asset.

(iii) A reconciliation of the gross and net carrying amounts of each class of assets at the beginning and end of the reporting period showing additions, disposals, acquisitions through business combinations, amount of change due to revaluation (if change is 10% or more in the aggregate of the net carrying value of each class of Property, Plant and Equipment) and other adjustments and the related depreciation and impairment losses/reversals shall be disclosed separately.

(iv) Where sums have been written off on a reduction of capital or revaluation of assets or where sums have been added on revaluation of assets, every balance sheet subsequent to date of such write-off, or addition shall show the reduced or increased figures as applicable and shall by way of a note also show the amount of the reduction or increase as applicable together with the date thereof for the first five years subsequent to the date of such reduction or increase.

J. INTANGIBLE ASSETS

(i) Classification shall be given as:

(a) Goodwill.

(b) Brands /trademarks.

(c) Computer software.

(d) Mastheads and publishing titles.

(e) Mining rights.

(f) Copyrights, and patents and other intellectual property rights, services and operating rights.

(g) Recipes, formulae, models, designs and prototypes.

(h) Licenses and franchise.

(i) Others (specify nature).

(A) A reconciliation of the gross and net carrying amounts of each class of assets at the beginning and end of the reporting period showing additions, disposals, acquisitions through business combinations, amount of change due to revaluation (if change is 10% or more in the aggregate of the net carrying value of each class of intangible assets) and other adjustments and the related depreciation and impairment losses or reversals shall be disclosed separately.

(B) Where sums have been written off on a reduction of capital or revaluation of assets or where sums have been added on revaluation of assets, every balance sheet subsequent to date of such write-off, or addition shall show the reduced or increased figures as applicable and shall by way of a note also show the amount of the reduction or increase as applicable together with the date thereof for the first five years subsequent to the date of such reduction or increase.

K. NON-CURRENT INVESTMENTS

(i) Non-current investments shall be classified as trade investments and other investments and further classified as:

(a) Investment property;

(b) Investments in Equity Instruments;

(c) Investments in preference shares

(d) Investments in Government or trust securities;

(e) Investments in debentures or bonds;

(f) Investments in Mutual Funds;

(g) Investments in partnership firms

(h) Other non-current investments (specify nature)

Under each classification, details shall be given of names of the bodies corporate [indicating separately whether such bodies are (i) subsidiaries, (ii) associates, (iii) joint ventures, or (iv) controlled special purpose entities] in whom investments have been made and the nature and extent of the investment so made in each such body corporate (showing separately investments which are partly-paid).

In regard to investments in the capital of partnership firms, the names of the firms (with the names of all their partners, total capital and the shares of each partner) shall be given.

(ii) Investments carried at other than at cost should be separately stated specifying the basis for valuation thereof.

(iii) The following shall also be disclosed:

(a) Aggregate amount of quoted investments and market value thereof;

(b) Aggregate amount of unquoted investments;

(c) Aggregate provision for diminution in value of investments.

L. LONG-TERM LOANS AND ADVANCES

(i) Long-term loans and advances shall be classified as:

(a) Capital Advances;

(b) Loans and advances to related parties (giving details thereof);

(c) Other loans and advances (specify nature).

(ii) The above shall also be separately sub-classified as:

(a) Secured, considered good;

(b) Unsecured, considered good;

(c) Doubtful.

(iii) Allowance for bad and doubtful loans and advances shall be disclosed under the relevant heads separately.

(iv) Loans and advances due by directors or other officers of the company or any of them either severally or jointly with any other persons or amounts due by firms or private companies respectively in which any director is a partner or a director or a member should be separately stated.

M. OTHER NON-CURRENT ASSETS

Other non-current assets shall be classified as:

(i) Long Term Trade Receivables (including trade receivables on deferred credit terms);

(ia) Security Deposits;

(ii) Others (specify nature);

(iii) Long term Trade Receivables, shall be sub-classified as:

(a) (A) Secured, considered good;

(B) Unsecured considered good;

(C) Doubtful

(b) Allowance for bad and doubtful debts shall be disclosed under the relevant heads separately.

(c) Debts due by directors or other officers of the company or any of them either severally or jointly with any other person or debts due by firms or private companies respectively in which any director is a partner or a director or a member should be separately stated.

(iv) For trade receivables outstanding, following ageing schedule shall be given:

TRADE RECEIVABLES AGEING SCHEDULE

(Amount in ₹)

Particulars	Outstanding for following periods from due date of payment#					
	Less than 6 months	6 months-1 year	1-2 years	2-3 years	More than 3 years	Total
(i) Undisputed Trade receivables – considered good						
(ii) Undisputed Trade Receivables – considered doubtful						
(iii) Disputed Trade Receivables considered good						
(iv) Disputed Trade Receivables considered doubtful						

Unbilled dues shall be disclosed separately.

N. CURRENT INVESTMENTS

(i) Current investments shall be classified as:

(a) Investments in Equity Instruments;

(b) Investment in Preference Shares

#similar information shall be given where no due date of payment is specified, in that case disclosure shall be from the date of the transaction.

(c) Investments in government or trust securities;

(d) Investments in debentures or bonds;

(e) Investments in Mutual Funds;

(f) Investments in partnership firms

(g) Other investments (specify nature).

Under each classification, details shall be given of names of the bodies corporate [indicating separately whether such bodies are (i) subsidiaries, (ii) associates, (iii) joint ventures, or (iv) controlled special purpose entities] in whom investments have been made and the nature and extent of the investment so made in each such body corporate (showing separately investments which are partly-paid). In regard to investments in the capital of partnership firms, the names of the firms (with the names of all their partners, total capital and the shares of each partner) shall be given.

(ii) The following shall also be disclosed:

(a) The basis of valuation of individual investments

(b) Aggregate amount of quoted investments and market value thereof;

(c) Aggregate amount of unquoted investments;

(d) Aggregate provision made for diminution in value of investments.

O. INVENTORIES

(i) Inventories shall be classified as:

(a) Raw materials;

(b) Work-in-progress;

(c) Finished goods;

(d) Stock-in-trade (in respect of goods acquired for trading);

(e) Stores and spares;

(f) Loose tools;

(g) Others (specify nature).

(ii) Goods-in-transit shall be disclosed under the relevant sub-head of inventories.

(iii) Mode of valuation shall be stated.

P. TRADE RECEIVABLES

(i) For trade receivables outstanding, the following ageing schedules shall be given:

TRADE RECEIVABLES AGEING SCHEDULE

(Amount in ₹)

Particulars	Outstanding for following periods from due date of payment#					
	Less than 6 months	6 months -1 year	1-2 years	2-3 years	More than 3 years	Total
(i) Undisputed Trade receivables – considered good						
(ii) Undisputed Trade Receivables – considered doubtful						
(iii) Disputed Trade Receivables considered good						
(iv) Disputed Trade Receivables considered doubtful						

Unbilled dues shall be disclosed separately.

(ii) Trade receivables shall be sub-classified as:

(a) Secured, considered good;

(b) Unsecured considered good;

(c) Doubtful.

(iii) Allowance for bad and doubtful debts shall be disclosed under the relevant heads separately.

(iv) Debts due by directors or other officers of the company or any of them either severally or jointly with any other person or debts due by firms or private companies respectively in which any director is a partner or a director or a member should be separately stated.

# similar information shall be given where no due date of payment is specified in that case disclosure shall be from the date of the transaction.

Q. CASHANDCASHEQUIVALENTS

(i) Cash and cash equivalents shall be classified as:

(a) Balances with banks;

(b) Cheques, drafts on hand;

(c) Cash on hand;

(d) Others (specify nature).

(ii) Earmarked balances with banks (for example, for unpaid dividend) shall be separately stated.

(iii) Balances with banks to the extent held as margin money or security against the borrowings, guarantees, other commitments shall be disclosed separately.

(iv) Repatriation restrictions, if any, in respect of cash and bank balances shall be separately stated.

(v) Bank deposits with more than 12 months maturity shall be disclosed separately.

R. SHORT-TERM LOANS AND ADVANCES

(i) Short-term loans and advances shall be classified as:

(a) Loans and advances to related parties (giving details thereof);

(b) Others (specify nature).

(ii) The above shall also be sub-classified as:

(a) Secured, considered good;

(b) Unsecured, considered good;

(c) Doubtful.

(iii) Allowance for bad and doubtful loans and advances shall be disclosed under the relevant heads separately.

(iv) Loans and advances due by directors or other officers of the company or any of them either severally or jointly with any other person or amounts due by firms or private companies respectively in which any director is a partner or a director or a member shall be separately stated.

S. OTHER CURRENT ASSETS (SPECIFY NATURE).

This is an all-inclusive heading, which incorporates current assets that do not fit into any other asset categories.

T. CONTINGENT LIABILITIES AND COMMITMENTS

(TO THE EXTENT NOT PROVIDED FOR)

(i) Contingent liabilities shall be classified as:

- (a) Claims against the company not acknowledged as debt;
- (b) Guarantees;
- (c) Other money for which the company is contingently liable

(ii) Commitments shall be classified as:

- (a) Estimated amount of contracts remaining to be executed on capital account and not provided for;
- (b) Uncalled liability on shares and other investments partly paid
- (c) Other commitments (specify nature).

U. The amount of dividends proposed to be distributed to equity and preference shareholders for the period and the related amount per share shall be disclosed separately. Arrears of fixed cumulative dividends on preference shares shall also be disclosed separately.

V. Where in respect of an issue of securities made for a specific purpose, the whole or part of the amount has not been used for the specific purpose at the balance sheet date, there shall be indicated by way of note how such unutilized amounts have been used or invested.

W. Where the company has not used the borrowings from banks and financial institutions for the specific purpose for which it was taken at the balance sheet date, the company shall disclose the details of where they have been used.

X. If, in the opinion of the Board, any of the assets other than Property, Plant Equipment, "Intangible assets and non-current investments do not have a value on realization in the ordinary course of business at least equal to the amount at which they are stated, the fact that the Board is of that opinion, shall be stated.

Y. Additional Regulatory Information

(i) Title deeds of Immovable Property not held in name of the Company

The company shall provide the details of all the immovable property (other than properties where the Company is the lessee and the lease agreements are duly executed in favour of the lessee) whose title deeds are not held in the name of the company in format given below and where such immovable property is jointly held with others, details are required to be given to the extent of the company's share.

Relevant line item in the Balance sheet	Description of item of property	Gross carrying value	Title deeds held in the name of	Whether title deed holder is a promoter, director or relative# of promoter* / director or employee of promoter/ direct or	Property held since which date	Reason for not being held in the name of the company**
PPE - Investment property - PPE retired from active use and held for disposal - others	Land Building Land Building Land Building	-	-	-	-	**also indicate if in dispute

(ii) Where the Company has revalued its Property, Plant and Equipment, the company shall disclose as to whether the revaluation is based on the valuation by a registered valuer as defined under rule 2 of the Companies (Registered Valuers and Valuation) Rules, 2017.

(iii) Following disclosures shall be made where Loans or Advances in the nature of loans are granted to promoters, directors, KMPs and the related parties (as defined under Companies Act, 2013,) either severally or jointly with any other person, that are:

(a) repayable on demand or

(b) without specifying any terms or period of repayment

#Relative here means relative as defined in the Companies Act, 2013.

**Promoter here means promoter as defined in the Companies Act, 2013.*

Type of Borrower	Amount of loan or advance in the nature of loan outstanding	Percentage to the total Loans and Advances in the nature of loans
Promoters		
Directors		
KMPs		
RelatedParties		

(iv) Capital-Work-in Progress (CWIP)

(a) For Capital-work-in progress, following ageing schedule shall be given:

CWIP aging schedule

(Amount in ₹)

CWIP	Amount in CWIP for a period of				Total*
	Less than 1 year	1-2 years	2-3 years	More than 3 years	
Projects in progress					
Projects temporarily suspended					

(b) For capital-work-in progress, whose completion is overdue or has exceeded its cost compared to its original plan, following CWIP completion schedule shall be given**:

(Amount in ₹)

CWIP	To be completed in			
	Less than 1 year	1-2 years	2-3 years	More than 3 years
Project 1 Project 2"				

**Total shall tally with CWIP amount in the balance sheet.*

***Details of projects where activity has been suspended shall be given separately.*

(v) Intangible assets under development:

(a) For Intangible assets under development, following ageing schedule shall be given:

Intangible assets under development aging schedule

(Amount in ₹)

Intangible assets under development	Amount in CWIP for a period of				Total*
	Less than 1 year	1-2 years	2-3 years	More than 3 years	
Projects in progress					
Projects temporarily suspended					

(b) For Intangible assets under development, whose completion is overdueor has exceeded its cost compared to its original plan, following **Intangible assets under development completion schedule** shall be given**:

(Amount in ₹)

Intangible assets under development	To be completed in				Total*
	Less than 1 year	1-2 years	2-3 years	More than 3 years	
Project 1					
Project 2					

(vi) Details of Benami Property held

Where any proceedings have been initiated or pending against the company for holding any benami property under the Benami Transactions (Prohibition) Act, 1988 (45 of 1988) and the rules made thereunder, the company shall disclose the following:-

(a) Details of such property, including year of acquisition,

(b) Amount thereof,

(c) Details of Beneficiaries,

(d) If property is in the books, then reference to the item in the Balance Sheet,

* *Total shall tally with the amount of Intangible assets underdevelopment in the balance sheet.*

***Details of projects where activity has been suspended shall be given separately.*

(e) If property is not in the books, then the fact shall be stated with reasons,

(f) Where there are proceedings against the company under this law as an abetter of the transaction or as the transferor then the details shall be provided,

(g) Nature of proceedings, status of same and company's view on same.

(vii) Where the Company has borrowings from banks or financial institutions on the basis of security of current assets, it shall disclose the following:-

(a) whether quarterly returns or statements of current assets filed by the Company with banks or financial institutions are in agreement with the books of accounts.

(b) if not, summary of reconciliation and reasons of material discrepancies, if any to be adequately disclosed.

(viii) Wilful Defaulter*

Where a company is a declared wilful defaulter by any bank or financial Institution or other lender, following details shall be given:

(a) Date of declaration as wilful defaulter,

(b) Details of defaults (amount and nature of defaults),

* "wilful defaulter" here means a person or an issuer who or which is categorized as a wilful defaulter by any bank or financial institution (as defined under the Act) or consortium thereof, in accordance with the guidelines on wilful defaulters issued by the Reserve Bank of India.

(ix) Relationship with Struck off Companies

Where the company has any transactions with companies struck off under section 248 of the Companies Act, 2013 or section 560 of Companies Act, 1956, the Company shall disclose the following details:-

Name of struck off Company	Nature of transactions with struck-off Company	Balance outstanding	Relationship with the Struck off company,if any, to be disclosed
	Investments in securities		
	Receivables		
	Payables		
	Shares held by stuck off company		
	Other outstanding balances (to be specified)		

(x) Registration of charges or satisfaction with Registrar of Companies

Where any charges or satisfaction yet to be registered with Registrar of Companies beyond the statutory period, details and reasons thereof shall be disclosed.

(xi) Compliance with number of layers of companies

Where the company has not complied with the number of layers prescribed under clause (87) of section 2 of the Act read with Companies (Restriction on number of Layers) Rules, 2017, the name and CIN of the companies beyond the specified layers and the relationship/extent of holding of the company in such downstream companies shall be disclosed.

(xii) Following Ratios to be disclosed:- Current Ratio,

a. Debt-Equity Ratio,

b. Debt Service Coverage Ratio,

c. Return on Equity Ratio,

d. Inventory turnover ratio,

e. Trade Receivables turnover ratio,

f. Trade payables turnover ratio,

g. Net capital turnover ratio,

h. Net profit ratio,

i. Return on Capital employed,

j. Return on investment.

The company shall explain the items included in numerator and denominator for computing the above ratios. Further explanation shall be provided for any change in the ratio by more than 25% as compared to the preceding year.

(xiii) Compliance with approved Scheme(s) of Arrangements

Where any Scheme of Arrangements has been approved by the Competent Authority in terms of sections 230 to 237 of the Companies Act, 2013, the Company shall disclose that the effect of such Scheme of Arrangements have been accounted for in the books of account of the Company 'in accordance with the Scheme' and 'in accordance with accounting standards' and deviation in this regard shall be explained.

(xiv) Utilisation of Borrowed funds and share premium:

(A) Where company has advanced or loaned or invested funds (either borrowed funds or share premium or any other sources or kind of funds) to any other person(s) or entity(ies), including foreign entities (Intermediaries) with the understanding (whether recorded in writing or otherwise) that the Intermediary shall

(i) directly or indirectly lend or invest in other persons or entities identified in any manner whatsoever by or on behalf of the company (Ultimate Beneficiaries) or

(ii) provide any guarantee, security or the like to or on behalf of the Ultimate Beneficiaries; the company shall disclose the following:-

(I) date and amount of fund advanced or loaned or invested in Intermediaries with complete details of each Intermediary.

(II) date and amount of fund further advanced or loaned or invested by such Intermediaries to other intermediaries or Ultimate Beneficiaries alongwith complete details of the ultimate beneficiaries.

(III) date and amount of guarantee, security or the like provided to or on behalf of the Ultimate Beneficiaries.

(IV) declaration that relevant provisions of the Foreign Exchange Management Act, 1999 (42 of 1999) and

Companies Act has been complied with for such transactions and the transactions are not violative of the Prevention of Money-Laundering act, 2002 (15 of 2003).;

(B) Where a company has received any fund from any person(s) or entity(ies), including foreign entities (Funding Party) with the understanding (whether recorded in writing or otherwise) that the company shall

(i) directly or indirectly lend or invest in other persons or entities identified in any manner whatsoever by or on behalf of the Funding Party (Ultimate Beneficiaries) or

(ii) provide any guarantee, security or the like on behalf of the Ultimate Beneficiaries, the company shall disclose the following:-

(I) date and amount of fund received from Funding parties with complete details of each Funding party.

(II) date and amount of fund further advanced or loaned or invested other intermediaries or Ultimate Beneficiaries alongwith complete details of the other intermediaries' or ultimate beneficiaries.

(III) date and amount of guarantee, security or the like provided to or on behalf of the Ultimate Beneficiaries

declaration that relevant provisions of the Foreign Exchange Management Act, 1999 (42 of 1999) and Companies Act has been complied with for such transactions and the transactions are not violative of the Prevention of Money-Laundering act, 2002 (15 of 2003).;

PART II –STATEMENT OF PROFIT AND LOSS

Name of the Company……………………

Profit and loss statement for the year ended ………………………

(Rupees in ……………)

Particulars		Note No.	Figures for the current reporting period	Figures for the previous reporting period
1		2	3	4
I.	Revenue from operations		xxx	xxx
II.	Other income		xxx	xxx
III.	Total Income (I + II)		xxx	xxx
IV.	Expenses:		xxx	xxx
	Cost of materials consumed		xxx	xxx
	Purchases of Stock-in-Trade		xxx	xxx
	Changes in inventories of finished goods		xxx	xxx
	work-in-progress and Stock-in-Trade		xxx	xxx
	Employee benefits expense		xxx	xxx
	Finance costs		xxx	xxx
	Depreciation and amortization expense		xxx	xxx
	Other expenses			
	Total expenses		xxx	xxx
V.	Profit before exceptional and extraordinary items and tax (III-IV)		xxx	xxx
VI.	Exceptional items		xxx	xxx
VII.	Profit before extraordinary items and tax (V - VI)		xxx	xxx
VIII.	Extraordinary Items		xxx	xxx
IX.	Profit before tax (VII- VIII)		xxx	xxx

Particulars		Note No.	Figures for the current reporting period	Figures for the previous reporting period
1		2	3	4
X	Tax expense: (1) Current tax (2) Deferred tax		xxx xxx xxx	xxx xxx xxx
XI	Profit (Loss for the period from continuing operations (VII-VIII)		xxx	Xxx
XII	Profit/(loss) from discontinuing operations		xxx	Xxx
XIII	Tax expense of discontinuing operations		xxx	Xxx
XIV	Profit/(loss) from Discontinuing operations (after tax) (XII-XIII)		xxx	Xxx
XV	Profit(Loss)for the period (XI+XIV)		xxx	xxx
XVI	Earnings per equity share: (1) Basic (2) Diluted		 xxx xxx	 xxx xxx

See accompanying notes to the financial statements.

GENERAL INSTRUCTIONS FOR PREPARATION OF STATEMENT OF PROFIT AND LOSS

1. The provisions of this Part shall apply to the income and expenditure account referred to in sub-clause (ii) of Clause (40) of Section 2 in like manner as they apply to a statement of profit and loss.

2. (A) In respect of a company other than a finance company revenue from operations shall disclose separately in the notes revenue from

    (a) Sale of products;

    (b) Sale of services;

    (ba) Grants or donations received (relevant in case of section 8 companies only)";

(c) Other operating revenues; Less:

(d) Excise duty.

(B) In respect of a finance company, revenue from operations shall include revenue from

(a) Interest; and

(b) Other financial services

Revenue under each of the above heads shall be disclosed separately by way of notes to accounts to the extent applicable.

3. **Finance Costs**

Finance costs shall be classified as:

(a) Interest expense;

(b) Other borrowing costs;

(c) Applicable net gain/loss on foreign currency transactions and translation.

4. **Other income**

Other income shall be classified as:

(a) Interest Income (in case of a company other than a finance company);

(b) Dividend Income;

(c) Net gain/loss on sale of investments

(d) Other non-operating income (net of expenses directly attributable to such income).

5. **Additional Information**

A Company shall disclose by way of notes additional information regarding aggregate expenditure and income on the following items:

(i) (a) Employee Benefits Expense [showing separately (i) salaries and wages, (ii) contribution to provident and other funds, (iii) expense on Employee Stock Option Scheme (ESOP) and Employee Stock Purchase Plan (ESPP), (iv) staff welfare expenses].

(b) Depreciation and amortization expense;

(c) Any item of income or expenditure which exceeds one per cent of the revenue from operations or ₹ 1,00,000, whichever is higher;

(d) Interest Income;

(e) Interest Expense;

(f) Dividend Income;

(g) Net gain/ loss on sale of investments;

(h) Adjustments to the carrying amount of investments;

(i) Net gain or loss on foreign currency transaction and translation (other than considered as finance cost);

(j) Payments to the auditor as

(a) auditor,

(b) for taxation matters,

(c) for company law matters,

(d) for management services,

(e) for other services,

(f) for reimbursement of expenses;

(k) In case of companies covered u/s 135, amount of expenditure incurred on corporate social responsibility activities.

(l) Details of items of exceptional and extraordinary nature;

(m) Prior period items;

(ii) (a) In the case of manufacturing companies,

(1) Raw materials under broad heads.

(2) goods purchased under broad heads.

(b) In the case of trading companies, purchases in respect of goods traded in by the company under broad heads.

(c) In the case of companies rendering or supplying services, gross income derived from services rendered or supplied under broad heads.

(d) In the case of a company, which falls under more than one of the categories mentioned in (a), (b) and (c) above, it shall be sufficient compliance with the requirements herein if purchases, sales and consumption of raw material and the gross income from services rendered is shown under broad heads.

(e) In the case of other companies, gross income derived under broad heads.

(iii) In the case of all concerns having works in progress, works-in-progress under broad heads.

(iv) (a) The aggregate, if material, of any amounts set aside or proposed to be set aside, to reserve, but not including provisions made to meet any specific liability, contingency or commitment known to exist at the date as to which the balance-sheet is made up.

(b) The aggregate, if material, of any amounts withdrawn from such reserves.

(v) (a) The aggregate, if material, of the amounts set aside to provisions made for meeting specific liabilities, contingencies or commitments.

(b) The aggregate, if material, of the amounts withdrawn from such provisions, as no longer required.

(vi) Expenditure incurred on each of the following items, separately for each item:-

(a) Consumption of stores and spare parts.

(b) Power and fuel.

(c) Rent.

(d) Repairs to buildings.

(e) Repairs to machinery.

(f) Insurance.

(g) Rates and taxes, excluding, taxes on income.

(h) Miscellaneous expenses,

(vii) (a) Dividends from subsidiary companies.

(b) Provisions for losses of subsidiary companies.

(viii) The profit and loss account shall also contain by way of a note the following information, namely:

(a) Value of imports calculated on C.I.F basis by the company during the financial year in respect of –

I. Raw materials;

II. Components and spare parts;

III. Capital goods;

(b) Expenditure in foreign currency during the financial year on account of royalty, know-how, professional and consultation fees, interest, and other matters;

(c) Total value if all imported raw materials, spare parts and components consumed during the financial year and the total value of all indigenous raw materials, spare parts and components similarly consumed and the percentage of each to the total consumption;

(d) The amount remitted during the year in foreign currencies on account of dividends with a specific mention of the total number of non-resident shareholders, the total number of shares held by them on which the dividends were due and the year to which the dividends related;

(e) Earnings in foreign exchange classified under the following heads, namely:

I. Export of goods calculated on F.O.B. basis;

II. Royalty, know-how, professional and consultation fees;

III. Interest and dividend;

IV. Other income, indicating the nature thereof

(ix) **Undisclosed income:** The Company shall give details of any transaction not recorded in the books of accounts that has been surrendered or disclosed as income during the year in the tax assessments under the Income Tax Act, 1961 (such as, search or survey or any other relevant provisions of the Income Tax Act, 1961), unless there is immunity for disclosure under any scheme and also shall state whether the previously unrecorded income and related assets have been properly recorded in the books of account during the year.

(x) **Corporate Social Responsibility (CSR):** Where the company covered under section 135 of the companies act, the following shall be disclosed with regard to CSR activities:-

(a) amount required to be spent by the company during the year,

(b) amount of expenditure incurred,

(c) shortfall at the end of the year,

(d) total of previous years shortfall,

(e) reason for shortfall,

(f) nature of CSR activities,

(g) details of related party transactions, e.g., contribution to a trust controlled by the company in relation to CSR expenditure as per relevant Accounting Standard,

(h) where a provision is made with respect to a liability incurred by entering into a contractual obligation, the movements in the provision during the year should be shown separately.

(xi) Details of Crypto Currency or Virtual Currency: Where the Company has traded or invested in Crypto currency or Virtual Currency during the financial year, the following shall be disclosed:-

(a) profit or loss on transactions involving Crypto currency or Virtual Currency

(b) amount of currency held as at the reporting date,

deposits or advances from any person for the purpose of trading or investing in Crypto Currency/ virtual currency.

Note: Broad heads shall be decided taking into account the concept of materiality and presentation of true and fair view of financial statements.

QUESTIONS ON SCHEDULE 3

QUESTION 1

What happens when requirements of schedule 3 contradicts with the Provisions of Accounting Standards?

SOLUTION

Where compliance with the requirements of the Act including Accounting Standards as applicable to the companies require any change in treatment or disclosure including addition, amendment, substitution or deletion in the head or sub-head or any changes, in the financial statements or statements forming part thereof, the same shall be made and the **requirements of this Schedule shall stand modified accordingly**. The disclosure requirements specified in this Schedule are in addition to and not in substitution of the disclosure requirements specified in the Accounting Standards prescribed under the Companies Act, 2013. Additional disclosures specified in the Accounting Standards shall be made in the notes to accounts or by way of additional statement unless required to be disclosed on the face of the Financial Statements.

NOTE: This part of Schedule sets out the minimum requirements for on the face of the Balance Sheet, and the Statement of Profit and Loss (hereinafter referred to as —Financial Statements || for the purpose of this Schedule) and Notes. Line items, sub-line items and sub-totals shall be presented as an addition or substitution on the face of the Financial Statements when such presentation is relevant to an understanding of the company's financial position or performance or to cater to industry/sector-specific disclosure requirements or when required for compliance with the amendments to the Companies Act or under the Accounting Standards.

QUESTION 2

How can an asset be classified as a current assets?

SOLUTION

(a) it is expected to be realized, or is intended for sale or consumption, in the company's normal operating cycle; or

(b) it is held primarily for the purpose of being traded; or

(c) it is expected to be realized within twelve months after the reporting date; or

(d) it is cash or cash equivalent unless it is restricted from being exchanged or used to settle a liability for at least twelve months after the reporting date.

QUESTION 3

How can an asset be classified as a non-current asset?

SOLUTION

The Asset other than Current Asset shall be classified as non current assets.

QUESTION 4

What is the meaning of an operating cycle?

SOLUTION

Time between the acquisition of assets for processing and Their realization in cash or cash equivalents.

Where the normal operating cycle cannot be identified: It is assumed to have duration of 12 months.

QUESTION 5

ICAI Ltd provides you the following information :

1. Raw material stock holding period : 3 months
2. Work –in-progress holding perios : 1 month
3. Finished goods holding period : 4 monjths
4. Debtors collection period : 6 months

You are required to compute the operating cycle.

SOLUTION

According to Schedule III “an operating cycle is the time between the acquisition of assets for processing and their realization in cash or cash equivalents”.

Operating Cycle = Raw material stock holding period+work-in-progress holding period + Finished goods holding period+Debtors Collection period = 3+1+4+6=14 months.

QUESTION 6

State giving reason whether the Trade Receivables are Current Assets or Non-Current Assets as per Schedule III in the following cases.

Case	Operating Cycle Period	Expected Realization period
1	11 months	10 months

2.	11 months	12 months
3.	11 months	13 months
4.	14 months	13 months
5.	14 months	15 months

SOLUTION

Case	Current Assets or Non-Current Assets	Reason
1	Current Assets	Expected Realization period - Is less than the Operating Cycle period and - Is within 12 months
2.	Current Assets	Expected Realization Period within 12 months although it is more than the Operating Cycle period
3.	Non-Current Assets	Expected Realization period is more than the Operating Cycle Period and 12 months Period.
4.	Current Assets	Expected Realization period is less than the Opeating Cycle period although it is more than the 12 months period.
5.	Non-Current Assets	Expected Realization period is more than the operating cycle period and the 12 months period.

QUESTION 7

State giving reason whether the Trade payables are Current Liabilities or Non-Current Liabilities as per schedule III in the following cases:

Case	Operating Cycle Period	Expected Payment Period
1	11 months	10 months
2	11 months	12 months
3	11 months	13 months
4.	11 months	15 months

SOLUTION:

Case	Operating Cycle Period	Expected Payment Period
1	Current Liabilities	Expected Payment Period - Is less than the Operating Cycle period and - Is within 12 months
2.	Current Liabilities	Expected Payment period is within 12 months although it in more than the Operating Cycle period.
3.	Non-Current Liabilities	Expected Payment period is more than the operating Cycle period and 12 months period.
4.	Non-Current Liabilities	Expected Payment period is more than the Operating Cycle Period and the 12 months period.

QUESTION 8 (MAY 14) (8 MARKS)

ICAI Ltd. Is in the process of finalizing its accounts for year ended 31st March, 2015 and furnishes the following information:

(i) Finished goods normally are held for 1 month before sale.

(ii) Sales realization from Debtors usually takes 2 months from date of credit invoice.

(iii) Raw materials are held in stock to cover 1 month's production requirements.

(iv) Packing materials, being specifically made for the company and having lead time of 3 months is held in stock for 3 months.

(v) Being a monopoly KAY Ltd. Enjoys a credit period of 12.5 months from its suppliers who sometimes at the end of their credit opt for conversion of their dues into long term debt of KAY Ltd.

You are required to compute the operating cycle of ICAI Ltd. As per Schedule III of The Companies Act, 2013. As the suppliers of the company are paid off after a credit period of 12.5 months should this be part of Current Liability ? Would your answer be the same if the creditors are settled in 330 days ?

SOLUTION:

Operating Cycle: 1+1+3+1+2=8 months

(Credit Period given by Suppliers should not be deducted while computing operating cycle as per Schedule 3)

Classification of Liability to suppliers : Schedule III provides that :

"A liability shall be classified as current when it satisfies any of the following criteria:

(i) It is expected to be settled in the company's normal operating cycle ;

(ii) It is held primarily for the purpose of being traded;

(iii) It is due to be settled within 12 months after the reporting date; or

(iv) The company does not have an unconditional right to defer settlement of the liability for at least 12 months after the reporting date. Terms of a liability that could, at the option of the counterparty, result in its settlement by the issue of equity instruments and do not affect its classification".

(a) When Credit period is 12.5 months : It will be treated as non-current liability since it is not due to be settled within 12 months after the reporting date.

(b) When credit period is 330 days (i.e. 11 months approx.) : It will be treated as current liability since it is due to be settled within 12 months after the reporting date.

QUESTION 9

X Ltd. Provides you the following Information.

1. Raw material stock holding period : 4 months.
2. Work-in-progress holding period : 2 months.
3. Finished goods holding period : 3 months.
4. Debtors collection period : 4 months

You are required to compute the operating Cycle.

SOLUTION

As per Schedule III "An operating Cycle is the time between the acquisition of Assets for processing and their realization in cash or cash equivalents".

Statement showing calculation of Operating Cycle

Raw material stock holding period	= 4 months
+ work-in-progress holding period	= 2 month
+ Finished goods holding period	= 3months
+Debtors collection period	= 4months
	---------------
	13 months

QUESTION 10

H Ltd. engaged in the business of manufacturing lotus wine. The process of manufacturing this wine takes around 18 months. Due to this reason H Ltd. has prepared its financial statements considering its operating cycle as 18 months and accordingly classified the raw material purchased and held in stock for less than 18 months as current asset. Comment on the accuracy of the decision and the treatment of asset by H Ltd. As per Schedule III.

SOLUTION

- As per Schedule III, one of the criteria for classification of an asset as a current asset is that the asset is expected to be realised in the company's operating cycle or is intended for sale or consumption in the company's normal operating cycle.
- Further, Schedule III defines that an operating cycle is the time between the acquisition of assets for processing and their realization in cash or cash equivalents.
- However, when the normal operating cycle cannot be identified, it is assumed to have duration of 12 months. As per the facts given in the question, the process of manufacturing of lotus wine takes around 18 months; therefore, its realisation into cash and cash equivalents will be done only when it is ready for sale i.e. after 18 months.
- ***This means that normal operating cycle of the product is 18 months. Therefore, the contention of the company's management that the operating cycle of the product lotus wine is 18 months and not l2 months is correct. H. Ltd. will classify the raw material purchased held in stock as current asset.***

QUESTION 11

How can a liability be classified as a current liability?

SOLUTION

(a) It is expected to be settled in the company normal operating cycle; or

(b) It is held primarily for the purpose of being traded; or

(c) It is due to be settled within twelve months after the reporting date; or

(d) The company does not have an unconditional right to defer settlement of the liability for least twelve months after the reporting cm Terms of a liability that could, at the option the counterparty, result in its settlement by the issue of equity instruments do not affect its classification.

QUESTION 12

How can a liability be classified as a non-current liability?

SOLUTION

The liability other than Current liability shall be classified as Non-Current.

QUESTION 13 (AUDIT-MAY-13)

The Balance Sheet of G Ltd as at 31st March 13 is as under. Comment on the presentation in terms of revised Schedule III and Accounting Standards issued by NFRA.

Heading	Note No.	31s' March, 13	31st March, 12
Equity & Liabilities			
Share Capital	1	xxx	xxx
Reserves & Surplus	2	0	0
Employee stock option outstanding	3	xxx	xxx
Share application money	4	xxx	xxx
Non-Current Liabilities	5	xxx	xxx
Deferred tax liability (Arising from Indian Income Tax)			
Current Liabilities	6	xxx	xxx
Trade Payables		xxx	xxx
Total		xxxx	xxxx
Assets			
Non-Current Assets			
Fixed Assets-Tangible	7	xxx	xxx
CWIP (including capital advances)	8	xxx	xxx
Trade Receivables	9	xxx	xxx
Deferred Tax Asset((Arising from Indian Income Tax)	10	xxx	xxx
P&l Debit balance			
Total		xxxx	xxxx

SOLUTION

Following Errors are noticed in presentation as per Schedule III:

(I) Share Capital & Reserve & Surplus are to be reflected under the heading Shareholders' funds, which is not shown while preparing the balance sheet. Although it is a part of Equity and Liabilities yet it must be shown under head Shareholders 'funds. The heading Shareholders 'funds is given in the question missing in the balance sheet.

(ii) Reserve & Surplus is showing zero balance, which is not correct in the given case. Debit balance of statement of profit & Loss should be shown as a negative figure under the head Surplus'. The balance of Reserves and Surplus', after adjusting negative balance of surplus shall be shown under the head Reserves and Surplus 'even if the resulting figure in negative.

(iii) Schedule III requires that Employee Stock Option outstanding should be disclosed under the heading Reserves and Surplus

(iv) Share application money refundable shall be shown under the sub-heading Other Current Liabilities. As this is refundable and not pending for allotment, hence it is not a part of equity.

(v) Deferred Tax Liability has been correctly shown under Non-Current Liabilities. But Deferred tax assets and deferred tax liabilities, both, cannot be shown in balance sheet because only the net Balance of Deferred Tax Liability or Asset is to be shown.

(vi) Under the main heading of Non-Current Assets, Fixed Assets are further classified as under:

I. Tangible assets	II. Intangible assets
III. Capital work in Progress	IV. Intangible assets under development.

Keeping in view the above, the CWIP shall be shown under Fixed Assets as Capital Work in Progress. The amount of Capital advances included in CWIP shall be disclosed under the sub heading Long term loans and advances under the heading Non-CurrentAssets.

(vii) Deferred Tax Asset shall be shown under Non-Current Asset. It should be the net balance of Deferred Tax Asset after adjusting the balance of deferred tax liability.

QUESTION 14

How will you disclose the following items while preparing the Balance Sheet of a company ?

1. Trade Receivables
2. Trade Payables
3. Current Maturities of Long-term debt.

SOLUTION:

1. Trade Receivables are to be classified as Current Assets if Expected Realization period is either within the Operating Cycle Period of within the 12 months period.
2. Trade Payables are to be classified as Current Liabilities if expected payment period is either within the 12 months period.
3. Current Maturities of Long-term Debt represents that portion of long-term borrowings which is due within 12 months from the date of Balance Sheet or with in Operating Cycle Period. It appears under the head 'Current Liabilities and sub-head 'Other Current Liabilities'. For example 12% Debentures of Reliance Ltd. Rs. 100 lacs (20% Redeemable within 1 year). Rs. 20 lacs will appear as Current maturity of Long-term Debt under the head 'Current Liabilities' and sub-head 'other Current Liabilities and Rs. 80 lacs will appear under the head 'Non-Current Liabilities' and sub head 'Long-Term Borrowing'.

QUESTION 15

State under which head these accounts should be classified in balance Sheet, as per Schedule III to The Companies Act 2013:

i) Shares application money received in excess of issued share capital.

ii) Share option outstanding account.

iii) Unpaid matured debenture and interest accrued thereon.

iv) Uncalled liability on shares and other partly paid investments.

v) Calls unpaid.

vi) Intangible Assets underdevelopment

vii) Money received against share warrant.

viii) Long term maturity of finance lease obligation.

SOLUTION:

Classification of following accounts for the presentation in Schedule III to be Companies Act, 2013.

	Accounts	Head
i)	Share application money received in excess of issue share capital	Other Current liabilities.
ii)	Share option outstanding account	Reserve & Surplus
iii)	Unpaid matured debenture and interest accrued thereon	Other Current Liabilities.

iv)	Uncalled liability on share and other partly paid investment.	Contingent Liabilities and commitments-Commitments to the extend not provided for
v)	Calls unpaid	Share Capital
vi)	Intangible Assets under development	Fixed Assets
vii)	Money received against share warrant	Shareholder's Fund
viii)	Long term maturity of finance lease obligation	Long term Borrowings.

QUESTION 16

The management of X Ltd. Contends that the work in process is not valued since it is difficult to ascertain the same in view of the multiple processes involved. They opined that the value of opening and closing work in process would be more or less the same. Accordingly, the management had not separately disclosed work in process in its financial statements. Comment in line with schedule III.

SOLUTION:

Schedule III to the Companies Act, 2013 requires the disclosure of opening and closing WIP under broad heads by way of additional information (General Instruction 5 (iii)). In addition, AS-2 also requires the valuation of WIP. Therefore, the non-disclosure in the financial statements by the company amounts to violation of Schedule III.

QUESTION 17

Is non-disclosure of source from which Bonus shares have been issued, a violation of Schedule III to the Companies Act, 2013?

SOLUTION

No, since Schedule III does not require such disclosure. Schedule III merely requires the disclosure of aggregate number and class of shares allotted as fully paid up bonus shares for a period of years immediately preceding the balance sheet date is the Notes to accounts.

QUESTION 18

ICAI Ltd. Paid Rs. 25 lakhs as advance to Y Ltd. Towards the purchase of printing machinery on 15.01.2015 with delivery instruction to deliver the same in the last week of June, 2015. Further on 15.02.2015 X Ltd. Purchased two diesel generator sets from Y Ltd. For Rs. 30 Lakhs on 90 days Credit term. In the accounts for 2014-15, X Ltd. Intends to adjust the advance paid against Credit purchase and show the net amount of Rs. 5 lakhs as due from them. As the Statutory Auditor, how would you deal with this?

SOLUTION:

Since X Ltd. Has paid advance amount to the supplier of machinery to be used in the project, such advance amount should be grouped under the main heading 'Non-Current Assets' with the sub-head as Fixed Assets with a sub-classification as 'Capital work-in-Progress.' This is as per requirement of Schedule iii to the Companies Act, 2013 and the existing accounting practice.

It the advance is for purchase of their machinery, it should be grouped under a separate head-'Long Term Loan and advance' with a sub-classification as 'Capital Advance' under the main heading 'Non-current Assets'. In view of the above, the proposal of X Ltd. To show the net balance in the personal accounts of Y Ltd. Is not correct. Such proposal will conceal the two material items in the balance sheet-one, expenditure towards capital asset and the other current liability for purchase of the generator set.

Hence, the auditor should advice X Ltd., to show these two items separately. If X Ltd., does not accept the advice, the auditor should qualify his report with suitable quantification of amount involved.

PROBLEM 19

ICAI Ltd. Issued Bonds to the tune of Rs. 100 lacs and provided security to the tune of Rs. 80 lacs for the same. It insists that it will disclose the Bonds as "Secured" in the balance Sheet of the company. Comment.

SOLUTION:

Prima Facie, the Bonds Issued to the tune of Rs. 100 lacs are provided with security to the tune of Rs. 80 lacs i.e. neither fully secured nor unsecured. Guidance Note on the 'Terms used in Financial Statements' issue by ICAI, states "Secured Loans' as loan secured wholly or partly against tan assets. Hence the Bond should be classified under 'Secured Loans' for the purpose of disclosure in the balance sheet. However the nature of security should be clearly specified.

QUESTION 20

What are the mandatory disclosures to be made in notes to accounts under the heading of share capital as per schedule 3?

SOLUTION

a. The number and amount of shares authorized.

b. The number of shares issued, subscribed and fully paid, and subscribed but not fully paid.

c. Par value per share.

d. ***A reconciliation of the number of shares outstanding at the beginning and at the end of the reporting period.***

e. The rights, preferences and restrictions attaching to each class of shares including restrictions on the distribution of dividends and the repayment of capital.

f. Shares in respect of each class in the company held by its holding company or its ultimate holding company including shares held by or by subsidiaries or associates of the holding company or the ultimate holding company in aggregate.

g. ***Shares in the company held by each shareholder holding more than 5 per cent, shares specifying the number of shares held.***

h. Shares reserved for issue under options and contracts/commitments for the sale of shares/disinvestment, including the terms and amounts.

i. For the period of five years immediately preceding the date as at which the Balance Sheet is prepared.

    i. Aggregate number and class of shares allotted as fully paid-up pursuant to contract(s) without payment being received in cash.

    ii. Aggregate number and class of shares allotted as fully paid-up by way of bonus shares.

    iii. Aggregate number and class of shares bought back.

j. Terms of any securities convertible into equity/preference shares issued along with the earliest date of conversion in descending order starting from the farthest such date.

k. Calls unpaid (showing aggregate value of calls unpaid by directors and officers).

l. Forfeited shares (amount originally paid-up).

QUESTION 21

What are the mandatory disclosures to be made under the heading of Reserves & Surpluses?

SOLUTION

As per the provisions of schedule 3 of companies act 2013, the reserves of a company should be classified as follows:

1) Capital Reserves;

2) Capital Redemption Reserve;

3) Securities Premium Reserve;

4) Debenture Redemption Reserve;

5) Revaluation Reserve;

6) Share Options Outstanding Account;

7) Other Reserves (specify the nature and purpose of each reserve and the amount in respect thereof);

8) Surplus i.e., balance in Statement of Profit and Loss disclosing allocations and appropriations such as dividend, bonus snares and transfer to/from reserves, etc.;

(Additions and deductions since last balance sheet to be shown under each of the specified heads);

Reserve specifically represented by earmarked investments shall be termed as a "fund". **Debit balance of statement of profit and loss** Shall be shown as a negative figure under the head "Surplus". Similarly, the balance of "Reserves and Surplus", after adjusting negative balance of surplus, if any, shall be shown under the head "Reserves and Surplus" even if the resulting figure is in the negative.

QUESTION 22

Explain the meaning of share warrants?

SOLUTION

Meaning: A share warrant is a bearer document of title to shares and can be issued only by public limited companies and that to against fully paid up shares only.

A share warrant cannot be issued by a private company, because the share warrant states that its bearer is entitled to a number of shares mentioned there in. It is a negotiable document and is easily transferable by mere delivery to another person. The holder of the share warrant is entitled to receive dividend as decided by the company.

A share warrant is accompanied by attached coupons for the payment of future dividends.

There are three parts of a share warrant:

(1) The counter foil.

(2) Share Warrant proper.

(3) The dividend coupons.

Conditions for the issue of a share warrant:

(1) **Only public limited companies:** Share warrant can be issued by the public limited companies. It cannot be issued by private companies.

(2) **Against share certificate of fully paid up shares:** A share warrant is only issued against share certificate of fully paid up shares.

(3) **Provision in the Articles:** There must be a provision in the Articles of Association regarding the issue of share warrant. If there is a provision, the company can issue a share warrant. If there is no provision in the Articles, the company cannot issue a share warrant.

(4) **Permission of the Central Government:** Prior permission from the Central Government is necessary for the issue of share warrant.

(5) **Share warrant not issued originally:** Share warrant are not issued originally at the time of initial issue.

(6) **At the request of the share holder:** A share warrant is issued at the request of the Shareholders / member and not by the company at its own initiative.

In simple terms, a warrant is like an option issued by a company that gives the holder the right to buy stock from the company at a specified price within a certain designated time period. Generally speaking, warrants are issued by the company whose stock underlies the warrant and when an investor exercises a warrant, he or she buys stock from the company. A stock warrant is a way for a company to raise money through equity (stocks). A stock warrant is a smart way to own shares of a company because a warrant usually is offered at a price lower than that of a stock option. ^1

Like an option, a warrant does not represent actual ownership in the stock of the company and it is simply the right (but not the obligation) to buy shares at a certain price in the future.

The main difference between warrants and call options is that warrants are issued and guaranteed by the company, whereas options are exchange instruments and are not issued by the company. Also, the lifetime of a warrant is often measured in years, while the lifetime of a typical option is measured in months

1. A share warrant can be issued only when the shares are fully paid up whereas a share certificate can be issued at any stage without the shares being fully paid up.
2. A share warrant is a negotiable instrument but a share certificate is not.
3. A share certificate is a document showing prima facie title to the shares represented thereby but a share warrant is the share security itself capable of easy transfer.
4. A holder of a share certificate is a member of the company but the holder of a share warrant is not, unless the articles otherwise provide.
5. A share certificate can be issued both by a public and a private company but a share warrant is issued only by a public company.

QUESTION 23

How will you disclose the following items while preparing the Balance Sheet of a Company?

Item	Major Head	Sub-Head	Sub-Sub-Head
Preference Share whose redemption overdue	Shareholder's Funds (As per ICAI's Guidance Note)	Share Capital	
Share Application money pending Allotment-Not exceeding Issued Capital and to the extend not refundable	Shareholder's Fund	Share Capital	
Share Application Money pending Allotment-to the extent refundable	Current Liabilities	Other Current Liabilities	
Debit Balance of Profit & Loss A/c	Shareholder's Funds	Reserves and Surplus (As a Negative Figure)	
Loans repayable after Operating Cycle	Non-Current liabilities	Long-term Borrowings	
Loans repayable within Operating Cycle/12 months	Current Liabilities	Short-Term Borrowing	
Loans repayable on demand	Current liabilities	Short-Term Borrowing	
Trade Payables to be settled within Operating Cycle /12 months	Current Liabilities	Trade Payables	
Interest accused and due on Long-Term Borrowings	Current Liabilities	Other Current Liabilities	
Outstanding Expenses	Current Liabilities	Other Current Liabilities	

Tax Payable	Current Liabilities	Other Current Liabilities	
Bank Overdraft	Current Liabilities	Other Current liabilities	
Unpaid/Unclaimed Dividend	Current Liabilities	Other Current Liabilities	
Matured Deposits	Current Liabilities	Other Current Liabilities	
Matured Debentures	Current Liabilities	Other Current Liabilities	Current Maturities of Long-Term Debt.
That portion of Long-Term Borrowings repayable within 12 months	Current Liabilities	Other Current Liabilities	
Provision for tax	Current Liabilities	Short-Term Provisions	
Declared Dividend	Current Liabilities ›Note: This treatment is as per ICAI's Guidance Note and AS 4)	Other Current Liabilities	It may be noted that revised schedule VI requires merely the disclosure in Note to Accounts.
Provision for Employee Benefits to the settled with 12 months	Current Liabilities	Short-Term Provisions	
Provision for Employee Provident Fund to be settled after 12 months	Non-Current Liabilities	Long-term Provisions	
Provision for Employee Provident Fund to be settled after 12 months	Non-Current Liabilities	Long-term Provision	

Live Stock	Non Current Assets	PPE	Tangible Assets
Brands	Non Current Assets	PPE	Intangible Assets
Intellectual Property Rights	Non Current Assets	PPE	Intangible Assets
Licenses and Franchise	Non Current Assets	PPE	Intangible Assets
Building under construction	Non Current Assets	Fixed Assets	Capital work-in-Progress
Computer Software under Development	Non-Current Assets	Fixed Assets	Intangible Assets under Development
Investment in Property	Non-Current Assets	Non-Current Investments	
Capital Advances	Non-Current Assets	Long-Term Loans and Advances	
Security Deposits	Non-Current Assets	Long-Term Loans and Advances	
Deposits with Custom Authorities	Non-Current Assets	Long-Term Loans and Advances	
Loans & Advances Receivable after 12 months	Non-Current Assets	Long-term loans and advances	
Discount/Loss on issue of Debentures /Share Issued Exp. To be w/o after 12 months **Preliminary Expenses**	As per Para 56 of AS 26, Intangible	Other Non-Current Assets	

Preliminary Expenses	As per Para 56 of AS 26, intangible Assets', Preliminary expenses are to be recognized as expenses as and when they are incurred. Hence, Preliminary Expenses are not to appear in the Balance Sheet.		
Work-in-Progress	Current Assets	Inventories	
Loose Tools	Current Assets	Inventories	
Stores & Spares	Current Assets	Inventories	
Trade Receivables to be realized within 12 months/ Operating Cycle	Current Assets	Trade Receivables	
Provision for Doubtful Debts	Current Assets	Trade Receivables (Shown by way of deduction).	
Cheques/Drafts on hand	Current Assets	Cash and Cash Equivalents	
Bank Deposits with more than 12 months maturity	Current Assets	Cash and Cash Equivalents	
Loan & Advances receivable within 12 months	Current Assets	Short-term Loans and Advances	
Prepaid Expenses	Current Assets	Other Current Assets	
Interest accrued on Investments	Current Assets	Other Current Assets	

Unpaid Amount on Shares subscribed by Subscribers to Memorandum of Association	Current Assets (Note: Subscribed and paid up share capital will include such unpaid amount)	Other Current Assets	
Calls Unpaid on Shares other than those subscribed by Subscribers to Memorandum of Associations	Notes to Accounts (Note : Subscribed and paid up Share Capital will be net of Calls unpaid).		
Guarantees	Notes to Accounts	Contingent Liabilities and Commitments	Contingent Liabilities
Bills Discounted but not yet matured	Notes to accounts	Contingent Liabilities and Commitments	Contingent liabilities.
Uncalled Liabilities on partly paid Shares held as Investments	Notes to Accounts	Contingent Liabilities and Commitments	Commitments
Uncalled liability on partly paid Debentures held as investments.	Notes to Accounts	Contingent Liabilities and Commitments	Commitments.
Arrears of Fixed Cumulative Dividends on Preference Shares	Notes to Accounts	Contingent Liabilities and Commitments	Commitments.
Allocations and Appropriations such as Dividend, bonus Shares and Transfer to/from Reserves	Notes to Accounts	Reserves and Surplus	Surplus

NOTES

BUSINESS COMBINATION (ACCOUNTING STANDARD 14)

(Dear Student, this topic does not include internal reconstruction as we have covered it separately

QUESTION 1(AS-14)

What are the conditions, which, according to Accounting Standard 14, must be satisfied for 'Amalgamation in the nature of Merger' and 'Amalgamation in the nature of Purchase'?

OR

What are the conditions, which, according to Accounting Standard 14, must be satisfied for 'Amalgamation in the nature of Merger'?

OR

Distinguish between amalgamation by merger and by purchase as per AS 14.

SOLUTION:

Amalgamation in the Nature of Merger: An amalgamation in the nature of merger should satisfy all the following conditions:

All the assets and liabilities of the transferor company become the assets and liabilities of the transferee company.

Shareholders holding at least 90% of the face value of the equity shares of the transferor company become equity shareholders of the transferee company (shares already held by the transferee company or its subsidiaries or their nominees are not to be considered for the purpose of 90%).

Purchase consideration is discharged wholly by the issue of equity shares in the transferee company; however, cash may be paid in respect of any fractional shares.

The business of the transferor company is intended to be carried on, after the amalgamation, by the transferee company.

No adjustment is intended to be made to the book values of the assets and liabilities of the transferor company when they are incorporated in the financial statements of the transferee company except to ensure uniformity of accounting policies.

Amalgamation in the Nature of Purchase: An amalgamation should be considered to be an amalgamation in the nature of purchase, when any one or more of the conditions specified above is not satisfied.

QUESTION 2(AS-14)

What are the methods of accounting for amalgamation? In what circumstances which method should be applied?

SOLUTION:

Methods of Accounting for Amalgamations: There are two main methods of accounting for amalgamations.

Pooling of interests method: An amalgamation in the nature of merger should be accounted for-under the pooling of interests method.

Purchase method: An amalgamation in the nature of purchase should be accounted for under the purchase method.

QUESTION 3(AS-14)

Explain pooling of interest method of amalgamation.

SOLUTION:

The Pooling of Interests Method: It requires that-

- Assets and liabilities of the transferor-company should be recorded at their existing carrying amounts, i.e., they are to be taken at their book values.
- Reserves (whether capital or revenue or arising on revaluation) of the transferor company should be recorded at their existing carrying amounts and in the same form, i.e., balance of general reserve should be carried as revaluation reserve, balance of revaluation reserve is carried as revaluation reserve etc.
- Difference of the share capital issued and other consideration paid to the transferor company over and above its own share capital should be adjusted in reserves.
- Balance of the Profit and Loss Account of the transferor company should be aggregated with that of the transferee company or transferred to the General Reserve.
- If transferor and transferee companies have conflicting accounting policies, a uniform set of accounting policies should be adopted, the effects on the financial statements of any changes in accounting policies should be reported in accordance with AS 5.

QUESTION 4 (AS-14)

Explain purchase method of amalgamation.

SOLUTION:

The Purchase Method:

It requires that-

- Assets and liabilities of the transferor company should be either incorporated at their existing carrying amounts or consideration should be allocated to individual identifiable assets and liabilities on the basis of their fair values at the date of amalgamation.
- Reserves (whether capital or revenue or arising on revaluation) of the transferor company, other than the statutory reserves, should not be included in the financial statements of the transferee company.
- Any excess of the consideration over the value of the net assets should be recognised as goodwill arising on amalgamation. If the consideration is lower than the value of the net assets acquired, the difference should be treated as Capital Reserve.
- Goodwill arising on amalgamation should be amortised to income on a systematic basis not exceeding five years unless a somewhat longer period can be justified.
- Identity of statutory reserve should be maintained, if required, by an equal charge to the Amalgamation Adjustment Account, which is presented under the head "Miscellaneous expenditure' and is adjusted against the balance of statutory reserves when their separate identities are no longer required.

QUESTION 5 (AS-14)

What are the discloser requirements prescribed under AS-14?

OR

Briefly describe the discloser requirements for amalgamation including additional discloser, if any, for different methods of amalgamation as per AS-14?

SOLUTION

Discloser Requirements: AS-14 requires following disclosers:

Common discloser: For all amalgamations, the following disclosures should be made:

Names and general nature of business of the amalgamating companies;

Effective date of amalgamation for accounting purposes;

Method of accounting used to reflect the amalgamation; **and**

Particulars of the scheme sanctioned under a statute.

Additional Discloser: In addition to above following should also be disclosed where-

1. **Pooling of interest method** is followed,

- Description and number of shares issued, together with % of each company's equity shares exchanged to effect the amalgamation;
- Amount of any difference between the consideration and the value of net identifiable assets acquired, and the treatment thereof

2. **Purchase method** is followed,

   Consideration for the amalgamation and a description of the consideration paid or contingently payable; and

   Amount of any difference between the consideration and the value of net identifiable assets acquired, and the treatment thereof including the period of amortisation of any goodwill arising on amalgamation.

QUESTION 6 (AS-14)

Briefly describe the disclosure requirements for Amalgamation including additional disclosure, if any, for different methods of amalgamation as per AS-14.

SOLUTION

The disclosure requirements for amalgamations have been prescribed in paragraphs 43 to 46 of AS 14 on Accounting for Amalgamation.

For all amalgamations, the following disclosures should be made in **the** first financial statements following the amalgamation:

- names and general nature of business of the amalgamating companies;
- the effective date of amalgamation for accounting purpose;
- the method of accounting used to reflect the amalgamation; and
- particulars of the scheme sanctioned under a statute.

For amalgamations accounted under the pooling of interests method, the following, additional disclosures should be made in the first financial statements following the amalgamation:

(i) Description and number of shares issued, together with the percentage of each company's equity shares exchanged to effect the amalgamation; and

(ii) the amount of any difference between the consideration and the value of net identifiable assets acquired, and the treatment thereof. For amalgamations, accounted under the purchase method, the following additional disclosures should be made in the first financial statements following the amalgamation;

   (i) Consideration for the amalgamation and a description of the consideration paid or contingently payable; and

(ii) the amount of any difference between the consideration and the value of net identifiable assets acquired, and the treatment thereof including the period of amortisation of any goodwill arising on amalgamation.

QUESTION 7

Briefly explain the methods of accounting for amalgamation as per Accounting Standard-14.

SOLUTION

As per AS 14 on 'Accounting for Amalgamations', there are two main methods of accounting for amalgamations:

(i) The Pooling of interest Method

Under this method, the assets, liabilities and reserves of the transferor company are recorded by the transferee company at their existing carrying amounts (after making the necessary adjustments).

If at the time of amalgamation, the transferor and the transferee companies have conflicting accounting policies, a uniform set of accounting policies is adopted following the amalgamation. The effects on the financial statements of any changes in accounting policies are reported in accordance with AS 5 on 'Net Profit or Loss for the Period, Prior Period items and Changes in Accounting Policies'.

(ii) The Purchase Method

Under the purchase method, the transferee company accounts for the amalgamation either by incorporating the assets and liabilities at their existing carrying amounts or by allocating the consideration to individual identifiable assets and liabilities of the transferor company on the basis of their fair values at the date of amalgamation. The identifiable assets and. liabilities may include assets and liabilities not recorded in the financial statements of the transferor company.

Where assets and liabilities are restated on the basis of their fair values, the determination of fair values may be influenced by the intentions of the transferee company, amalgamation.

BASIC QUESTIONS FROM THE POINT OF VIEW ACCOUNTING

QUESTION 8 (NET ASSET METHOD)

The financial position of two companies Hari Limited and Vayu Limited as on 31st March 2002 was as under:

	Hari Limited ₹	Vayu Limited ₹
Assets:		
Goodwill	50,000	25,000
Building	3,00,000	1,00,000
Machinery	5,00,000	1,50,000
Stock	2,50,000	1,75,000
Debtors	2,00,000	1,00,000
Cash at bank	50,000	20,000
Preliminary expenses	30,000	10,000
	13,80,000	5,80,000
Liabilities:		
Share capital:		
Equity shares of ₹10 each	10,00,000	3,00,000
9% preference shares of ₹100 each	1,00,000	
10% preference shares of ₹100 each		1,00,000
General reserve	1,00,000	80,000
Retirement Gratuity fund	50,000	20,000
Sundry creditors	1,30,000	80,000
	13,80,000	5,80,000

Hari Limited absorbs Vayu Limited on the following terms:

1. 10% Preference shareholders are to be paid by issue of 9% preference shares of Hari Limited.
2. Goodwill of Vayu Limited is valued at ₹50,000, Buildings are valued at ₹1,50,000 and the machinery at ₹1,60,000.

3. Stock to be taken over at 10% less value and reserve on bad and doubtful debts to be created @ 7.5%.
4. Equity shareholders of Vayu Limited will be issued equity shares @ 5% premium.

Prepare necessary ledger accounts to close the books of Vayu Limited and show the acquisition entries in the books of Hari Limited. Also draft the Balance Sheet after absorption as at 31st March 2002.

QUESTION 9 (NET PAYMENT METHOD)

Wye Ltd acquires the business of Z Limited. Whose Balance Sheet on 31stDecember, 1996 is as follows:

Liabilities	Amount	Assets	Amount
Share capital divided into shares of ₹100 each:-		Goodwill	2,00,000
		Land and building	4,00,000
6% preference shares capital	4,00,000	Plant and machinery	6,00,000
Equity share capital		Patents	50,000
Capital reserve	8,00,000	Stock	1,50,000
Profit and Loss account	1,00,000	Book debts	1,80,000
6% debentures	50,000	Cash at bank	70,000
Interest outstanding on above	2,00,000	Underwriting commission	40,000
Workmen's compensation reserve	12,000		
- expected Liability ₹5000	8,000		
Trade creditors	1,20,000		
	16,90,000		16,90,000

Wye Limited was to take over all assets (except cash) and Liabilities (except doe interest due on debentures) and to pay following amounts:

(a) ₹2,00,000 7% debentures (₹100 each) in Wye Limited for the existing debentures in Z Limited; for the purpose, each debenture of Wye Limited is to be treated as worth ₹105

(b) For each preference shares in Z Limited ₹10 in cash and one 9% preference shares of ₹100 each in Wye Limited

(c) For each equity share in Z Limited ₹20 in cash and one equity share in Wye Limited of ₹100 each having market value of ₹140.

(d) Expenses of Liquidation of Z Limited are to be reimbursed by Wye Limited to the extent of ₹10,000. Actual expenses amounted to ₹12,500.

Wye Limited valued land and building at ₹5,50,000, plant and machinery at ₹6,50,000 and patents at ₹20,000.

QUESTION 10 (NET ASSET METHOD)

The Indo-Gulf Company Limited sells its business to the Continental Company Limited as on December 31,1984 on which date its Balance Sheet was as under:

Liabilities	₹	Assets	₹
Paid up capital:		Freehold property	1,50,000
2,000 shares of ₹100 each	2,00,000	Goodwill	50,000
Debentures	1,00,000	Plant and tools	83,000
Trade creditors	30,000	Stock	35,000
Reserve fund	50,000	Bills receivable	4,500
Profit and Loss account	20,000	Sundry debtors	27,500
		Cash at bank	50,000
	4,00,000		4,00,000

The Continental Company Limited agreed to take over the assets (exclusive of cash at bank and goodwill) at 10 percent less than the book value, to pay ₹75,000 for goodwill and to take over the Debentures.

The purchase consideration was to be discharged by the allotment to the Indo-Gulf Company Limited of 1,500 shares of ₹100 each at a premium of ₹10 per share and the balance in cash.

The cost of the liquidation amounted to ₹3,000. Show the necessary accounts in the books of the Indo-Gulf Company Limited and show the necessary journal entries recording the transactions in the books of the Continental Company Limited.

QUESTION 11 (NET PAYMENT METHOD)

X Limited agreed to acquire the business of Y Limited as on December 31 1995. The summarized Balance Sheet of Y Limited on that date was as follows:

Liabilities	Amount	Assets	Amount
Share capital in fully paid up shares of ₹10 each	6,00,000	Goodwill	1,00,000
		Land and Building and Plant	6,40,000
General Reserve	1,70,000	Stock in trade	1,68,000
Profit and Loss a/c	1,10,000	Debtors	36,000
6% Debentures	1,00,000	Cash	56,000
Creditors	20,000		
	10,00,000		10,00,000

The amount payable by X Limited was agreed as follows:

1. A Cash payment equivalent to ₹2.50 for every ₹10 share in Y Limited.
2. The issue of such an amount of fully paid 5 per cent Debentures of X Limited at 96 per cent as is sufficient to discharge the 6 per cent Debentures of Y Limited at a premium of 20 per cent.
3. The issue of 90,000 ₹10 shares fully paid in X Limited having an agree value of ₹15 per share.

When computing the agreed consideration, the directors of X Limited valued the land, building and plant at ₹12,00,000, the stock in trade at ₹1,42,000 and debtors at their face value subject to an allowance of 5 per cent to cover doubtful debts. The cost of liquidation (met by X) of Y Limited comes to ₹5000. Close the books of Y Limited and pass the journal entries required in the books of X Limited.

QUESTION 12 (C.A.FINAL NOV 1995) (16 MARKS)

(NET PAYMENT METHOD)

With a view to reducing establishment expenses and generally to effect economy on working; Divya Limited agreed to take over the Pranav Limited as a going concern both companies engaged in the same trade.

Divya Limited was to pay the Debentures and liabilities of Pranav Limited and take over the assets the consideration being the issue by Divya Limited of 4,00,000 fully paid shares of

₹10 each and the payment of ₹3,00,000 in cash to the Pranav Limited. Divya Limited was to pay the liquidation expenses, which amounted to ₹1,40,000.

The balances in the books of the respective companies as on the date of absorption are given hereunder:

	Divya Limited (₹)	Pranav Limited (₹)	Divya Limited (₹)	Pranav Limited (₹)
Authorized capital:				
Divya Limited 20,00,000 shares of ₹10 each				
Pranav Limited 7,50,000 shares of ₹10 each				
Issued capital			1,50,00,000	50,00,000
Unpaid calls	50,000	10,000		
10% Debentures			50,00,000	10,00,000
Land and building	1,03,33,000	35,68,200		
Goodwill	30,00,000	5,00,000		
Sundry debtors & creditors	7,24,000	3,98,400	8,34,200	4,36,200
Bank balances	16,84,200			2,00,000
Stock	17,92,600	7,85,200		
Plant & machinery	38,76,800	16,43,900		
Bills receivable	3,62,100			
Profit and Loss a/c			9,88,500	2,69,500
	2,18,22,700	69,05,700	2,18,22,700	69,05,700

Assume that the absorption was duly effected but that the unpaid calls and a book debt of ₹40,000 due to the Pranav Limited proved irrecoverable.

Prepare the Realisation account and Members account in the books of Pranav Limited and the Balance Sheet of Divya Limited after the absorption.

CALCULATION OF PURCHASE CONSIDERATION

QUESTION 13 (FRACTIONAL SHARES) STUDY MATERIAL

A Limited agreed to absorb B Limited on 31st March 1999, whose balance sheet stood as follows:

Liabilities	₹	Assets	₹
Share capital		Fixed assets	7,00,000
80,000 shares of ₹10 each fully paid	8,00,000	Investments	
Reserve and surplus		Current assets	
General reserve	1,00,000	Loans and advances	
Secured loan		Stock in trade	1,00,000
Unsecured loan		Sundry debtors	2,00,000
Current liabilities & Provisions			
Sundry creditors	1,00,000		
	10,00,000		10,00,000

The consideration was agreed to be paid as follows:

(a) A payment in cash of ₹5 per share in B Limited and

(b) The issue of shares of ₹10 each in A Limited on the basis of 2 equity shares (valued at ₹15) and one 10% cum, preference share (valued at ₹10) for every five shares held in B Limited.

The whole of the share capital consists of shareholdings in exact multiple of five except the following holding.

Chopra	116	
Karki	76	
Amar singh	72	
Malhotra	28	
Other individuals	8	(eight members holding one share each)

	300	

It was agreed that A Limited will pay in cash for fractional shares equivalent at agreed value of shares in B Limited i.e. ₹65 for five shares of ₹50 paid. Prepare a statement showing the purchase consideration receivable in shares and cash.

QUESTION 14 (16 MARKS)

The summarized Balance Sheets of R Limited and P Limited for the year ending on 31.3.2000 are as under:

	R Limited ₹	P Limited ₹		R Limited ₹	P Limited ₹
Equity share capital (in shares of ₹10 each)	24,00,000	12,00,0000	Fixed assets	55,00,000	27,00,000
8% pref. Share capital (in shares of ₹10 each)	8,00,000		Current assets	25,00,000	23,00,000
10% pref. Share capital (in shares of ₹10 each)		4,00,000			
Reserves	30,00,000	24,00,000			
Current liabilities	18,00,000	10,00,000			
	80,00,000	50,00,000		80,00,000	50,00,000

The following information is provided:

(i)

	R Limited ₹	P Limited ₹
Profit before tax	10,64,000	4,80,000
Taxation	4,00,000	2,00,000
Preference dividend	64,000	40,000
Equity dividend	2,88,000	1,92,000

(ii) The equity shares of both companies are quoted in the market. Both the companies are carrying on similar manufacturing operations.

(iii) R Limited proposes to absorb P Limited as on 31.3.2000. The terms of absorption are as under:

(a) Preference shareholders of P Limited will receive 8% preference shares of R Limited sufficient to increase the income of preference shareholders of P Limited by 10%.

(b) The equity shareholders of P Limited will receive equity shares of R Limited on the following basis:

(i) The equity shares of P Limited will be valued by applying to the earnings per share of P Limited.75% of price earnings ratio of R Limited based on the results of 199-2000 of both the companies.

(ii) The market price of equity shares of R Limited is ₹40 per share.

(iii) The number of shares to be issued to the equity shareholders of P Limited will be based on the above market value.

(iv) In addition to equity shares, 8% preference shares of R Limited will be issued to the equity shareholders of P Limited to make up for the loss in income arising from the above exchange of shares based on the dividends for the year 19999-2000.

(v) The assets and liabilities of P Limited as on 31.3.2000 are revalued by professional valuer as under:

	Increased by ₹	Decreased by ₹
Fixed assets	1,00,000	
Current assets		2,00,000
Current assets		40,000

For the next two years no increase in the ratio of equity dividend is expected.

You are required to;

Set out in detail the purchase consideration

QUESTION 15

Channai Limited and Kolkata Limited have agreed that Chennai Limited will take over the business of Kolkata Limited with effect from 31st December 2001 it is agreed that:

(i) 10,00,000 shareholders of Kolkata Limited will receive shares of Chennai Limited. The swap ratio is determined on the basis of 26 weeks average market prices of shares of both the companies. Average prices have been worked out at ₹50 and ₹25 for the shares of Chennai Limited and Kolkata Limited respectively.

(ii) In addition to (i) above shareholders of Kolkata Limited will be paid cash based on the projected synergy that will arise on the absorption of the business of Kolkata Limited by Chennai Limited. 50% of the projected benefits will be paid to the shareholders of Kolkata Limited.

The projection has been agreed upon by the management of both the companies:

Year	2002	2003	2004	2005	2006
Benefit (in ₹ Lakhs)	50	75	90	100	105

The benefit is estimated to grow at the rate of 2% from 2007 onwards.

It has been further agreed that a discount rate of 20% should be used to calculate the cash that the holder of each share of Kolkata Limited will receive:

(i) Calculate the cash that holder of each share of Kolkata Limited will receive.

(ii) Calculate the total purchase consideration.

QUESTION 16

The Massive Company Ltd. was incorporated on 1st July 2014 for the purpose of acquiring North Ltd. South Ltd. and West Ltd.

The summarized balance sheets of these companies as on 30th June 2014 are as	North Ltd.	South Ltd.	West Ltd.
Assets			
Tangible fixed assets – at cost less	5,00,000	4,00,000	3,00,000
Goodwill	Nil	60,000	Nil
Other assets	2,00,000	2,80,000	85,000
	7,00,000	7,40,000	3,85,000

	North Ltd.	South Ltd.	West Ltd.
Liabilities			
Issued ordinary share capital shares of ₹10	4,00,000	5,00,000	2,50,000
P&L A/c.	1,50,000	1,10,000	60,000
10% Debentures	70,000	Nil	40,000
Trade Payables	80,000	1,30,000	35,000
	7,00,000	7,40,000	3,85,000

Average annual profits before			
Debentures interest (July 2013 to June 2014 inclusive)	90,000	1,20,000	50,000
Professional valuation of tangible assets on 30th June 2014	6,20,000	4,80,000	3,60,000

(1) The directors in their negotiations agreed that (i) the recorded goodwill of South Ltd. is valueless (ii) the 'other assets' of North Ltd. are worth ₹ 30,000 (iii) the valuation of 30th June 2014 in respect of tangible fixed assets should be accepted, (iv) these adjustments are to be made by the individual company before the completion of the acquisition.

(2) The acquisition agreement provides for the issue of 12 per cent unsecured Debentures to the value of the net assets of companies North Ltd., South Ltd., and West Ltd. and for the issuance of 10 nominal value ordinary shares for the capitalized average profit of each acquired company in excess of net assets contributed. The capitalisation rate is established at 10 per cent.

You are required to calculate purchase consideration and show the purchase consideration as discharged.

QUESTION 17 (CA INTER MAY 2019) (5MARKS)

Distinguish between Amalgamation, Absorption and External Reconstruction of Company.

Basis	Amalgamation	Absorption	External Reconstruction
Meaning	Two or more companies are wound up and a new company is formed to take over their business.	In this case, an existing company takes over the business of one or more existing companies.	In this case, a newly formed company takes over the business of an existing company.
Minimum number of Companies involved	At least three companies are involved.	At least two companies are involved.	Only two companies are involved.

Number of new resultant companies	Only one resultant company is formed. Two companies are wound up to form a single resultant company.	No new resultant company is formed.	Only one resultant company is formed. Under this case a newly formed company takes over the business of an existing company.
Objective	Amalgamation is done to cut competition and reap the economies in large scale.	Absorption is done to cut competition and reap the economies in large scale.	External reconstruction is done to reorganise the financial structure of the company.
Example	A Ltd. and B Ltd. amalgamate to form C Ltd.	A Ltd. takes over the business of another existing company B Ltd.	B Ltd. is formed to take over the business of an existing company A Ltd.

QUESTION 18 (C A FINAL NOV 2008 16 MARKS)

System Ltd. and HRD Ltd. decided to amalgamate as on 01.04.2008. Their Balance Sheets as on 31.03.2008 were as follows:

(in '000)

Particulars	System Ltd.	HRD Ltd.
Source of Funds:		
Equity share capital (₹10 each)	150	140
9% preference share capital (₹ 100 each)	30	20
Investment allowance reserve	5	2
Profit and Loss Account	10	6
10% Debentures	50	30
Sundry Creditors	25	15
Tax provision	7	4
Equity Dividend Proposed	30	28
Total	307	245

Application of Funds:	50	50
Building	80	70
Plant and Machinery	40	25
Investments	45	35
Sundry Debtors	36	40
Stock	40	25
Cash and Bank	6	--
Preliminary Expenses	307	245
Total		

From the following information, you are to prepare the draft Balance Sheet as on 01.04.2008 of a new company, intranet Ltd. which was formed to take over the business of both the companies and took over all the assets and liabilities:

(i) 50% Debentures are to be converted into Equity Shares of the New Company.

(ii) Out of the investments, 20% are non-trade investments.

(iii) Fixed Assets or systems Ltd. were valued at 10% above cost and that or HD Ltd. at 5% above cost.

(iv) 10% of sundry Debtors were doubtful for both the companies. Stocks to be carried at cost.

(v) Preference shareholders were discharged by issuing equal number of 9% preference shares at par.

(vi) Equity shareholders of both the transfer or companies are to be discharged by issuing Equity shares of ₹10 each of the new company at a premium of ₹ 5 per share.

Amalgamation is in the nature of purchase.

SOLUTION:

M/s. Intranet Ltd.
Draft Balance Sheet as at 1.4.2008

Particulars	Note No.	Rs
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	3,27,990
(b) Reserves and Surplus	2	1,45,995
(2) Non-Current Liabilities	3	40,000
Long term borrowings		
(3) Current Liabilities		
(a) Trade Payables		40,000
(b) Short Term provisions	4	11,000
Total		5,64,985
II. Assets		
(1) Non-current assets		
(a) Fixed Assets		
Tangible Assets	5	2,80,00
(b) Non-current investments	6	65,000
(c) Other non-current assets	7	7,000
(2) Current assets		
(a) Inventories		76,000
(b) Trade receivables	8	72,000
(c) Cash and cash equivalents	9	64,985
Total		5,64,985

Notes to Accounts

1.	Share Capital		
	Equity share capital (W.N.2)	2,77,990	
	27,799 Equity shares of ₹10 each, fully paid up		
	(25,133+2,666)		
	9% Preference share capital (W.N.2)	50,000	3,27,990
	Shares of ₹100 each		
2.	Reserve and Surplus		
	Securities premium (1,25,665+13,330) (W.N.2)	1,38,995	
	Investment allowance reserve (₹5,000+2,000)	7,000	1,45,995
3.	Long Term Borrowings		
	Secured		
	10% Debentures (50% of ₹80,000)	40,000	40,000
4.	Short term Provisions		
	Tax Provision (₹7,000 + ₹4,000)		11,000
5.	Tangible Assets		
	Building (₹66,000 + ₹52,000)	1,18,500	
	Plant and machinery (₹88,000 + ₹73,500)	1,61,500	2,80,000
6.	Non-current investments		
	Trade investments (80%)	48,750	
	Non-Trade investments (20%)	16,250	65,000
7.	Other non-current assets		7,000
	Amalgamation adjustment account		
8.	Trade receivables		
	Sundry debtors (₹45,000 + ₹35,000)	80,000	
	Less: Provision for doubtful debts @ 10%	(8,000)	72,000
9.	Cash & Cash equivalents		
	Cash and Bank (₹ 40,000 + ₹25,000 – ₹15)		64,985

Working Notes:

1. Calculation of value of equity shares issued to transferor companies.

		System Ltd.		HRD Ltd.
Assets taken over:				
Building		66,000		52,500
Plant and Machinery		88,000		73,500
Investments (trade and non- trade)		40,000		25,000
Stock		36,000		40,000
Sundry Debtors		40,500		31,500
Cash & Bank		40,000		25,000
		3,10,500		2,47,500
Less: Liabilities				
10% Debentures	50,000		30,000	
Sundry Creditors	25,000		15,000	
Tax Provision	7,000	(82,000)	4,000	(49,000)
		2,28,500		1,98,500
		(30,000)		(20,000)
Less: Preference Share Capital		1,98,500		1,78,500

2. Number of shares issued to equity shareholders, debentures holders and preference shareholders.

	System Ltd.	HRD Ltd.	Total
Equity shares issued @ ₹15 per share (including ₹5 Premium)			
1,98,500 divided by 15	13,233 Shares		
1,78,500 divided by 15		11,900 shares	25,133 shares
Equity Share capital @ ₹10	1,32,330	1,19,000	2,51,330
Securities premium @ ₹ 5	66,165	59,500	1,25,665
	1,98,495	1,78,500	3,76,995

50% of Debentures are converted into equity shares @ ₹ 15 per share			
25,000 divided by 15	1,666 Shares		
15,000 divided by 15		1,000 shares	2,666 Shares
Equity share capital @ ₹10	16,660	10,000	26,660
Security premium @ ₹5	8,330	5,000	13,330
	24,990	15,000	39,990
9% Preference share capital issued	30,000	20,000	50,000

QUESTION 19 (CA FINAL MAY 2013 16 MARKS)

Sun Limited agreed to absorb Moon Limited on 31st March 2012 whose Summarized Balance Sheet stood as follows:

Equity and Liabilities		Assets	
Share capital		Fixed Assets	10,50,000
1,20,000 shares of ₹10 each	12,00,000	Investments	
Reserves & Surplus			
General reserve	1,50,000	Current Assets,	
Secured Loan	-	Loans and Advances	
Unsecured Loan	-	Stock in Trade	1,50,000
Current Liabilities &		Sundry Debtors	3,00,000
Provisions			
Sundry Creditors	1,50,000		
	15,00,000		15,00,000

The consideration was agreed to be paid as follows:

(a) A payment in cash of ₹ 5 per share in Moon Ltd. and

(b) The issue of shares of ₹ 10 each in Sun Ltd. on the basis of two equity shares (valued at ₹15) and one 10% cumulative preference share (valued at rs.10) for every five shares held in Moon Ltd.

The whole of the share capital consist of shareholdings in exact multiple of five except the following holding.

P	174
Q	114
R	108
S	42

Other individuals 12 (Twelve members holding one share each)

It was agreed that Sun Ltd. will pay in cash for fractional shares equivalent at agreed value of shares in Moon Ltd. i.e. 65 for five shares of ₹ 50 paid.

Prepare a statement showing the purchase consideration receivables in shares and cash.

SOLUTION:

(a) Schedule showing determination of fractional shares

	Holding of Shares (A)	Exchangeable in nearest multiple of live (B)	Exchange in equity shares (C) = (B)/5x2	Exchange in Preference shares (D) = (B)/5x1	Non-exchangeable shares (E) = (A)-(B)
P	174	170	68	34	4
Q	114	110	44	22	4
R	108	105	42	21	3
S	42	40	16	8	2
Other Individuals	12	-	-	-	12
	450	425	170	85	25

(B) (i) Shares Exchangeable in Equity Shares of Sun Ltd.

	No. of Shares		No. of Shares
1,20,00-450 (Total A above)	1,19,550	2/5 there of	47,820
450-25 (Total E Above)	425	2/5 thereof	170
	1,19,975		47,990

(ii) Shares Exchangeable in 10% Cumulative Preference Shares of Sun Ltd.

	No. of Shares		No. of Shares
Shares held as in b (i) (above)	1,19,550	1/5 there of	23,910
Shares held as in b(i) above	425	1/5 thereof	85
	1,19,975		23,995

(c) There are 25 shares in Moon Ltd. which are not capable of exchange into equity and preference shares of Sun Ltd. They will be paid @ ₹65 for five shares of ₹50 Paid. = 325

Statement showing calculation of Purchase Consideration.

47,990 Equity shares @ ₹ 15 each	7,19,850
23,995, 10% Cumulative Preference shares @ ₹10 each	2,39,950
Cash on 1,19,975 shares @ ₹ 5 each	5,99,875
Add: Cash for 25 fractional shares.	325
	15,60,000

UPDATION OF ACCOUNTS

QUESTION 20 (SIMILAR QUESTION IN JULY 21 CA INTER EXAM)

The Balance Sheets of Rama Limited and Krishan Limited as at 31st December 1980 were as following:

Liabilities	Rama Limited	Krishan Limited	Assets	Rama Limited	Karishan Limited
Share capital:			Fixed assets (other than goodwill)	5,00,000	3,50,000
Divided into equity shares of ₹10 each	6,00,000	4,00,000	Stock in trade	95,000	75,000
			Debtors	1,40,000	1,00,000
Reserves	1,50,000	1,00,000	Cash at bank	1,17,500	60,000
Profit and Loss account	75,000	60,000	Preliminary expenses	10,000	5,000
Sundry creditors	37,500	30,000			
	8,62,500	5,90,000		8,62,500	5,90,000

Rama Limited took over and absorbed Krishan Limited as on 1st July 1981. No Balance Sheet of Krishan Limited was prepared on the date of take over. But the following information is made available to you:

(a) In the six months ended 30th June, 1981 Krishan Limited made a net profit of ₹60,000 after providing for depreciation at 10% per annum on fixed assets;

(b) Rama Limited during that period had made net profits of ₹1,45,000 after providing for depreciation at 10% per annum on the fixed assets;

(c) Both the companies had distributed dividends of 10% on 1st April 1981;

(d) Goodwill of Krishan Limited on the date of take over was estimated at ₹25,000 and it was agreed that the stock of Krishan Limited would be appreciated by ₹15,000 on the date of take over;

(e) Rama Limited to issue shares to shareholders of Krishan Limited on the basis of the intrinsic value of shares on the date of take over.

Draft the Balance Sheet of Rama Limited after absorption.

QUESTION 21 (C A FINAL NOV.2007 16 MARKS)

The Balance sheets of Strong Ltd. and Weak Ltd. as on 31.03.2007 is as follows:

Balance Sheet as on 31.03.2007

Liabilities	Strong Ltd.	Weak Ltd.	Assets	Strong Ltd	Weak Ltd.
Equity Share Capital (₹100 each)	50,00,000	30,00,000	Fixed Assets other than Goodwill	30,00,000	20,00,000
Reserve	4,00,000	2,00,000	Stock	8,00,000	6,00,000
P/L A/c.	6,00,000	4,00,000	Debtors	14,00,000	9,00,000
Creditors	5,00,000	3,00,000	Cash & Bank	12,00,000	3,50,000
			Preliminary Expenses	1,00,000	50,000
	65,00,000	39,00,000		65,00,000	39,00,000

Strong Ltd. takes over Weak Ltd. on 01.07.07. No Balance Sheet of Weak Ltd. is available as on that date. It is however estimated that Weak Ltd. earns estimated profit of ₹ 2,00,000 after charging proportionate depreciation @ 10% p.a. on fixed assets, during April-June, 2007.

Estimated profit of Strong Ltd. during these a month is ₹ 4,00,000 after charging proportionate depreciation @ 10% p.a. on fixed assets.

Both the companies have declared and paid 10% dividend within this 3 months period Goodwill of Weak Ltd. is valued at ₹ 2,00,000 and Fixed Assets are valued at ₹ 1,00,000 above the estimated book value. Purchase consideration is to be satisfied by strong Ltd. by shares at par, Ignore Income Tax.

You are required to calculate the following:

(i) No. of shares to be issued by Strong Ltd. to Weak Ltd. against purchase consideration.

(ii) Net Current Assts of Strong Ltd. and Weak Ltd. as on 01.07.2007.

(iii) P/L A/c. balance of the Strong Ltd. as on 01.07.2007.

(iv) Fixed Assets as on 01.07.2007;

(v) Balance Sheet of Strong Ltd. as on 01.07.2007 after takeover of Weak Ltd.

SOLUTION:

(i) **Number of shares to be issued by Strong Ltd. to Weak Ltd. against purchase consideration.**

Weak Ltd.		
Goodwill		2,00,000
Fixed Assets	20,00,000	
Less: Depreciation	50,000	
	19,50,000	
Add: Appreciation	1,00,000	20,50,000
Stock		6,00,000
Debtors		9,00,000
Cash and Bank Balances		
Add: Profit after deprecation 2,00,000	3,50,000	
Add: Depreciation (non-cash) 50,000	2,50,000	
Less: Dividend	(3,00,000)	3,00,000
		40,50,000
Less: Creditors		3,00,000
Purchase Consideration		37,50,000

(ii) Calculation of Net Current Assets as on 01.07.2007

		Strong Ltd.		**Weak Ltd.**
Current Assets:				
Stock		8,00,000		6,00,000
Debtors		14,00,000		9,00,000
Cash and Bank	12,00,000		3,50,000	
Less: Dividend	(5,00,000)		(3,00,000)	
Add: Profit before depreciation	4,75,000	11,75,000	2,50,000	3,00,000
				18,00,000

Less: Creditors		33,75,000		18,00,000
		5,00,000		3,00,000
		28,75,000		15,00,000

(iii) Profit and Loss Account balance of Strong Ltd. as on 1.07.2007

P&L A/c. balance as on 31.03.2007	6,00,000
Less: Dividend Paid	5,00,000
	1,00,000
Add: Estimated profit for 3 months after charging depreciation	4,00,000
	5,00,000

(iv) Fixed Assets as on 01.07.2007

Fixed Assets of Strong Ltd. as on 31.03.2007		30,00,000
Less: Depreciation for 3 months		75,000
		29,25,000
Fixed assets taken over of Weak Ltd. as on 31.03.2007	20,00,000	
Less: Proportionate depreciation for 3 months on fixed assets	50,000	
	19,50,000	
Add: Appreciation above the estimated book value	1,00,000	20,50,000
		49,75,000

(v) Balance sheet of Strong Ltd. as on 01.07.2007 (after Take Over)

Particulars	Note No.	₹
1. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	87,50,000
(b) Reserve and Surplus	2	8,00,000
(2) Current Liabilities		
Trade Payables	3	8,00,000
Total		1,03,50,000

II. Assets		
(1) Non-Current assets		
(a) Fixed Assets		
i. Tangible assets	4	49,75,000
ii. Intangible assets	5	2,00,000
(2) Current Assets		
(a) Inventories (8,00,000+6,00,000)		14,00,000
(b)Tradereceivables (14,00,000+9,00,000)		23,00,000
(c) Cash and Cash equivalents (11,75,000 + 3,00,000) – As per (Ii) above		14,75,000
Total		1,03,50,000

NOTES TO ACCOUNTS

1.	Share Capital		
	87,500 (50,000+37,500) equity shares of ₹ 100 each		87,50,000
2.	Reserve and Surplus		
	Reserves Less Preliminary expenses		
	(4,00,000 – 1,00,000)	3,00,000	
	Profit and Loss Account (As computed (iii)	5,00,000	8,00,000
3.	Trade Payables (5,00,000+3,00,000)		8,00,000
4.	Tangible Assets		
	Fixed assets (as computed in (iv)		49,75,000
5.	Intangible assets		2,00,000

INTRINSIC VALUE METHOD

QUESTION 22

The following are the Balance Sheets of Strong Limited and Small Limited as at 31st December 1988:

Liabilities	Strong Limited	Small Limited	Assets	Strong Limited	Small Limited
Share capital			Fixed assets cost		
Shares of the face value of ₹10 each	1,50,000	1,20,000	Less depreciation	1,40,000	75,000
			Current assets		
Reserves	95,000	10,000	Stock	42,000	47,000
Secured loans			Trade debtors	30,000	50,000
10% Debentures		20,000	Balance at bank	80,000	10,000
Current liabilities					
Trade creditors	47,000	32,000			
	2,92,000	1,82,000		2,92,000	1,82,000

Strong Limited agreed to absorb Small Limited as on 31st December 1988 on the following terms:

(a) Strong Limited agreed to repay 10% Debentures of Small Limited

(b) Strong Limited to revalue its fixed assets at ₹1,95,000 to be incorporated in the books.

(c) Shares of both the companies to be valued on net assets basis, after considering ₹50,000 towards value of goodwill of Small Limited

(d) The costs of absorption of ₹3,000 are met by Strong Limited

You are required to:

(i) Calculate the ratio of exchange of shares.

(ii) Give journal entries in the books of Strong Limited

(iii) Construct the bank account to arrive at the balance on absorption.

QUESTION 23

B Co. Limited had the following Balance Sheet as on 31st March 1978.

Liabilities	Amount	Assets	Amount
Share capital of 100 each	50,00,000	Fixed Assets	83,00,000
Capital reserve	10,00,000	Current Assets	69,00,000
General reserve	36,00,000	Investments	17,00,000
Unsecured loans	22,00,000	Goodwill	2,00,000
Sundry creditors	42,00,000		
Provision for taxation	11,00,000		
	1,71,00,000		1,71,00,000

B Co. Limited is Amalgamated with Beeson Limited as on 31st March, 1978 on which date the Balance Sheet of Beeson Limited as follows:

Liabilities	Amount	Assets	Amount
Share capital of 10 each	80,00,000	Fixed Assets	1,60,00,000
General Reserve	1,00,00,000	Current Assets	1,68,00,000
Secured Loans	40,00,000		
Sundry Creditors	46,00,000		
Provision for taxation	52,00,000		
Proposed Dividend	10,00,000		
	3,28,00,000		3,28,00,000

For the purpose of the Amalgamation the goodwill of B Co. Limited was considered valueless. There are also arrears of depreciation in B Co. Limited amounting to ₹4,00,000. The shareholders in B Co. Limited are allotted, in full satisfaction of their claims. Shares in Beesons in the same proportion as the respective intrinsic values of shares of two companies bear to one another. Pass journal entries in the books of both the companies to give effect to

ENTRIES ARE TO BE MADE AT PAR

QUESTION 24

Exe Limited is absorbed by Wye Limited. Given below are the Balance Sheets of the two companies prepared after revaluation of their assets on a uniform basis:

Balance Sheet of Exe Limited

Liabilities	Amount	Assets	Amount
Paid up capital:		Sundry assets	16,85,000
9,000 equity shares of ₹150 each ₹135 paid up	12,15,000	Cash in hand	3,500
General reserve	4,03,500		
Profit and Loss account	15,000		
Sundry creditors	55,000		
	16,88,500		16,88,500

Balance Sheet of Wye Limited

Liabilities	Amount	Assets	Amount
Paid up capital:		Sundry assets	43,57,500
40,000 equity shares of ₹75 paid up (fully paid)	30,00,000	Cash in hand	27,500
General reserve	12,85,000		
Profit and Loss account	35,000		
Sundry creditors	65,000		
	43,85,000		43,85,000

The holder of every three shares in Exe Limited was to receive five shares in the Wye Limited plus as much cash as is necessary to adjust the rights of shareholders of both the companies. In accordance with the intrinsic value of the share as per the respective Balance Sheets.

Pass necessary journal entries in the books of Wye Limited and prepare the Balance Sheet giving effect to the above scheme of absorption. Entries are to be made at par value only.

QUESTION 25 (IMPORTANT QUESTION FOR EXAMS 16 MARKS)

The following are the Balance Sheets of Big Limited and Small Limited for the year ending on 31st March 1998.

(Figures in crores of rupees)

	Big Limited	Small Limited
Equity share capital in equity shares of ₹10 each	50	40
Preference share capital in 10% preference shares of		60
₹100 each	200	150
Reserves and surplus	250	250
Loans secured	100	100
Total funds	350	350
Applied for: fixed assets at cost less depreciation	150	150
Current assets less current liabilities	200	200
	350	350

The present worth of fixed assets of Big Limited is ₹200 crores and that of Small Limited is ₹429 crores. Goodwill of Big Limited is ₹40 crores and of Small Limited is 75 crores.

Small Limited absorbs Big Limited by issuing equity shares at par in such a way that intrinsic net worth is maintained.

Goodwill account is not to appear in the books. Fixed assets are to appear at old figures.

(a) Show the Balance Sheet after absorption.

(b) Draft a statement of valuation of shares on intrinsic value basis and prove the accuracy of your workings.

PURCHASE CONSIDERATION WITH VALUATION OF GOODWILL

QUESTION 26 (CA FINAL NOV 1986)

The following is the Balance Sheet of weak Limited as on June 30, 1976:

Liabilities	Amount	Assets	Amount
Share capital (2000 shares of ₹100 each)	2,00,000	Goodwill	35,000
		Land and Building	85,000
Reserve fund	20,000	Plant and Machinery	1,60,000
5% Debentures	1,00,000	Stock	55,000
Loan from A (a director)	40,000	Debtors	65,000
Sundry creditors	80,000	Cash at bank	34,000
		Discount on Debentures	6,000
	4,40,000		4,40,000

The business of the company is taken over by strong Limited as on the date on the following terms:

(i) Strong Limited to take over all assets except cash, to value the assets at their book value less 10 per cent except goodwill which was to be valued at 4 years purchase of the excess of average (five years) profits over 8 per cent of the combined amount of share capital and reserves.

(ii) Strong Limited to take over trade creditors, which were subject to a discount of five per cent. Other outside liabilities were discharged by strong Limited at their book values.

(iii) The purchase consideration was to discharged in cash to the extent of ₹10,000 and the balance in fully paid equity shares of ₹10 each valued at ₹12.50 per share.

(iv) The average of five years profits was ₹30100. the expenses of liquidation amounted to ₹4000. weak Limited had sold prior to 30th June, 1976 goods costing ₹30,000 to strong Limited for ₹40,000. Debtors include ₹20,000 still due from strong Limited on the date of absorption, ₹25,000 worth of the goods were still in stocks of strong Limited. Show the important ledger accounts in the books of weak Limited and journal entries in the books of strong Limited.

QUESTION 27 (STUDY MATERIAL

Balance Sheets of Ax Ltd. and Tx Ltd. as on 31.12.1999. Tx Ltd. was merged with Ax Ltd. with effect from 1.1.2000 and merger was in the nature of purchase:

BALANCE SHEET AS ON 31.12.1999

	AX Ltd.	TX Ltd.		AX Ltd.	TX Ltd.
Share capital	7,00,000	2,50,000	Fixed assets	9,50,000	4,00,000
(₹10each)			Investments	2,00,000	50,000
General reserve	3,50,000	1,20,000	(non trade)		
Profit and Loss			stock	1,20,000	50,000
Account	2,10,000	65,000	Debtors	75,000	80,000
Export reserve	70,000	40,000	Advance tax	80,000	20,000
12% debentures	1,00,000	1,00,000	Cash and bank	2,75,000	1,30,000
Creditors	40,000	45,000	Preliminary exp.	10,000	-
Tax provision	1,00,000	60,000			
Proposed dividend	1,40,000	50,000			
	17,10,000	7,30,000		17,10,000	7,30,000

Ax Ltd. would issue 12% debentures to discharge the claims of the debentures holders of Tx Ltd. at par. Non trade investments of Ax Ltd. fetched @ 25% while those of Tx Ltd. fetched @ 18% profit (pre tax) by Ax Ltd. and Tx Ltd. during 1997, 1998 and 1999 and were as follows:

	AX Ltd.	TX Ltd.
1997	5,00,000	1,50,000
1998	6,50,000	2,10,000
1999	5,75,000	1,80,000

Goodwill may be calculated on the basis of capitalization method taking 20% as the pre tax normal rate of return. Purchase consideration is discharged by Ax Ltd. on the basis of intrinsic value per share. The company decided to cancel the proposed dividend. Prepare Balance Sheet of Ax Ltd after taking over the business.

QUESTION. 28 (C A FINAL MAY 2008 16 MARKS)

T. Ltd. and V. Ltd. propose to amalgamate. Their balance sheets as at 31st March, 2008 were as follows:

Liabilities	T. Ltd.	V. Ltd.	Assets	T. Ltd.	V Ltd.
Share capital:			Fixed Assets:		
Equity shares of 10 each	15,00,000	6,00,000	Less: Dep.	12,00,000	3,00,000
General reserve	6,00,000	60,000	Investment (face value of ₹3 Lakhs, 6% tax free G.P. notes)	3,00,000	
Profit & Loss A/c.	3,00,000	90,000			
Creditors	3,00,000	1,50,000			
			Stock	6,00,000	3,90,000
			Debtors	5,10,000	1,80,000
			Cash and Bank Balances	90,000	30,000
	27,00,000	9,00,000		27,00,000	9,00,000

Their net profits (after taxation) were as follows:

Year	T. Ltd.	V. Ltd.
2005-06	3,90,000	1,35,000
2006-07	375,000	1,20,000
2007-08	4,50,000	1,68,000

Trading Profit may be considered as 15% on closing capital invested. Goodwill may be taken as 4 years purchase of average super profits. The stock of T. Ltd. are to be taken at ₹ 6,12,000 and ₹ 4,26,000 respectively for the purpose of amalgamation. W. Ltd. is formed for the purpose of amalgamation of two companies.

(a) Suggest a scheme of capitalization of W. Ltd. and ratio of exchange of shares; and

(b) Draft the opening balance sheet of W. Ltd.

SOLUTION:

(a) Scheme of capitalization of W. Ltd. and radio of exchange of shares Computation of Net Assets of amalgamating companies.

	T. Ltd.	V. Ltd.
Goodwill (W.N.2)	3,19,200	1,21,200
Fixed Assets	12,00,000	3,00,000
6% investments (Non-trade)	3,00,000	
Stock	6,12,000	4,26,000
Debtors	5,10,000	1,80,000
Cash and Bank Balances	90,000	30,000
	30,31,200	10,57,200
Less: Creditors	3,00,000	1,50,000
Net Assets	2731,200	9,07,200
	1,50,000	60,000
No. of equity shares	18,208	15.12
Intrinsic Value of a share		
No. of shares to be issued by W. Ltd. to T. Ltd. 1,50,000 x 18,208/10	2,73,120 Shares	
V. Ltd. 60,000 x 15.12/10		90,720 Shares

In total 2,73,120 + 90,720 i.e. 3,63,840 shares will be issued by W. Ltd. Ratio by exchange of shares will be as follows:

1. Holders of 1,50,000 equity shares of T.Ltd. will get 2,73,120 shares in W. Ltd.
2. Similarly, holders, of 60,000 equity shares of V. Ltd. will get 90,720 shares in W.Ltd.

(b) Opening Balance Sheet of W. Ltd.

Particulars	Note No.	`
1. Equity and Liabilities		
(1) Shareholder's Funds		
Share Capital	1	36,38,400
(2) Current Liabilities		
Trade payable (3,00,000 + 1,50,000)		4,50,000
Total		40,88,400

II. Assets		
(1) Non-current assets		
(a) Fixed Assets		
i. Tangible assets	2	15,00,000
ii. Intangible assets	3	4,40,000
(b) Non-current Investments	4	3,00,000
(b) Current Assets		
(a) Inventories (6,12,000+4,26,000)		10,38,000
(b) Trade receivables (5,10,000+1,80,000)		6,90,000
(c) Cash and Cash equivalents (90,000 + 30,000)		1,20,000
Total		40,88,400

Notes to Accounts

1.	Share Capital Equity share capital 3,63,840 Equity shares of ` 10 each (Issued for consideration other than cash, pursuant to scheme of amalgamation)	36,38,400
2.	Tangible Assets Other Fixed Assets (` 12,00,000+` 3,00,000)	15,00,000
3.	Intangible assets Goodwill (W.N.2) (` 3,19200+` 1,21,200)	4,40,000
4.	Non-current Investments Investments in 6% Tax Free G.P. Notes	3,00,000

Working Notes:

1. **Calculation of closing trading capital employed on the basis of net assets.**

Particulars	T Ltd.	V. Ltd.
Fixed Assets	12,00,000	3,00,000
Stock	6,12,000	4,26,000
Debtors	5,10,000	1,80,000
Cash and Bank Balances	90,000	30,000
	24,12,000	9,36,000
Less: Creditors	3,00,000	1,50,000
	21,12,000	7,86,000
Net Assets		

2. **Calculation of Value of goodwill**

(i) Average Trading Profit	T Ltd.	V Ltd.
2005-06	3,90,000	1,35,000
2006-07	3,75,000	1,20,000
2007-08	4,50,000	1,68,000
Profit after tax	12,15,000	4,23,000
Profit before tax (40%)	20,25,000	7,05,000
Add: Under Valuation of closing stock	12,000	36,000
	20,37,000	7,41,000
Average of 3 Years Profit before tax	6,79,000	2,47,000
Less: Income from non-trade investments		
(3,00,000 x 6%)	18,000	--
Average profit before tax	6,61,000	2,47,000
Less: 40% tax	2,64,400	98,800
Average profit after tax	3,96,600	1,48,200

(ii) Super Profits	3,96,600	1,48,200
Average trading profit		
Less Normal Profit		
T. Ltd. Rs 21,12,000 x 15%	3,16,800	
V. Ltd. ₹ 7,86,000 x 15%		1,17,900
	79,800	30,300
(iii) Value of goodwill at 4 years purchase of super Profits	3,19,200	1,21,200

DISSENTING SHAREHOLDERS

QUESTION 29 (DISSENTING SHAREHOLDERS)

Modern Ltd. agrees to acquire the business of the simple cotton Ltd. on the basis of the following Balance Sheet:

Liabilities	Amount	Assets	Amount
10,000 shares of ₹50, 30 paid up	3,00,000	Freehold property	1,25,000
		Plant and machinery	25,000
Reserve fund	62,500	Stock	1,50,000
Profit and loss account	30,000	Investments	5,000
Creditors	37,500	Debtors	1,00,000
		Bank	25,000
	4,30,000		4,30,000

Modern Ltd. took over all the assets and liabilities of the vendor company. A sum of ₹7,500 was retained by the vendor company for the payment of expenses of liquidation, income tax liability and settlement for dissenting shareholders.

Vendor Company was allotted one share of ₹100 each, ₹50 paid up for two shares held by its shareholders. Out of the amount of ₹7500 retained by the liquidator of Simple Cotton Ltd. payments were made as under:

Cost of liquidation ₹1250, tax ₹3750 and dissenting shareholders holding 50 shares @ ₹32.50 per share i.e., ₹1625. the market value of the share of the Modern textile Ltd. was ₹60 per share.

Prepare necessary books.

QUESTION. 30 (CA FINAL NOV.2013 16 MARKS)

Following is the Extract of Balance Sheet of M/s. Sunny Ltd. and Money as on 31.03.2013:

Balance Sheet Extract as on 31.03.2013

	Sunny Ltd.	Money Ltd.
Authorised Share Capital	15,00,000	5,00,000
Equity Share Capital of ₹10 each fully paid	8,00,000.00	2,00,000.00
General Reserve	1,10,000.00	45,000.00

Profit & Loss Account	42,000.00	18,000.00
Statutory Fund	16,000.00	8,000.00
Trade Payable	45,000.00	24000.00
Provisions	95,000.00	12000.00
	11,08,000.00	3,07,000.00
Goodwill	20,000.00	0.00
Machines & Plant	5,10,000.00	1,95,000.00
Other fixed Assets	90,000.00	15,000.00
Current Assets		
Inventories	1,85,000.00	35,000.00
Debtors	1,00,500.00	35,000.00
Prepaid expenses	24,500.00	2,000.00
Cash in Hand & Bank	1,78,000.00	25,000.00
	11,08,000.00	3,07,000.00

The two companies have entered into a scheme of Amalgamation and a new company Z Ltd. is formed. The Amalgamation is to take place in the following manner:

(1) For the purpose of Amalgamation a new Company Z is to be formed with an authorized Share Capital of 2,50,000 equity shares of s.10 each.

(2) Z Ltd. is issue fully paid shares to the shareholders of Sunny Ltd. and Money Ltd. at a price of ₹ 5 and ₹ 3 above the intrinsic value of the shares respectively.

(3) The scheme or amalgamation was not supported by 100 shareholders of Sunny Ltd. and had to be paid ₹ 10 per share above intrinsic value as consideration. The amount of the dissenting shareholders was borne by Z Ltd.

(4) Fixed Assets of Sunny Ltd. were last revalued in the year 2009 after which there has been an increase of 15% in the values, while assets of Money Ltd. have not shown any change in prices. The current assets of Money Ltd. include Debtors of ₹20,000 which are considered bad.

(5) Money Ltd.'s Stock-in-trade as on 31.03.2013 includes stock of s.25,000 purchased from Sunny Ltd. at a profit of 25% on cost price.

(6) The Statutory Fund of the companies is to be maintained by Z Ltd. for a period of 3 years.

(7) Sunny Ltd. had declared dividend of 10% on 31.03.2013 which has still not been paid.

(8) Goodwill shown in books of Sunny Ltd. was considered to be worthless.

(9) All the assets of the companies are taken over by Z Ltd. at the revalued amounts, Liabilities have to be paid in full.

Calculate the purchase consideration paid by Z to the shareholders of both the companies and prepare the Balance Sheet of Z Ltd. as per revised Schedule VI after the Amalgamation (Notes to Balance Sheet need not form part of the answer).

ANSWER

Calculation of Net Assets	Sunny Ltd.		Money Ltd.	
Goodwill (given to be of nil value)				
Machines and Plant	510,000		1,95,000	
Other Fixed Assets	90,000		15,000	2,10,000
	6,00,000			
Add: 15% increase in price	90,000	6,90,000		
Current Assets				
Inventories		1,85,000	35,000	30,000
Less: Loading on Stock			5,000	
(25,000x25/125)				
Debtors		1,00,500	35,000	
Less: Debtors considered bad			20,000	15,000
Prepaid expenses	1,78,000	24,500		2,000
Cash in Hand & Bank				
Less: Payment of Dividend	(80,000)	98,000		25,000
(10% of ₹ 8,00,000)				
Value of Total Assets		10,98,000		2,82,000
Less: Liabilities				
Trade Payables		45,000		24,000
Provisions	95,000	15,000		12,000
Less: Proposed dividend	(80,000)			
paid and adjusted in cash				
(assumed that proposed dividend was included in provisions)		10,38,000		2,46,000

WORKING NOTES:

1. Calculation of Intrinsic Value of Shares

	Sunny Ltd.	Money Ltd.
Net Assets value as on 31.03.2013	10,38,000.00	2,46,000.00
No. of shares of the Company	80,000.00	20,000.00
Intrinsic Value of shares	12.975	12.30

2. Calculation of Purchase Consideration

	Sunny Ltd.	Money Ltd.
Intrinsic Value of Shares	12.975	12.30
Premium to be paid by Z Ltd.	5.00	3.00
Amount to be paid per share	17,975	15.30
No. of shareholders agreeing to amalgamation	79,900	20,000
Total amount to be paid by Z Ltd.	14,36,202	3,06,000
No. of shares to be issued by Z Ltd. ₹10 per share (₹ 2 paid in cash)	1,43,620	30,600
Total Number of equity shares	1,74,220	
Payment to dissenting shareholders (100 shares x 22.98)	2,298	
Total purchase consideration	14,38,500	3,06,000

Entries in Books of Z Ltd.

Business Purchase A/c.	Dr.	1,744,500	
To Liquidators of Sunny Ltd.			14,38,500
To Liquidators of Money Ltd.			3,06,000
(Being the purchase of Sunny Ltd. and Money Ltd.)			
Fixed Assets	Dr.	900,000	
Inventories	Dr.	2,15,000	

Debtors	Dr.	1,15,500	
Prepaid Expenses	Dr.	26,500	
Cash & Bank	Dr.	1,23,000	
Goodwill (balancing figure)	Dr.	4,60,000	
To Trade Payables			69,000
To Provisions			27,000
To Business Purchase A/c.			17,44,500
(Being the assets and liabilities of the companies taken over at revalued values)			
Liquidators of Sunny Ltd.	Dr.	14,38,500	
Liquidators of Money Ltd.	Dr.	3,06,000	
To Equity Shares Capital A/c.			17,42,200
To Cash A/c.			2,300
Amalgamation Adjustment A/c.	Dr.	24,000	
To Statutory Funds			24,000
(Being the statutory reserves of Sunny and Money Ltd.)			

Balance Sheet of Z Ltd. as on 31st March, 2013

	Note No.	
Equity and Liabilities		
Shareholders' Funds		
(a) Share Capital		1742,200
(b) Reserves and surplus		
Statutory Funds		24,000
Non-Current Liabilities		-
Long term borrowings		

Current Liabilities		
(a) Trade Payables		69,000
(b) Other Current Liabilities		
(c) Short term provisions		27,000
Total		18,62,200
Non-Current Assets		
(a) Fixed Assets		9,00,000
(i) Tangible Assets		4,60,500
(Ii) Intangible Assets		24,000
Current Assets		
(a) Inventories		2,15,000
(b) Trade Receivables		1,15,500
(c) Cash and Bank Balances		1,210,700
(d) Short-term loans and advances		26,500
Total		18,62,200

STATUTORY RESERVES IN BALANCE SHEET OF VENDOR COMPANY

QUESTION 31 (CA FINAL MAY 1996)

A Limited and B Limited were amalgamated on and from 1st April 1995. A new company C Limited was formed to take over the business of the existing companies. The Balance Sheets of A Limited and B Limited as on 31st March 1995 are given below:

(₹ In lakhs)

Liabilities	A Limited	B Limited	Assets	A Limited	B Limited
Share capital			Fixed Assets		
Equity shares of ₹100 each	800	750	Land and Building	550	400
			Plant and Machinery	350	250
12% Preference shares of ₹100	300	200	Investment	150	50
Reserve and Surplus:			Current assets, Loans and Advances		
Revaluation Reserve	150	100	Stock	350	250
General Reserve	170	150	Sundry Debtors	250	300
Investment Allowance Reserve	50	50	Bills receivable	50	50
Profit and Loss a/c	50	30	Cash and bank	300	200
Secured Loans:					
10% Debentures (₹100 each)	60	30			
Current Liabilities and Provisions:					
Sundry Creditors	270	120			
Bills Payable	150	70			
	2,000	1,500		2,000	1,500

Additional information:

(i) 10% Debenture-holders of A Limited and B Limited are discharged by C Limited issuing such number of its 15% Debentures of ₹100 each so as to maintain the same amount of interest.

(ii) Preference shareholders of the two companies are issued equivalent number of 15% preference shares of C Limited at a price of ₹150 per share (face value ₹100)

(iii) C Limited will issue 5 equity shares for each equity share of A Limited and 4 equity shares for each equity shares of B Limited. The share are to be issued @ ₹30 each, having a face value of ₹10 per share.

(iv) Investment allowance reserve is to be maintained for 4 more years

Prepare the Balance Sheet of C Limited as on 1st April 1995 after the amalgamation has been carried out on the basis of amalgamation in the nature of purchase.

BUSINESS COMBINATION IN THE NATURE OF MERGER (POOLING INTEREST METHOD)

QUESTION 32 (BASED ON MERGER)

A Limited and B Limited were amalgamated on and from 1st April, 1999. A new company AB Limited was formed to take over the business of existing companies. The Balance Sheet of A Limited and B Limited as on 31st March 1999 are given below:

	A Limited	B Limited		A Limited	B Limited
Equity shares of ₹10 each	2,400	1,600	Fixed assets	4,800	3,200
12% Preference shares of ₹100 each	1,200	800	Less: Depreciation	800	600
				4,000	2,600
Capital reserve	800	600	Investments	1,600	600
General reserve	1,200	600	Stock	1,200	600
Profit and Loss a/c	400	200	Debtors	1,600	800
Secured loans	1,600	800	Cash and bank balance.	1,200	600
Trade creditors	1,200	400			
Tax provision	800	200			
	9,600	5,200		9,600	5,200

Other information:

(i) Preference shareholders of the two companies are issued equivalent number of 15% preference shares of AB Limited at an issue price of ₹125 per share.

(ii) AB Limited will issue one equity share of ₹10 each for every share of A Limited and B Limited. The shares are issued at a premium of ₹5 per share. Prepare the Balance Sheet of AB Limited on the assumption that the Amalgamation is in the nature of merger.

QUESTION 33 (C.A.FINAL MAY 2001)

Alpha Limited and Beta Limited were amalgamated on and from 1st April 2001. A new company Gamma Limited was formed to takeover the business of the existing companies. The Balance Sheets of Alpha Limited and Beta Limited as on 31st March 2001 are given below:

(₹ In lakhs)

Liabilities	Alpha Limited	Beta Limited	Assets	Alpha Limited	Beta Limited
Share capital			Fixed Assets	1,200	1,000
Equity shares of ₹100 each	1,000	800	Current Assets, Loans and Advances	880	565
15% Preference shares of ₹100 each	400	300			
Reserve and Surplus:					
Revaluation Reserve					
General Reserve	100	80			
Profit and Loss a/c	200	150			
Secured Loan	80	60			
12% Debentures of ₹100 each	96	80			
Current Liabilities and Provisions	204	95			
	2,080	1,565		2,080	1,565

Other information:

(i) 12% Debenture holders of Alpha Limited and Beta Limited are discharged by Gamma Limited by issuing adequate number of 16% Debentures of ₹100 each to ensure that they continue to receive the same amount of interest.

(ii) Preference shareholders of Alpha Limited and Beta Limited have received same number of 15% preference shares of ₹100 each of Gamma Limited

(iii) Gamma Limited has issued 1.5 equity shares of each equity share of Alpha Limited and 1 equity share for each equity share of Beta Limited. The face value of shares issued by Gamma Limited is ₹100 each.

Prepare the Balance Sheet of Gamma Limited as on 1st April 2001 after the amalgamation has been carried out using the "pooling of interest method".

PAST EXAMINATION QUESTIONS FOR SELF READING

QUESTION 34 (CA INTER MAY 2019) (10 MARKS)

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

Particulars	VT Ltd. (₹)	MG Ltd. (₹)
Equity and Liabilities		
Equity Shares of ₹ 10 each	12,00,000	6,00,000
10% Pref. Shares of ₹ 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. (₹)	MG Ltd. (₹)
Trade Receivable		
Debtors	7,20,000	3,80,000
Bills Receivable	1,20,000	40,000
	8,40,000	4,20,000
Trade Payables		
Sundry Creditors	4,40,000	2,50,000
Bills Payable	60,000	50,000
	5,00,000	3,00,000

Fixed Assets of both the companies are to be revalued at 15% above book value. Inventory in Trade and Debtors are taken over 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 ₹ 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 ₹ 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) ₹ 60,000 is to be paid by VT Ltd. to MG Ltd. for Liquidation expenses.

(v) Sundry Debtors of MG Ltd. includes ₹ 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 :

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

		Dr. ₹	Cr. ₹
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 ₹ 5,00,000)	Dr.	5,75,000	
Inventory (95% of ₹ 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	
(₹ 80,000 –₹ 60,000 dividend paid)			
To Provision for Bad Debts (5% of ₹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 and difference of net assets and 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. (₹ 3,00,000 × 108%)	Dr.	3,24,000	
Discount on Issue of Debentures	Dr.	36,000	
To 12% Debentures			3,60,000
(Allotment of 12% Debentures to debenture holders of MG Ltd. at a discount of 10%)			

Sundry Creditors	Dr.	20,000	
To Sundry Debtors			20,000
(Cancellation of mutual owing)			
Goodwill	Dr.	60,000	
To Bank			60,000
(Being liquidation expenses reimbursed to MG Ltd.)			
Capital Reserve/P&L A/c	Dr.	60,000	
To Goodwill			60,000
(Being goodwill set off)			

(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 ₹ 10 each i.e. For 10% preference shares, to be paid at 10% discount	₹ 8,00,000	(i)
₹ 2,00,000x 90/100	₹ 1,80,000	(ii)
Consideration amount [(i) + (ii)]	₹ 9,80,000	

QUESTION 35 (CA INTER NOV 2018) (5MARKS)

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

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

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

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

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

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

SOLUTION:

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

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

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

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

QUESTION 36 (CA INTER NOV 2020) (15MARKS)

High Ltd. and Low Ltd. were amalgamated on and from, 1st April, 2020. A new company Little Ltd. was formed to take over the business of the existing Companies. The summarized Balance sheets of High Ltd. and Low Ltd. as on 31st March, 2020 are as under:

(₹ in Lakhs)

Liabilities	High Ltd.	Low Ltd.	Assets	High Ltd.	Low Ltd.
Share Capital:			Property, Plant and Equipment:		
Equity Shares of ₹ 100 each	1000	850	Land & Building	670	385
14% Pref Shares of	320	175	Plant & Machinery	475	355
₹ 100 each					
Reserves & Surplus:			Investments	95	80
Revaluation Reserve	225	110	Current Assets:		
General Reserve	360	240	Stock	415	389
Investment Allowance Reserve	80	40	Sundry Debtors	322	213
P & L Account	85	82	Bills Receivables	35	-
Non-Current Liabilities:			Cash & Bank	303	166
Secured Loans:					
13% Debentures	100	56			
(₹ 100 each)					
Unsecured Loans (Public Deposits)	50	-			
Current Liabilities & Provisions:		-			
Sundry Creditors	65	35			
Bills Payable	30	-			
TOTAL	2315	1588	TOTAL	2315	1588

Other Information:

(1) 13% Debenture holders of High Ltd. & Low Ltd. are discharged by Little Ltd. by issuing such number of its 15% Debentures of ₹ 100 each so as to maintain the same amount of interest.

(2) Preference Shareholders of the two companies are issued equivalent number of 15% Preference shares of Little Ltd. at a price of ₹ 125 per share (Face Value ₹ 100)

(3) Little Ltd. will issue 4 Equity Shares for each Equity Share of High Ltd. & 3 equity shares for each Equity Share of Low Ltd. The shares are to be issued at ₹ 35 each having a face value of ₹ 10 per share.

(4) Investment Allowance Reserve is to be maintained for two more years.

Prepare the Balance sheet of Little Ltd. as on 1st April, 2020 after the amalgamation has been carried out in basis of in the nature of Purchase.

SOLUTION:

Balance Sheet of Little Ltd. as at 1st April, 2020

Particulars	Note No.	(₹ in lakhs)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	1,150.0
(b) Reserves and Surplus	2	2,437.8
(2) Non-Current Liabilities		
Long-term borrowings	3	135.2
Other Borrowings- Unsecured Loans		50
(3) Current Liabilities		
Trade payables	4	130.0
Total		3,903
II. Assets		
(1) Non-current assets		
(a) Property, Plant and Equipment	5	1,885
(b) Non-current investment (95 + 80)		175
(2) Current assets		
(a) Inventory (415+389)		804
(b) Trade receivables	6	570
(c) Cash and bank balances (303 + 166)		469
Total		3,903

Notes to Accounts

			(₹ in lakhs)	(₹ in lakhs)
1.	Share Capital			
	Equity share capital (W.N.1)			
	65,50,0001 Equity shares of 10 each		655	
	4,95,0002 Preference shares of ₹ 100 each		495	
	(all the above shares are allotted as fully paid-up pursuant to contracts without payment being received in cash)			1,150
2.	Reserves and surplus			
	Securities Premium Account (W.N.3) (1080+ 681.25)		1,761.25	
	Capital Reserve (W.N. 2)(283.33 + 393.22)		676.55	
	Investment Allowance Reserve (80 + 40)		120	
	Amalgamation Adjustment Reserve (80 + 40)		(120)	2,437.8
3.	Long-term borrowings			
	15% Debentures			135.2
4.	Trade payables			
	Sundry Creditors: High Ltd.		65	
	Low Ltd.		35	
	Bills Payable: High Ltd.		30	130
5.	Property, Plant and Equipment			
	Land and Building : High Ltd	670		
	Low Ltd	385	1055	
	Plant and Machinery: High Ltd.	475		
	Low Ltd.	355	830	1,885
6.	Trade receivables			
	Sundry Debtors: High Ltd.		322	
	Low Ltd.		213	
	Bills Receivables: High Ltd.		35	570

Working Notes:

(₹ in lakhs)

			High Ltd.		Low Ltd.
(1)	Computation of Purchase consideration				
	(a) Preference shareholders				
	($\frac{3,20,00,000}{100}$ i.e. 3,20,000 shares × ₹ 125 each)		400		
	($\frac{1,75,00,000}{100}$ i.e. 1,75,000 shares × ₹ 125 each)				218.75
(b)	Equity shareholders :				
	($\frac{10,00,00,000 \times 4}{100}$ i.e. 40,00,000 shares × ₹ 35 each)		1,400		
	($\frac{8,50,00,000 \times 3}{100}$ i.e. 25,50,000 shares × ₹ 35 each)				892.50
	Amount of Purchase Consideration		1,800		1,111.25
	Assets taken over				
	Land and Building		670		385
	Plant and Machinery		475		355
	Investments		95		80
	Inventory		415		389
	Trade receivables		322		213
	Bills Receivables		35		
	Cash and bank		303		166
			2,315		1,588
	Less : Liabilities taken over				
	Debentures	86.67		48.53	
	Unsecured Loan	50			
	Creditors	65		35	
	Bills Payable	30			
			213.67		83.53

	Net assets taken over	2083.33	1,504.47
	Purchase consideration	1,800	1,111.25
	Capital reserve	283.33	393.22
(3)	Computation of securities premium		
	On preference share capital		
	High Ltd. – 3,20,000 x 25	80	
	Low Ltd. – 1,75,000 x 25		43.75
	On equity share capital		
	High Ltd. – 40,000 x 25	1000	
	Low Ltd. – 25,50,000 x25		637.5
	Total	1080	681.25

QUESTION 37 (CA INTER JAN 21 EXAM) (15 MARKS)

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

		Galaxy Ltd.	**Glory Ltd.**
		₹	₹
(I)	**Equity & Liabilities**		
	(1) Shareholders'fund Share Capital		
	Equity shares of ₹ 10 each	8,40,000	4,55,000
	Reserves & Surplus		
	General Reserve	4,48,000	40,000
	Profit & Loss A/c	1,12,000	72,000
	(2) Non-current Liabilities Secured Loan		
	6% Debentures	—	3,30,000

	(3) Current Liabilities		
	Trade Payables	4,20,000	1,83,000
	Total	18,20,000	10,80,000
(II)	**Assets**		
	(1) Non-current assets Property, Plant & Equipment		
	Freehold property, at cost	5,88,000	3,36,000
	Plant & Machinery, at cost less depreciation	1,40,000	84,000
	Motor vehicles, at cost less depreciation	56,000	-
	(2) Current Assets		
	Inventories	3,36,000	4,38,000
	Trade Receivables	4,62,000	1,18,000
	Cash at Bank	2,38,000	1,04,000
	Total	18,20,000	10,80,000

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

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

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

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

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

You are required to :

(1) Compute the number of shares to be issued to the shareholders of Galaxy Ltd. and Glory Ltd, assuming the nominal value of each share in Glorious Ltd. is ₹ 10.

(2) Prepare Balance Sheet of Glorious Ltd., as on 1st April, 2020 and also prepare notes to the accounts as per Schedule III of the Companies Act, 2013.

SOLUTION:

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

	Galaxy Ltd.	Glory Ltd.
Purchase Consideration:	₹	₹
Goodwill	4,48,000	1,68,000
Freehold property	5,88,000	3,36,000
Plant and Machinery	2,52,000	84,000
Motor vehicles	56,000	-
Inventory	3,36,000	4,38,000
Trade receivables	4,62,000	-
Cash at Bank	2,38,000	24,000
	23,80,000	10,50,000

Less: Liabilities:		
6% Debentures (3,00,000 x 110%)	-	(3,30,000)
Trade payables	(4,20,000)	7,20,000
Net Assets taken over	19,60,000	72,000
To be satisfied by issue of shares of Glorious. Ltd. @ ₹ 10 each	1,96,000	

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

		Particulars	Note No	Amount
				₹
		EQUITY AND LIABILITIES		
1		Shareholders' funds		
	(a)	Share capital	1	26,80,000
	(b)	Reserves and surplus	2	30,000
2		Non-current liabilities		
	(a)	Long-term borrowings	3	3,00,000

3		Current liabilities		
	(a)	Trade payables		4,20,000
		Total		34,30,000
		ASSETS		
1		i Non-current assets		
	(a)	Property, plant and equipment	4	13,16,000
		Intangible assets	5	6,16,000
2		ii Current assets		
	(a)	Inventories	6	7,74,000
	(b)	Trade receivables		4,62,000
	(c)	Cash and cash equivalents	7	2,62,000
		Total		34,30,000

Notes to accounts:

		₹	₹
1.	Share Capital Equity		
	share capital 2,68,000 shares of ₹ 10 each (All the above shares are issued for consideration other than cash)		26,80,000
2.	Reserves and surplus		
	Securities Premium (10% premium on debentures of ₹3,00,000) Long-term borrowings		30,000
3.	Secured 8% 3,000 Debentures of ₹ 100 each Property Plant and Equipment		3,00,000
4.	Freehold property		
	Galaxy Ltd.	5,88,000	
	Glory Ltd.	3,36,000	9,24,000

	Plant and Machinery		
	Galaxy Ltd.	2,52,000	
	Glory Ltd.	84,000	3,36,000
	Motor vehicles - Galaxy Ltd.		56,000
			13,16,000
5	Intangible assets Goodwill		
	Galaxy Ltd.	4,48,000	
	Glory Ltd.	1,68,000	6,16,000
6	Inventories		
	Galaxy Ltd.	3,36,000	
	Glory Ltd.	4,38,000	7,74,000
7	Cash and cash equivalents		
	Galaxy Ltd.	2,38,000	
	Glory Ltd. (As per working note)	24,000	2,62,000

Working note:

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

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

Note:

1. It is assumed that the nominal value of debentures of Glory Ltd. is ₹ 100 each.
2. As per the information given in the question, debentures of Glory Ltd. are to be discharged by the issue of debentures of Glorious Ltd. at premium of 10%. It is assumed in the above solution that the debentures are issued at premium of ₹ 10 for discharge of debentures of ₹ 3,30,000. Alternative answer considering other reasonable assumption is also possible.

QUESTION 38 (CA INTER JULY 2021 EXAMS : 10 MARKS)

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

Particulars	Notes	Black Limited (₹ In 000)	White Limited (₹ In 000)
Equity and Liabilities			
Shareholders' Funds			
(a) Share Capital	1	6,000	3,600
(b) Reserves and Surplus	2	1,080	660
Current Liabilities			
Trade payables		600	360
Total		7,680	4,620
Assets			
Non-current assets			
Property, Plant and Equipment		3,600	2,400
Current assets			
(a) Inventories		960	720
(b) Trade receivables		1,680	1,080
(c) Cash and Cash Equivalents		1,440	420
Total		7,680	4,620

Note No.	Particulars	Black Limited (₹ in 000)	White Limited (₹ in 000)
1.	Share Capital	6,000	3,600
	Equity Shares of ₹ 100 each		
2.	Reserves and Surplus		
	General Reserve	360	180
	Profit and Loss Account	720	480
	Total	1,080	660

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

No Balance Sheet of White Limited is available as on that date. It is, however estimated that White Limited earned profit of ₹ 2,40,000 after charging proportionate depreciation @ 10% p.a. on Property Plant and Equipment, during April-June, 2020.

Estimated profit of Black Limited during these 3 months was ₹ 4,80,000 after charging proportionate depreciation @ 10% p.a. on Property Plant and Equipment.

Both the companies have declared and paid 10% dividend within this 3 months' period.

Goodwill of White Limited is valued at ₹ 2,40,000 and Property Plant and Equipment are valued at ₹ 1,20,000 above the depreciated book value on the date of takeover.

Purchase consideration is to be satisfied by Black Limited by issuing shares at par. Ignore income tax. You are required to:

(i) Compute No. of shares to be issued by Black Limited to White Limited against purchase consideration.

(ii) Calculate the balance of Net Current Assets of Black Limited and White Limited as on 1st July, 2020.

(iii) Give balance of Profit or Loss of Black Limited as on 1st July, 2020

(iv) Give balance of Property Plant and Equipment as on 1st July, 2020 after takeover.

SOLUTION :

(i) No. of shares issued by Black Ltd. to White Ltd. against purchase consideration

White Ltd.	₹	₹
Goodwill		2,40,000
Property, plant and equipment	24,00,000	
Less: Depreciation [24,00,000 × 10 % × 3/12]	(60,000)	
	23,40,000	

Add: Appreciation		1,20,000	24,60,000
Inventory			7,20,000
Trade receivables			10,80,000
Cash and Bank balances		4,20,000	
Add: Profit after depreciation	2,40,000		
Add: Depreciation (non-cash)	60,000	3,00,000	
Less: Dividend [36,00,000 × 10%]		(3,60,000)	3,60,000
			48,60,000
Less: Trade payables			(3,60,000)
Purchase Consideration			45,00,000
Number of shares to be issued by Black Ltd. @ ₹ 100 each			45,000 shares

(ii) Calculation of Net Current Assets as on 01.07.2020

		Black Ltd.		White Ltd.
	₹	₹		₹
Current assets:				
Inventory		9,60,000		7,20,000
Trade receivables		16,80,000		10,80,000
Cash and Bank	14,40,000		4,20,000	
Less: Dividend	(6,00,000)		(3,60,000)	
Add: Profit after depreciation	4,80,000		2,40,000	
Add: Depreciation being non cash	90,000	14,10,000	60,000	3,60,000
		40,50,000		21,60,000
Less: Trade payables		(6,00,000)		(3,60,000)
		34,50,000		18,00,000

(iii) Profit and Loss Account balance of Black Ltd. as on 1.07.2020

	₹
P & L A/c balance as on 31.03.2020	7,20,000
Less: Dividend paid	(6,00,000)
	1,20,000
Add: Estimated profit for 3 months after charging depreciation	4,80,000
	6,00,000

(iv) Property, plant and equipment as on 01.07.2020

Property, plant and equipment of Black Ltd. as on 31.03.2020		36,00,000
Less: Depreciation for 3 months [36,00,000 x 10% x 3/12]		(90,000)
Property, plant and equipment of White Ltd. Taken over as on 31.03.2020	24,00,000	35,10,000
Less: Proportionate depreciation for 3 months on fixed assets	(60,000)	
	23,40,000	
Add: Appreciation above the estimated book value	1,20,000	24,60,000
Total Property, plant and equipment as on 1.7.2020		59,70,000

QUESTION 39 (CA INTER DEC. 2021 EXAMS : 5 MARKS)

Moon Limited is absorbed by Sun Limited; the consideration, being the takeover of liabilities, the payment of cost of absorption not exceeding ₹ 10,000 (actual cost ₹ 9000); the payment of 9% Debentures of ₹ 50,000 at a premium of 20% through 8% debentures issued at a premium of 25% of face value; the payment of ₹ 18 per share in cash; allotment of two 11% preference shares of ₹ 10/- each and one equity share of ₹ 10/- each at a premium of 30% fully paid for every three shares in Moon Limited respectively.

The number of shares of the vendor company is 1,50,000 of ₹ 10/- each fully paid. Calculate purchase consideration as per AS-14.

SOLUTION :

As per AS 14 "Accounting for Amalgamations", the term consideration has been defined as the aggregate of the shares and other securities issued and the payment made in the form of cash or other assets by the transferee company to the shareholders of the transferor company.

Purchase consideration will be:

	₹	**Form**
Equity shareholders:		
1,50,000 × ₹ 18	27,00,000	Cash
1,50,000 × 2/3 × ₹ 10	10,00,000	11% Pref. shares
1,50,000 × 1/3 × ₹ 13	6,50,000	Equity shares
	43,50,000	

Note:

1. According to AS 14, 'consideration' excludes the any amount payable to debenture-holders. The liability in respect of debentures of vendor company will be taken by transferee company, which will then be settled by issuing new debentures.
2. Liquidation expenses will also not form part of purchase consideration.

QUESTION 40 (CA INTER DEC. 2021 EXAMS : 15 MARKS)

Dark Ltd. and Fair Ltd. were amalgamated on and from 1st April, 2021. A new company Bright Ltd. was formed to take over the business of the existing companies. The balance Sheets of Dark Ltd. and Fair Ltd. as at 31st March, 2021 are given below:

(₹ In Lakhs)

	Particulars	Note No.	Dark Ltd.	Fair Ltd.
I	**Equity and Liabilities**			
	(1) Shareholders' Funds			
	(a) Share Capital	1	1,650	1,425
	(b) Reserves and Surplus	2	630	495
	(2) Non-Current Liabilities			
	Long Term Borrowings:			
	10% Debentures of 100 ₹ each		90	45
	(3) Current Liabilities			
	Trade Payables		630	285
	Total		3,000	2,250
II	**Assets**			
	(1) Non Current Assets			
	(a) Property, Plant and Equipment		1,350	975
	(b) Non Current Investments		225	75
	(2) Current Assets			
	(a) Inventories		525	375
	(b) Trade Receivables		450	525
	(c) Cash and Cash Equivalents		450	300
	Total		3,000	2,250

Notes to Accounts

		Dark Ltd. (₹ in Lakh)	Fair Ltd. (₹ in Lakh)
1	Share Capital		
	Equity Shares of ₹ 100 each	1, 200	1,125
	14% Preference Shares of ₹ 100 each	450	300
		1,650	1,425
2	Reserves and Surplus		
	Revaluation Reserve	225	150
	General Reserve	255	225
	Investment Allowance Reserve	75	75
	Profit and Loss Account	75	45
		630	495

Additional Information:

(i) Bright Limited will issue 5 equity shares for each equity share of Dark Limited and 4 equity shares for each equity share of Fair Limited. The shares are to be issued @ ₹ 35 each having a face value of ₹ 10 per share.

(ii) Preference shareholders of the two companies are issued equivalent number of 16% preference shares of Bright Limited at a price of ₹ 160 per share (face value ₹ 100).

(iii) 10% Debenture holders of Dark Limited and Fair Limited are discharged by Bright Limited, issuing such number of its 16% Debentures of ₹ 100 each so as to maintain the same amount of interest.

(iv) Investment allowance reserve is to be maintained for 4 more years.

(v) Liquidation expenses are for Dark Limited ₹ 6,00,000 and for Fair Limited ₹ 3,00,000. It is decided that these expenses would be borne by Bright Limited.

(vi) All the assets and liabilities of Dark Limited and Fair Limited are taken over at book value.

(vii) Authorized equity share capital of Bright Limited is ₹ 15,00,00,000 divided into equity share of ₹ 10 each. After issuing required number of shares to the liquidators of Dark Limited and Fair Limited, Bright Limited issued balance shares to public. The issue was fully subscribed.

You are required to prepare Balance Sheet of Bright Limited as at 1st April, 2021 after amalgamation has been carried out on the basis of Amalgamation in the nature of purchase.

SOLUTION :

Balance Sheet of Bright Ltd. as at 1st April, 2021

Particulars	Note No.	(₹ in lakhs)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	2,250
(b) Reserves and Surplus	2	4,200
(2) Non-Current Liabilities		
Long-term borrowings	3	84.375
(3) Current Liabilities		
Trade payables	4	915
Total		7449.375
II. Assets		
(1) Non-current assets		
(a) i. Property, plant and equipment	5	2,325
ii. Intangible assets	6	633.375
(b) Non-current investments	7	300
(2) Current assets		
(a) Inventories	8	900
(b) Trade receivables	9	975
(c) Cash and cash equivalents	10	2316
Total		7449.375

Notes to Accounts

		(₹ in lakhs)	(₹ in lakhs)
1.	Share Capital		
	Authorized Share Capital		
	1,50,00,000 Equity shares of ₹10 each	1500	
	7,50,000 16% Preference Share of 100 each	750	
	Issued: 1,50,00,000 Equity shares of ₹ 10 each	1500	
	(Out of which 1,05,00,000 Shares were Issued for consideration other than cash)		

	7,50,000 16% Preference Shares of 100 each (Issued for consideration other than cash)	750	2,250
2.	Reserves and surplus		
	Securities Premium Account		
	(1,50,00,000 shares ×₹ 25) 3750		
	(7,50,000 shares × ₹ 60) 450	4,200	
	Investment Allowance Reserve	150	
	Amalgamation Adjustment Reserve	(150)	4,200
3.	Long-term borrowings		
	16% Debentures (56,25,000+28,12,500) (W.N. 3)		84.375
4.	Trade payables		
	Dark Ltd.	630	
	Fair Ltd.	285	915
5.	Property, plant & equipment		
	Land and Building	1350	
	Plant and Machinery	975	2,325
6.	Intangible assets		
	Goodwill [W.N. 2] 624.375		
	Add: liquidation exp. (6+3) 9.00		633.375
7.	Non-current Investments		
	Investments (225+75)		300
8.	Inventories		
	Dark Ltd.	525	
	Fair Ltd.	375	900
9	Trade receivables		
	Dark Ltd.	450	
	Fair Ltd.	525	975
10	Cash & cash equivalents		
	Dark Ltd.	450	
	Fair Ltd.	300	
	Liquidation Expenses (6+3)	(9)	
	Shares issued for cash (45 lakh shares x ₹35)	1575	2316

Working Notes:

			(₹ in lakhs)		
			Dark Ltd.		Fair LTd.
(1)	Computation of Purchase consideration				
	(a) Preference shareholders:				
	$\left(\frac{4,50,00,000}{100}\right)$		720		
	i.e. 4,50,000 shares × ₹ 160 each				
	$\left(\frac{3,00,00,000}{100}\right)$				480
	i.e. 3,00,000 shares × ₹ 160 each				
	(b) Equity shareholders:				
	$\left(\frac{12,00,00,000 \times 5}{100}\right)$		2,100		
	i.e. 60,00,000 shares x ₹ 35 each				
	$\left(\frac{11,25,00,000 \times 4}{100}\right)$		—		1,575
	i.e. 45,00,000 shares × ₹ 35 each		2,820		2,055
	Amount of Purchase Consideration				
(2)	Net Assets Taken Over				
	Assets taken over:				
	Property Plant & Equity		1,350		975
	Non-Current Investments		225		75
	Inventory		525		375
	Trade receivables		450		525
	Cash and bank		450		300
			3,000		2,250
	Less: Liabilities taken over				
	10% Debentures	56.25		28.125	
	Trade payables	630	(686.25)	285	(313.125)
	Net assets taken over		2,313.75		1936.875

	Purchase consideration	2,820		2055.00
	Goodwill	506.25		118.125
	Total goodwill			624.375

(3) Issue of Debentures

Debentures	₹ 90,00,000	₹ 45,00,000
Interest 10%	₹ 9,00,000	₹ 4,50,000
	$\left(\frac{9,00,000 \times 100}{16}\right) = 56,25,000$	$\left(\frac{4,50,000 \times 100}{16}\right) = 28,12,500$

NOTE: In the above solution ₹ 35 has been considered as the issue price of Equity shares for public issue also. Alternative considering this as ₹ 10 also possible. In that case, the balance of cash and cash equivalents will be ₹ 1,191 lakhs and securities premium will be ₹ 3,075 lakhs in place of the balances given in the balance sheet in the above solution.

QUESTION 41 (CA INTER MAY 2022 EXAMS : 20 MARKS)

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

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

Cash and Bank	3,00,000	3,00,000
	71,80,000	43,80,000

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

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

(a) The authorized share capital of Z Ltd. is ₹ 60 lakhs divided into ₹ 6 lakhs equity shares of ₹ 10 each.

(b) As per Registered Valuer the value of equity shares of A Ltd. is ₹ 18 per share and of B Ltd. is ₹ 12 per share respectively and agreed by respective shareholders of the companies.

(c) 10% Debentures of A Ltd. to be issued 12% Debentures of Z Ltd. at par in consideration of their holdings.

(d) A contingent liability of A Ltd. of ₹ 2,00,000 is to be treated as actual liability.

(e) Liquidation expenses including Registered Valuer fees of A Ltd.₹ 50,000 and B Ltd. ₹ 30,000 respectively to be borne by Z Ltd.

(f) The shareholders of A Ltd. and B Ltd. is to be paid by issuing sufficient number of fully paid up equity shares of ₹ 10 each at a premium of ₹ 10 per share.

Assuming amalgamation in the nature of purchase, you are required to pass the necessary journal entries (narrations not required) in the books of Z Ltd. and Prepare Balance Sheet of Z Ltd. immediately after amalgamation of both the companies.

SOLUTION :

Journal Entries in the books of Z Ltd.

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

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

Note:

1. The journal entries for A Ltd. and B Ltd. have been given separately in the above solution. Alternatively, the entries may be given as combined for both companies.

2. *Alternatively, following set of entries may be given in place of the last entry given in the above solution:

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

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

Particulars	Note No.	(₹)
I. Equity and Liabilities		
(1) Shareholder's Funds		
(a) Share Capital	1	41,40,000
(b) Reserves and Surplus	2	41,40,000
(2) Non-Current Liabilities		
(a) Long-term borrowings	3	20,00,000
(b) Long term provisions	4	1,00,000
(3) Current Liabilities		
(a) Short-term borrowings1	5	12,00,000
(b) Trade payables	6	4,40,000
(c) Other liability		2,00,000
Total		1,22,20,000
II. Assets		
(1) Non-current assets		76,60,000
(a) i. Property, plant and equipment	7	
ii. Intangible assets (Goodwill 12,20,000-20,000)		12,00,000
(2) Current assets		

(a) Inventories	8	17,40,000
(b) Trade receivables	9	13,40,000
(c) Cash and cash equivalents	10	2,80,000
Total		1,22,20,000

Notes to Accounts

		(₹)	(₹)
1.	Share Capital		
	Authorized Share Capital		
	6,00,000 Equity shares of ₹ 10 each		60,00,000
	Issued: 4,14,000 Equity shares of ₹ 10 each		41,40,000
	(all these shares were Issued for consideration other than cash)		
2.	Reserves and surplus		
	Securities Premium Account		
	(4,14,000 shares × ₹ 10)		41,40,000
3.	Long-term borrowings		
	12% Debentures		20,00,000
4	Long term Provisions		
	Retirement gratuity fund		1,00,000
5.	Short-term borrowings		
	Unsecured loans		
	A Ltd. 6,00,000		
	B Ltd. 8,20,000	14,20,000	
	Less: Mutual	(2,20,000)	12,00,000
6.	Trade payables		
	A Ltd.	1,00,000	
	B Ltd.	3,40,000	4,40,000
7.	Property, plant & equipment		
	Land and Building		
	A Ltd.	28,00,000	
	B Ltd.	21,00,000	49,00,000
	Plant and Machinery		

	A Ltd.	20,00,000	
	B Ltd.	7,60,000	27,60,000
			76,60,000
8.	Inventories		
	A Ltd.	10,40,000	
	B Ltd.	7,00,000	17,40,000
9	Trade receivables		
	A Ltd.	8,20,000	
	B Ltd.	5,20,000	13,40,000
10	Cash & cash equivalents		
	A Ltd.	3,00,000	
	B Ltd. [3,00,000-2,40,000(dividend)]	60,000	
		3,60,000	
	Less: Liquidation Expenses	(80,000)	2,80,000

Working Note:

Calculation of amount of Purchase Consideration

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

QUESTION 42 (CA INTER NOV. 2022 EXAMS : 5 MARKS)

Star Limited agreed to take over Moon Limited on 1st April,2022. The terms and conditions of takeover were as follows:

(i) Star Limited issued 70,000 Equity shares of ₹ 100 each at a premium of ₹ 10 per share to the equity shareholders of Moon Limited.

(ii) Cash payment of ₹ 1,25,000 was made to the equity shareholders of Moon Limited.

(iii) 25,000 fully paid Preference shares of ₹ 70 each issued at par to discharge the preference shareholders of Moon Limited.

You are required:

(i) to give the meaning of “consideration for the amalgamation’ as per AS-14, and

(ii) Calculate the amount of purchase consideration.

SOLUTION :

Consideration for the amalgamation means the aggregate of the shares and other securities issued and the payment made in the form of cash or other assets by the transferee company to the shareholders of the transferor company.

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

JINDAL SIR MESSAGE

Dear students, I am still not satisfied with number of questions on amalgamation that we have done in class so far but all concepts have been covered.

I want to provide you more classes on this topic. So refer Volumn II (Second Book) for more practice.

NOTES

EXTRA QUESTION ON AMLGAMATION OF COMPANIES

QUESTION NO 1

Following is the Balance Sheet of AB Ltd.:

Liabilities	Amount	Assets	Amount
Share capital	20,000	Goodwill	4,000
(2,000 shares of ₹10 each)		Fixed assets	16,500
Profit and loss account	7,000	Current assets	19,500
Debentures	10,000		
Creditors	3,000		
	40,000		40,000

XY Ltd. agreed to take absorb the above company on following terms:

(1) To take over assets (excluding goodwill, a fixed asset of ₹4,000 and cash ₹1,000 included in current assets) at 10% less than book values.

(2) To take over trade liabilities and debentures

(3) To pay ₹8000 for goodwill

(4) The purchase price was to be discharged by the issue of 1,000 shares of ₹10 each at a market value of ₹15 per share and the balance in cash

(5) Liquidation expenses amounted to ₹400. find out the amount of purchase consideration.

QUESTION NO 2

Following is the Balance Sheet of X Ltd.:

Liabilities	Amount	Assets	Amount
50,000 shares of ₹10 each	5,00,000	Intangible assets	50,000
Debentures	1,00,000	Fixed assets	4,20,000
Creditors	50,000	Current assets	1,10,000
		Profit and loss account	70,000
	6,50,000		6,50,000

Ram Ltd. agreed to absorb the above company on the following terms:

(1) The assets of X Ltd. are be considered as worth ₹5,00,000

(2) The purchase price is to be paid one quarter in cash and balance in shares which are issued at market price.

(3) Ram Ltd. agreed to take over all assets and liabilities

(4) Liquidation expenses amounted to ₹300 agreed to be paid by X Ltd.

(5) Market value of share of ₹10 each of Ram Ltd. is ₹12 per share

(6) Debentures of X Ltd. were paid

You are required to show:

1. Purchase consideration
2. Ledger accounts in the books of X Ltd.
3. Opening entries in the books of Ram Ltd.

QUESTION NO 3

S Limited is absorbed by P. Limited. The Balance Sheet of S Limited is as under:

Liabilities	Amount	Assets	Amount
Share capital:		Sundry assets	13,00,000
2,000 7% preference shares			
of ₹100 each (fully paid up)	2,00,000		
5,000 equity shares of			
₹100 each (fully paid up)	5,00,000		
Reserves	3,00,000		
6% debentures	2,00,000		
Trade creditors	1,00,000		
	13,00,000		13,00,000

P. Limited has agreed:-

(a) To issue 9% preference shares of ₹100 each, in the ratio of 3 shares of P. Limited for 4 preference shares in S Limited.

(b) To issue to the debenture holders in S Limited 8% mortgage debentures at ₹96 in lieu of 6% debentures in S Limited, which are to be redeemed at a premium of 20%.

(c) To pay ₹20 per share in cash and to issue six equity shares of ₹100 each (market value ₹125) in lieu of every five shares held in S Limited and

(d) To assume the liability to trade creditors.

Calculate the purchase consideration.

QUESTION NO 4

Y Limited decides to absorb X Limited. The Balance Sheet of X Limited is as follows:

Liabilities	Amount	Assets	Amount
3,000 equity shares of ₹100 each fully paid up	3,00,000	Sundry Net assets	2,90,000
		Profit and loss account	70,000
Preference shares	60,000		
	3,60,000		3,60,000

Y Limited agrees to take over the net assets of X Limited. An equity share in X Limited for purpose of absorption, is valued @ ₹70. Y Limited agrees to pay ₹60,000 in cash for payment to preference shares holders and the balance in the form of its equity shares valued at ₹120 each.

QUESTION NO 5

The Balance Sheet as on 31st March, 1993 of X Limited and Y Limited are as under:

X LIMITED

Liabilities	Amount	Assets	Amount
Authorized and subscribed capital:		*Fixed assets*:	
60,000 equity shares of ₹ 100 each		Building	20,00,000
fully paid	60,00,000	Machinery	26,00,000
Reserve and surplus:		Furniture	40,000
General reserve	8,00,000	*Current assets:*	
Profit and Loss account	4,80,000	Stock	16,00,000
Current liabilities:		Debtors	9,20,000
Creditors	9,60,000	Bank	2,80,000
		Cash balance	8,00,000
	82,40,000		82,40,000

Y LIMITED

Liabilities	Amount	Assets	Amount
Authorized and subscribed capital:		Goodwill	4,00,000
		Fixed assets:	
20,000 equity shares of ₹ 100		Machinery	16,80,000
each fully paid	20,00,000	Furniture	20,000
Reserve and surplus:		*Current assets*:	
Capital reserve	2,00,000	Stock	7,20,000
General reserve	1,00,000	Debtors	7,20,000
Profit and Loss account	1,40,000	Bank	1,60,000
12% debentures	12,00,000	Cash balance	20,000
Current liabilities:		Expenditure on new project	3,00,000
Creditors	3,80,000		
	40,20,000		40,20,000

Y Limited was absorbed by X Limited on 1st April, 1993 on the following terms:-

(a) Fixed assets other than goodwill to be valued at ₹20,00,000 including ₹24,000 for furniture.

(b) Stock to be reduced by ₹80,000 and debtors by 5 per cent.

(c) X Limited to assume liabilities and to discharge the 12% debentures by issue of 11% debentures of the same value and in addition a premium of 6% was paid in cash.

(d) The new project to be valued at ₹3,80,000.

(e) The shareholders of Y Limited to receive cash payment of ₹30 per share plus four equity shares in X Limited for every five shares held in Y Limited.

(f) Both the companies to declare and pay dividend of 6% prior to absorption.

(g) Expenses of liquidation of Y Limited are to be reimbursed by X Limited to the extent of ₹20,000. The actual expenses amounted to ₹24,000.

Draft journal entries recording the scheme in the books of Y Limited and prepare the Balance Sheet of X Limited after absorption assuming that X Limited's authorized capital has been increased to ₹80,00,000.

QUESTION NO 6

The following are the summarized Balance Sheet of X Limited and Y Limited:

	X Limited	Y Limited
Liabilities:		
Share capital	1,00,000	50,000
Profit and Loss account	10,000	
Creditors	25,000	5,000
Loan X Limited		15,000
	1,35,000	70,000
Assets:		
Sundry assets	1,20,000	60,000
Loan Y Limited		15,000
Profit and Loss account		10,000
	1,35,000	70,000

A new company XY Limited is formed to acquire the sundry assets and creditors of X Limited and Y Limited and for this purpose, the sundry assets of X Limited are to revalued at ₹1,00,000. The debt due to X Limited is also to be discharged in shares of XY Limited.

Show the ledger accounts to close the books of X Limited.

QUESTION NO 7

Super express Limited and Fast express Limited were in company business. They decided to form a new company named super fast express Limited. The Balance Sheets of both companies were as under:

Super Express Limited

Balance Sheet as at 31st December 2002

Liabilities	Amount	Assets	Amount
20,000 equity shares of ₹100 each	20,00,000	Building	10,00,000
provident fund	1,00,000	Machinery	4,00,000

sundry creditors	60,000	Stock	3,00,000
Insurance reserve	1,00,000	Sundry debtors	2,40,000
		Cash at bank	2,20,000
		Cash in hand	1,00,000
	22,60,000		22,60,000

Fast express Limited

Balance Sheet as at 31st December 2002

Liabilities	Amount	Assets	Amount
10,000 equity shares of ₹100 each	10,00,000	Goodwill	1,00,000
Employees profit sharing account	60,000	Building	6,00,000
Sundry creditors	40,000	Machinery	5,00,000
Reserve account	1,00,000	Stock	40,000
Surplus	1,00,000	Sundry debtors	40,000
		Cash at bank	10,000
		Cash in hand	10,000
	13,00,000		13,00,000

The assets and liabilities of both the companies were taken over by the new company at their book values. The companies were allotted equity shares of ₹100 each in lieu of purchase consideration.

Prepare opening balances sheet of super fast express Limited

QUESTION NO 8

The following are the Balance Sheets of Y. Limited and V Limited as at 31st March 2001:-

	Y. Limited (₹ In lakhs)	V Limited (₹ In lakhs)
Liabilities:-		
Equity share capital (fully paid shares of ₹10)	15,000	6,000

Securities premium	3,000	---
Foreign projects reserve	---	310
General reserve	9,500	3,200
Profit and Loss account	2,870	825
12% debentures	--	1,000
Bills payable	120	--
Sundry creditors	1,080	463
Sundry provisions	1,830	702
	33,400	12,500
Assets:-		
Land and building	6,000	--
Plant and machinery	14,000	5,000
Furniture, fixtures and fittings	2,304	1,700
Stock	7,862	4,041
Debtors	2,120	1,020
Cash at bank	1,114	609
Bills receivable	---	130
	33,400	12,500

All the bills receivable held by V Limited were Y Limited acceptances.

On 1ST April, 2001 Y Limited took over V Limited in an Amalgamation in the nature of merger. It was agreed that in discharge of consideration for the business. Y Limited would allot three fully paid equity shares of ₹10 each at par for every two shares held in V Limited. It was also agreed that 12% debentures in V Limited would be converted into 13% debentures in Y Limited of the same amount and denomination.

Expenses of Amalgamation amounting to ₹1 lakh were borne by Y Limited.

You are required to :-

1. Pass journal entries in the books of Y Limited.
2. Prepare Y Limited Balance Sheet immediately after the merger.

QUESTION NO 9

Given below are the Balance Sheet of two companies as on 31st December, 2002

Anand Limited (Balance Sheet as at 31st December, 2000)

Liabilities	Amount	Asset	Amount
Share capital of ₹10 fully paid up	15,00,000	Goodwill	1,50,000
		Freehold property	4,00,000
Share premium	4,500	Plant and machinery	3,50,000
General reserve	1,00,000	Stock	6,82,000
Profit and Loss account	1,65,650	Sundry debtors	2,58,500
8%Debentures	3,50,000	Bank	3,37,500
sundry creditors	57,850		
	21,78,000		21,78,000

Bhanu Limited (Balance Sheet as at 31stDecember, 2000)

Liabilities	Amount	Asset	Amount
Share capital of ₹10 fully paid up	3,90,000	Goodwill	50,000
		Freehold property	1,80,000
8%Debentures	70,000	Plant and machinery	1,00,000
Bank overdraft	6,000	Stock	1,62,000
Sundry creditors	2,57,000	Sundry debtors	95,000
		Profit and Loss account	1,36,000
	7,23,000		7,23,000

The two companies decided to amalgamate, as on 31st December 2000, and a new company called Anand Bhanu Limited was formed with an authorized capital of ₹25,00,000 in shares of ₹10 each. The terms of Amalgamation were as follows:-

For Anand Limited :-

(a) 6 shares of ₹10 each fully paid in the new company in exchange for every 5 shares in Anand Limited and ₹10,000 in cash;

(b) The debentures-holders were to be allotted such Debentures in the new company bearing interest at 7% per annum as would bring the same amount of interest.

For Bhanu Limited :-

(a) 1 share of ₹10 each fully paid in the new company in exchange for every 3 shares in Bhanu Limited and 5000 in cash.

(b) Debentures –holders were to be allotted such Debentures in the new company bearing interest at 7% per annum as would bring the same amount of interest.

The new company took over all the assets and liabilities of the two existing companies.

Show journal entries in the books of Anand Bhanu Limited, giving effect to the arrangement and prepare its opening Balance Sheet.

QUESTION NO 10

Sagar Limited was formed on 1st January 1997 with an authorized share capital of 5,00,000 equity shares of ₹10 each. 1,00,000 equity shares were issued for cash at a premium of ₹2.50 per share. No other transactions took place until 1st April 1997 when Sagar Limited agreed to buy the assets, including goodwill and assume the liabilities of River Limited and Canal Limited for a total of 4,00,000 of its shares.

For the purpose of determining the premium at which the shares of Sagar Limited were to be issued, fixed assets, current assets and the liabilities are to be taken at their book values: goodwill is to be determined on the basis of two and half times the average profit of the past three years after deducting a standard profit of 10 per cent on capital employed as on 31st March 1997. The summarized Balance Sheet of River Limited and Canal Limited as on 31st March 1997 were as follows:

	River Limited ₹	Canal Limited ₹		River Limited ₹	Canal Limited ₹
Issued equity shares of ₹10 each	15,50,000	16,75,000	Fixed assets	22,50,000	14,50,000
Profit and Loss account	9,50,000	75,000	Current assets	12,50,000	30,50,000
Sundry creditors	10,00,000	27,50,000			
	35,00,000	45,00,000		35,00,000	45,00,000

Operating profits for the last three years:

	River Limited (₹)	Canal Limited (₹)
Year ended 31st March 1995	3,52,500	2,75,000
1996	4,40,000	3,20,000
1997	4,45,000	3,42,500

You are required to:

(a) Calculate the numbers of shares to be issued by Sagar Limited to the shareholders of River Limited and Canal Limited respectively and;

(b) Prepare a Balance Sheet of Sagar Limited after completion of business purchased.

QUESTION NO 11

Star Limited and Moon Limited had been carrying on business independently. They agreed to amalgamate and form a new company Neptune Limited with an authorized share capital of ₹2,00,000 divided into 40,000 equity shares of ₹5 each.

On 31st March 1999 the respective Balance Sheets of Star Limited and Moon Limited were as follows:

	Star Limited	Moon Limited
	₹	₹
Fixed assets	3,17,500	1,82,500
Current assets	1,63,500	83,875
	4,81,000	2,66,375
Less: current liabilities	2,98,500	90,125
Representing capital	1,82,500	1,76,250

Additional information:

(a) Revalue figures of fixed and current assets were as follows:

	Star Limited	Moon Limited
	₹	₹
Fixed assets	3,55,000	1,95,000
Current assets	1,49,750	78,875

The debtors and creditors include ₹21,675 owed by Star Limited to Moon Limited.

The purchase consideration is satisfied by issue of shares as follows:

30,000 equity shares of Neptune Limited to Star Limited and Moon Limited in the proportion to the profitability of their business based on the average net profit during the last three years were as follows:

	Star Limited ₹	Moon Limited ₹
1994-95 Profit	2,24,788	1,36,950
1995-96 (Loss)/Profit	(1,250)	1,71,050
1996-97 Profit	1,88,962	1,79,500

You are required to compute the amount of shares to be issued to Star Limited and Moon Limited and a Balance Sheet of Neptune Limited showing the position immediately after amalgamation.

QUESTION NO 12

Exe Ltd. was wound up on 31.3.2004 and its balance sheet as on that date was given below:

Balance sheet of Exe Ltd. as on 31.3.2004

Liabilities	Rs	Assets	Rs	Rs
Share capital		Fixed assets		9,64,000
1,20,000 Equity shares of ₹10 each	12,00,000	Current assets Stock	7,75,000	
Reserves and surplus		Sundry Debtors		
Profit prior to incorporation	42,000	1,60,000		
Contingency reserve	2,70,000	Less provision for doubtful debts		
Profit and loss a/c	2,52,000			
Current liabilities		8,000	1,52,000	
Bills payable	40,000	Bills receivable	30,000	
Sundry creditors	2,26,000	Cash at bank	3,29,000	12,86,000
Provisions:				
Provisions for income tax	2,20,000			
	22,50,000			22,50,000

Wye Ltd. tookover the following assets at values shown as under;

Fixed assets ₹12,80,000, stock ₹7,70,000 and bills receivable ₹30,000

Purchase consideration was settled by Wye Ltd. as under:

₹5,10,000 of the consideration was satisfied by the allotment of fully paid 10% Preference shares of ₹100 each. The balance was settled by issuing Equity shares of ₹10 each at ₹8 per share paid up.

Sundry Debtors realized ₹1,50,000. Bills payable was settled for ₹38,000. Income tax authorities fixed the taxation liability at ₹2,22,000.

Creditors were finally settled with the cash remaining after meeting liquidation expenses amounting to ₹8,000.

You are required to:

1) Calculate the number of Equity shares and Preference shares to be allotted by Wye Ltd. in discharge of purchase consideration.
2) Prepare the realization account, cash/bank account, Equity shareholders account and Wye Ltd. account in the books of Exe Ltd.
3) Pass journal entries in the books of Wye Ltd.

QUESTION 13

Following are the summarised Balance Sheets of A Ltd. and B Ltd. as at 31.3.2012.

Particulars	A Ltd.	B. Ltd.
Share capital.' Equity shares 10 each (fully paid up)	10,00,000	6,00,000
Securities premium	2,00,000	-
General reserve	3,00,000	2,50,000
Profit and loss account	1,80,000	1,60,000
10% Debentures	5,00,000	-
Secured loan	-	3,00,000
Trade payable	2,60,000	,170,000
	24,40,000	**14,80,000**

Land and building	9,00,000	4,50,000
Plant and machinery	5,00,000	3,80,000
Investment	80,000	-
Inventory	5,20,000	3,50,000
Trade receivables	4,10,000	2,60,000
Cash at bank	30,000	40,000
	24,40,000	**14,80,000**

The companies agree on a scheme of amalgamation on the following terms:

(i) A new company is to be formed by name AB Ltd.

(ii) AB Ltd. to take over all the assets and liabilities of the existing companies.

(iii) For the purpose of amalgamation, the shares of the existing companies are to be valued as under:

A Ltd. Rs l8 per share

B Ltd. Rs 20 per share

(iv) A contingent liability of A Ltd. of Rs 60,000 is to be treated as actual existing liability.

(v) The shareholders of A Ltd. and B Ltd. are to be paid by issuing sufficient number of shares of AB Ltd. at a premium of Rs 6 per share.

(vi) The face value of shares of AB Ltd. are to be of Rs 10 each.

You are required to:

(i) Calculate the purchase consideration (i.e., number of shares to be issued to A Ltd. and B Ltd.).

(ii) Pass journal entries in the books of A Ltd. for the transfer of assets and liabilities.

(iii) Pass journal entries in the books of AB Ltd. for acquisition of A Ltd. and B Ltd.

(iv) Prepare the Balance Sheet of AB Ltd.

QUESTION 14

A Ltd. agreed to acquire the business of B Ltd. as on 31st December 2011 on that date Balance Sheet of B Ltd. was summarized as follows:

Liabilities	Rs	Assets	Rs
Shares Capital (Fully paid shares of Rs 10 each)	3,00,000	Goodwill	50,000
General Reserves	85,000	Land, Building and plant	3,20,000
P&L A/c	55,000	Inventory -	84,000
6% Debentures	50,000	Trade receivables	18,000
Trade payables	10,000	Cash & Bank Balance	28,000
	5,00,000		5,00,000

The. Debenture holders agreed to receive such 7% Debentures issued as 96 each as would discharge the debentures in B Ltd. at a premium of 20%. The shareholders in B Ltd. were to receive Rs 2.50 in cash per share and 3 shares in A Ltd. for every two shares held the shares in A Ltd. being considered as worth Rs 12.50each. - There were fractions equaling 50 shares for which each was paid. The directors of. A Ltd. considered the various assets to be valued as follows:

	Rs
Land	1,00,000
Buildings	2,50,000
Plant	3,50,000
Inventory	80,000
Trade receivables	18,000

The cost of liquidation of B Ltd. ultimately was Rs 5,000. Due to a technical hitch, the transaction could be completed only on 1st July, 2011. Till date B Ltd. carried on trading which resulted in a profit Rs 20,000 (subject to interest) after providing Rs 15,000 as depreciation, On 30th June, 2011 Inventory was Rs 90,000. Trade receivables were Rs 25,000 and Trade payables were Rs 15,000. There was no addition to or deletion from the fixed assets. It was agreed that the profit should belong to A Ltd.

You are required, as on July 1, 2012, to:

(i) Prepare Realisation Account and the Shareholders Account in the ledger of B Ltd., and

(ii) give journal entries in the books of A Ltd.

SOLUTION

Ledger of B Ltd.
Realisation Account

	Rs		Rs
To Sundry Assets, transfer :		By Trade payables	15000
Goodwill	50,000	By 6% Debentures	50000
Land, Building, Plant	3,20,000	ByA Ltd.- purchase	6,37500
To Inventory	90,000	consideration (2)	
To Trade receivable	25,000	By Provision for Depreciation	15000
To cash & bank Balance (1)	55,000	By A Ltd. [for profit (3)]	20000
To Shareholders-profit	1,97,500		
	7,37,500		7,37,500

Shareholders Account

	₹		Rs
To cash	75625	By Share capital A/c- Transfer	3,00,000
To Shares in A Ltd.	561875	By General Reserve	85,000
		By P&L A/c	55,000
		By Realisation A/c	197,500
	637500		**637,500**

Note : It is clear that the costs of liquidation will be payable by A Ltd since the amount payable to the shareholders has been specified.

		Rs	Rs
(1)	Cash and bank Balance as on Jan. 1,2012		28000
	Add: Profit earned		20000
	Depreciation provided (no cash payment)		15000
	Increase in trade payables		5000
			68000
	Less: Increase in Inventory	6,000	

	Increase in Trade receivables	70,00	(13,000)
			55,000
(2)	Purchase consideration :		
	For Shareholder - Cash 30,000 x Rs 2.50		75,000
	- Shares 30,000 x 3/2-50 = 44,950@ Rs 12.5		5,61,875
	- Cash for fractions of shares 50 @ 12.5		625
(3)	Since the transfer of assets is an on 30th June, 2012 the profit of Rs 20,000 must be standing to the credit of A Ltd.		6,37,500

Journal of A Ltd.

2011		Dr. (Rs)	Cr. (Rs)
(1) Business Purchase Account	Dr	637500	
To Liquidator of B Ltd.			637500
(Purchase consideration settled as per agreement dated.., for the business of B Ltd.)			
(2) Land A/c	Dr.	1,00,000	
Buildings A/c	Dr.	2,50,000	
Plant A/c	Dr.	3,50,000	
Inventory A/c	Dr.	86,000	
Trade receivables A/c	Dr.	25,000	
Bank A/c...	Dr.	55,000	
To Provision for Depreciation A/c			15000
To Profit & Loss Suspense A/c			20000
To Trade payables A/c			15000
To Business Purchase A/c			637500
To Liability for Debentures in B Ltd			60000
To Capital Reserve A/c			115500
(Various assets and liabilities taken over from B Ltd. -profit up to June 30, 2012 being credited to P & L Suspense since it is to be adjusted for interest and additional depreciation due to increase in values of assets)			

(3)	Capital Reserve A/c Dr. To Cash A/c (Expenses of Liquidation paid by A Ltd.)	5000	5000
(4)	Liquidator of B Ltd. Dr. To Cash A/c To Share Capital A/c To Securities Premium A/c	637500	75625 449500 112375
(4)	Liability for debenture's in b Ltd A/c Dr. Discount on issue of debenture A/c To 7% debenture A/c (Discharge of Debenture holder of B Ltd.)	60,000 2,500	62500

QUESTION 15

P and Q have been carrying on same business independently. Due to competition in the market, they decided to amalgamate and form a new company called PQ Ltd. Following is the summarized Balance Sheet of P and Q as at 31.3.2012:

Liabilities	P	Q	Assets	P	Q
	Rs	Rs		Rs	Rs
Capital	7,75000	8,55,000	Plant & Machinery	4,85,000	6,14,000
Current liabilities	623500	5,57,600	Building	7,50,000	6,40,000
			Current assets	1,63,500	1,58,600
	13,98,500	**14,12,600**		**13,98,500**	**14,12,600**

Following are the additional Information:

(i) The authorised capital of the new company will be 25,00,000 divided into 1,00,000 equity shares of Rs 25 each.

(ii) Liabilities of P includes Rs 50,000 due to 0 for the purchases made. Q made a profit of 20% on sale to P.

P has goods purchased from Q, cost to him rs 10,000. This is included in the Current asset of P as at 31St March, 2012.

The assets of P and Q are to be revalued as under:

	P Rs	Q Rs
Plant and machinery	525000	675000
Building	775000	648000

v) The purchase consideration is to be discharged as under:

(a) Issue 24,000 equity shares of ₹ 25 each fully paid up in the proportion of their profitability in the preceding 2 years.

(b) Profits for the preceding 2 years are given below:

	P Rs	Q Rs
1st year	2,62,800	2,75,125
IInd year	2,12,200	2,49,875
Total	4,75,000	525000

(c) Issue 12% preference shares of 10 each fully paid up at par to provide income equivalent to 8% return on capital employed in the business as on 31.3.2012 revaluation of assets of P and Q respectively.

You are required to:

(i) Compute the amount of equity and preference shares issued to P and Q.

(ii) Prepare the Balance Sheet of P & Q Ltd. immediately after amalgamation.

QUESTION 16

X Ltd. And Y Ltd. were amalgamated on and from 1st April, 2012 and formed a new company Z Ltd. to take over the business of X Ltd. and Y Ltd. The summarized Balance Sheets of X Ltd. and Y Ltd., as on 31st March, 2012 are as follows:

					(Rs in crores)
Liabilities	**X Ltd.**	**Y Ltd.**	**Assets**	**X Ltd.**	**Y Ltd.**
Share capital :			Land and Building	38	25
Equity share of Rs 10 each	50	45	Plant and Machinery	24	17

10% Preference Share of			Investments	10	6
Rs 10 each	20	14	Inventory	22	15
Revaluation Reserve	10	6	Trade Receivable	30	24
General Reserve	12	8	Cash at Bank	16	13
Investment Allowance					
Reserve	5	4			
Profit & Loss Account	8	6			
15% Debentures of Rs 100	4	5			
each (Secured)					
Trade payable	31	12			
	140	100		140	100

Additional Information:

(1) Z Ltd. will issue 6 equity shares for 10 equity shares of X Ltd. and 2 equity shares for 5 equity shares of B Ltd. The shares are issued @ Rs 30 each having a face value of Rs 10 shares.

(2) Preference shareholders of two companies are issued equivalent number of .15% preference shares of Z Ltd. at a price of Rs 120 per share (face value 100).

(3) 15% Debenture holders of X Ltd. and Y Ltd are discharged by Z Ltd. issuing such number of its 18% Debentures of Rs 100 each so as to maintain the same amount of interest.

(4) Investment allowance reserve is to be maintained for 4 more years. Prepare the Balance Sheet of Z Ltd. after amalgamation. the amalgamation took place in the nature of purchase.

QUESTION 17

The summarized balance Sheet A Limited and B Limited as at 31st March, 2012 are as follow:

Liabilities	A Ltd.	B. Ltd.	Assets	A Ltd.	B. Ltd.
Equity share of 10 each	20,00,000	12,00,000	Sundry assets	30,00,000	18,00,000
General reserve	4,00,000	2,20,000			
Trade payables	6,00,000	3,80,000			
	30,00,000	18,00,000		30,00,000	18,00,000

Sundry assets of B Ltd. includes long term investment of 4,00,000, the market value of which is now Rs 4,80,000. A Ltd. absorbed B Ltd. on the basis of intrinsic value of the shares. The purchase consideration is to be discharged in fully paid-up equity shares. A sum of Rs 1,00,000 is owed by A Ltd. to B Ltd., also included in the Inventory of A Ltd. is Rs 1,20,000 goods supplied by B Ltd. at cost plus 20%. Give Journal entries in the books of both the companies, if entries are made at intrinsic value. Also prepare Balance Sheet of A Ltd. after absorption.

QUESTION 18

The following are the summarized balance Sheet of A Ltd and B Ltd as on 31st December, 2011:

Liabilities	A Ltd. Rs	B Ltd. Rs	Assets	A Ltd. Rs	B Ltd. Rs
Share Capital Equity			Fixed Assets	7,00,000	2,50,000
Equity Shares of Rs			Current Assets:		
10 each	6,00,000	3,00,000	Inventory	2,40,000	3,20,000
10% Pref. Shares of			Trade		
Rs 100 each	2,00,000	1,00,000	Receivable	5,00,000	2,90,000
Reserves and Surplus	3,00000	2,00,000	Cash at Bank	1,10,000	40,000
Secured Loans:					
12% Debentures	2,00,000	1,50,000			
Current Liabilities:					
Trade payable	2,50,000	1,50,000			
	15,50,000	9,00,000		15,50,000	9,00,000

Details of Trade receivables and trade payable are as under:

Trade payables	A Ltd.	B.Ltd.
Sundry Creditors	2,20,000	1,25,000
Bills Payable	30,000	25,000
	2,50,000	1,50,000
Trade receivables		
Debtors	3,60,000	1,90,000
Bills Receivable	1,40,000	1,00,000
	5,00,000	2,90,000

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 Rs 10% Equity dividend, Preference dividend having been already paid.

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

(i) 8 Equity Shares of Rs 10 each will be issued by A Ltd. at par against 6 shares of B Ltd.

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

(iii) 12% Debenture holders of B Ltd. are to be paid at 8% premium by 12% Debentures in A Ltd. issued discount of 10%.

(iv) Rs 30,000 by A Ltd to B Ltd. For liquidation expenses. Sundry Creditors of VB Ltd. include 10,000 due to A Ltd.

Prepare:

(a) Absorption entries in the books of A Ltd.

(b) Statement of consideration payable by A lid.

NOTES