AS 22 → Accounting for Taxes on Income

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30%.

A/c	IT
NPBT → 80cr	100cr
30%.	30%.
24cr	30cr

Inco. → 80cr

tax → 30cr → Investor Que → How?

But this ↑ tax will get reversed in future.

↳ Deferred Tax

Income as per
→ IT → Tax income
→ books → A/cing income

Tax payable in CY
= current Tax
↳ cal. on Tax income

Diff between current Tax & tax as per A/cing income
↳ Tax on A/cing income
↳ Tax Exp.

Recog only if such diff is temporary.

* Each item of Diff. will be treated seperately

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DTL

Y_1 (2022-23)

AI = 100cr → Tax Exp
CT Tax 24cr
Def Tax Exp 6cr
30cr

Tax Exp = 100cr × 30%.
= 30cr

Diff Tax = 80cr - 24cr
= 6cr

This 6cr will be paid in next yr

DTL = (AI - TI) × taxable
= (100 - 80) 30%.
= 6cr

TI = 80cr
(-) C.T (24cr)
@ 30%.
56cr

(PEL)
1) Current Tax A/C Dr 24cr -
TO Bank / Tax Payable A/C - 24cr

(PEL)
2) Def Tax Exp. A/C Dr 6cr -
TO DTL A/C - 6cr
(CL)

Y_2 (2023-24)

AI = 80cr
(-) Tax Exp
CT 30cr
(-) DTL cr (6cr) 24cr

TI = 100cr
(-) CT = (30cr)
@ 30%
70cr

CT A/C Dr 30cr -
TO B/T-P A/C - 30cr

3) DTL A/C Dr 6cr -
TO Def Tax. Exp (Rev) / Def Tax. income A/C - 6cr

→ Depri? → Usually in I.T the depri.n is ↑ due to which T.I & A.I ↑ ∴ DTL

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DTA

Y_1

AI = 120cr
(-) Tax Exp.
CT 45cr
(-) Def (9cr) 36cr.
T.I

T.I = 150cr
(-) CT 45cr
@ 30%.
105cr

CT A/C Dr 45cr -
TO B/T-P A/C - 45cr

Diff. Tax = 45 - 36
= 9cr
This Extra tax will be benefitting in next yr

DTA = (T.I - AI) 30%.
= (150 - 120) 30%.
= 9cr

1) DTA A/C Dr 9cr -
TO Deff T.I A/C - 9cr

Y_2

AI = 150cr
(-) Tax Exp.
CT 36cr
(+) DTA rev (9cr) 45cr

T.I = 120cr
(-) CT
@ 30% 36cr
84cr

CT A/C Dr 36cr -
TO B/T-P A/C - 36cr

2) Deff T.I income Dr 9cr -
(Rev)
TO DTA A/C - 9cr

I Key Terms

1) Accounting Income (AI) :- It is the net profit cal. in books of A/C as per AS

2) Taxable Income (TI) :- It is the N.P cal as per Income Tax Act.

3) Current Tax :- It is the income tax payable as per I.T Act in current yr.

4) Deferred Tax :- It is the tax effect (Diff.) due to timing Diff. between AI & TI.

5) Tax Exp. :- It tax amt, as per AI.
= current Tax ± Deferred Tax Exp./Income

II Condn for DTL / DTA
(when to cal. Deferred Tax)

Timing Diff. (Temporary)	Permanent Diff
→ It is the diff between AI & TI that originate in one period & are capable of reversal in subsequent period	→ It is the diff between AI & TI that originates in one period & are NOT capable of reversal in subsequent period
→ Eg Depri°, Preliminary Exp, sec 43B items, etc.	→ Eg Donation to unreg. trust, Indexation in cap. Gains, etc
→ In this case DTA / DTL should be created	→ NO DTA / DTL should be created

III Calc° of Deferred Tax

Def Tax = (AI - TI) × Tax rate

AI > TI.	AI < TI
→ DTL is created	→ DTA is created
→ J.E	→ J.E
a) For Current Tax paid / payable current Tax Exp A/C Dr (PAL A/C) TO Bank / Tax Payable A/C	a) For current Tax paid / Payable C.T. Exp A/C Dr TO Bank / T.P A/C
b) For creation of DTL (PAL A/C) Deferred Tax Exp A/C Dr. TO DTL A/C	b) For creation of DTA DTA A/C Dr TO Deferred Tax Income A/C (PAL A/C)

Imp Notes:-

→ If AI = TI then no deferred tax needs to be created.

→ Off setting / Off setting
→ DTA & DTL can be off settled while presenting it in B/s if :-
a) the underlying items creating diff. can be off settled while cal. tax

b) DTA & DTL are related to taxes that are levyed under same tax laws. eg Indian tax cannot be off settled against tax as per US tax laws.

Tran^n	Analysis	Nature of Diff	Effect	₹
iv) Repairs of ₹140L fully allo. for tax pour in 20-21; & will be in A/c books ₹140L, spread over 2 yrs	∵ Exp. in BOA will be allo. ₹70L & for tax pour will be ₹140L, AI > TI ∴ DTL would	Timing diff as it will be rev. in 2021-22	creation of DTL	(140-70) ×40% = 28L

Bal. as on 31-03-21
DTL = ~~₹28L~~ − ₹11.2L + ₹28L = ₹44.8L
(i) (iv)

Illus 8

Tran^n	Analysis	Nature of Diff	Effect	₹
i) Depn Diff. of ₹28L	Usually as per tax records the Depn on F.A during initial yrs of asset is ↑ due to WDV method being followed ∴ in initial year AI > TI	It is a case of Timing Diff. as diff betw. AI & TI occured in a period will be rev. in Sub. period	Rev. of DTL as in initial yrs of F.A DTL would have been created	28L×40% = 11.2L
ii) Exp of ₹14L dis. in 2019-20; is allowed in 2020-21.	In 2019-20, Exp. of ₹14L was dis. for tax pur., hence AI < TI; ∴ DTA would have been created.	It is a case of Timing Diff as Exp. was allowed in 2020-21 for tax pur	Rev. of DTA	14L×40% = 5.6L
iii) Exp of ₹7L dis. in 19-20; is allow. in 20-21	In. 19-20 Exp. of ₹7L was dis for tax pur; hence AI < TI; ∴ DTA would have been created	It is a case of Timing diff as Exp was all. in 20-21 for tax pur	Rev of DTA	7L×40% = 2.8L

DTA = ₹14L − ₹5.6L − ₹2.8L = ₹5.6L
(ii) (iii)

c/f loss

↳ due to c/f you will pay ↓ tax in next yr

↳ due to loss you will get benefit in Tax in next yr.

↳ create DTA in loss yr. — NO Ver. cer NO DTA

↳ only if Vertical Certainity (Documentary Evid.)

Y1	AI	TI
Net loss	100cr	100cr
(-)	30cr	DTA = 100 × 30% = 30cr
	70cr	DTA A/c Dr 30cr —
		To DTI A/c — 30cr

Y2

	AI	TI
Net Profit	20cr	20cr
(-) Tax Exp		(-) c/f (20cr)
Rev. of DTA (20cr × 30%)	(6cr) ← Retained earning	0
		Bal. in DTA
DTA rev. A/c Dr	6 cr —	= 24cr
To DTA A/c	— 6cr	

Y3	AI	TI
Net Prof.	90cr	90cr
(-) Tax Exp		(-) c/f (80cr)
C.T.E	30cr	10cr
(+) Rev.	24cr	×30% 3cr
	27cr	

(-) Tax Exp
C.T.E

(+) DTL (-) DTA

(-) Rev. DTL (+) Rev. DTA

IV Spl. cases

1) c/f losses

→ It would create DTA

→ DTA & corrosponding tax saving should be recorded in the yr when loss is incurred & should be reversed in years when loss is set off.

→ DTA on c/f losses can be created only when there is Virtual certainty (Documentary Evi.) supported by convincing evidence that co. will earn sufficient profits in next 8 yr.

→ for DTA on benefits of ded^n u/s 35D, 43B, etc there should be reasonable certainity. (No need of Doc evi.)

Note:- When nothing mentioned in Q, assume reasonable/Vertical certainity as the case may be.

2) Applicable Tax rates
→ For Deferred Tax cal°, tax rates applicable in feture yrs. should be taken based on laws (budget) which have been enacted / substantialy enacted till B/S date.

V Deferred Tax in case of entity which enjoy Tax Holidays (u/s 80IA, 80IB, 80IC, 10A, 10B)
→ If DTA/DTL arises in period of Tax Holidays MCQ & rev. also in period of Tax Holidays → No need to creat DTA/DTL
→ But if rev. beyond Tax Holidays period → creat DTA/DTL.

Timing Diff.

In case DTL/DTA originates during Tax Holiday period & also gets reversed during Tax Holiday period then No Deferred Tax to be created.	In case DTL/DTA originates during Tax Holiday period & gets reversed beyond Tax Holiday period then Deferred Tax should be created.
eg When Tax Holiday is for 3 yr. DTA/DTL originates in Y_1 & gets reversed in Y_2	eg When Tax Holiday is for 3 yr. DTA/DTL originate in Y_2 & gets reversed in Y_4

VI Transitionary Provision
→ On the first date when AS-22 becomes applicable to an entity, DTA/DTL should be created for diff accumulated till date with corresponding adj. (Dr./Cr) to Revenue Reserve (Gen. res.)
→ After DTA/DTL is created on 1st date of application subsequent changes will be recorded in statement of P&L

Illus → 4

2014-15	
Net loss → 200000	As per Tax
(-) Tax Exp	Net loss (2L)
C.Y Tax —	(-) C.Y tax —
Def Tax incom. 80k ← DTA creation	Net loss (2L)
(2L × 40%)	
Net loss 120000	

2015-16	
Net profit → 100000	As per tax
(-) tax Exp	Net profit 100000
C.Y tax —	(-) set off (100000)
DTA rev. → Def Tax Exp. 40k	Taxable income —
(1L × 40%)	
Net profit 60k	

2016 - 17

Net profit - 120000

(-) Tax Exp

C.Y Tax 8k

DTA rev. → Def tax Exp 40k

48k

Net profit 72k

15-16 (21-14)

As per Tax

Net profit 120000

(-) Set off (100000)

Net profit 20000

(-) C.Y Tax (8k)

20k × 40% 12k

Mat

(AI)

NPBT → 300 cr Tax rate → 30%.

NPBT → 200 cr

(TI)

MAT rate → 10%. NPBT MAT → 350 cr

Step 1 → AI > TI

DTL = (AI - TI) × rate

= (300 - 200) × 30% = 30 cr

Step 2 → C.Y Tax

Higher of

Tax on NP as Tax record = 200 cr × 30% = 60 cr

[OR]

Tax on N.P as per MAT = 350 cr × 10% = 35 cr

Diff MAT cr.

If no MAT cr

P&L

C.Y Tax 60cr

To Bank 60cr

→ P&L

DTL → 30cr

C.Y Tax → 60cr

90cr

P&L

C.Y Tax 35cr

B/S MAT Asset 25cr

To Bank 60cr

→ P&L

DTL → 30cr

C.Y Tax → 35cr 65cr

MAT Asset 25cr (60 - 35)

VII Deferred Tax & Minimum Alternative Tax (MAT)

→ As per ICAI notification, DTA / DTL should be created based on diff between AI & TI using regular Tax rate. We should not use Book profit u/s 115 JB & MAT Tax rate for purpose of DTA / DTL

Step 1 → Cal. DTA / DTL

= (AI - TI) × Tax rate

Step 2 → C.Y Tax payable

Higher of

→ Tax as per IT [OR]

→ Tax as per MAT

Step 3 → MAT > Tax as per IT & entity will be using MAT cr. in future then ~~Paid~~ MAT asset

MAT Asset = Tax as per MAT - Tax as per IT.

JE

Current Tax A/C (P&L) Dr. (3)

MAT Asset A/C Dr. (1)

To Bank A/C (2)

Option 2 → IF MAT > Tax as per IT & entity will not be using MAT cr. in future then MAT asset will not be created

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I Terms

→ **Reporting currency :-** The currency in which the financial reports are to be prepared in a country is called reporting currency.
→ eg In India the r.c is ₹.

→ **Foreign currency :-** The currency other than reporting currency is called foreign currency.
→ eg In India the currencies other than ₹ like $, pound, Yen, etc are called F.C.

→ **Foreign Exchange rate :-** It is the ratio between reporting currency & foreign currency.
→ eg 1$ = ₹84

→ **Foreign Exchange Transactions :-** The transactions in foreign currency & which are required to be sett. in foreign currency are called foreign exchange transactions.

→ Monetary Items :-
The assets & liabilities to be received or paid is contractualy fixed i.e the amt. is determinable are called M.I. terms of
→ eg Bank Bal / Cash Bal. & incomes of foreign currency, Debtors / creditors interms of foreign currency, loan taken/ given interms of foreign currency

→ Non-monetary Items :-
The assets & liabilities to be received or paid is NOT contractualy fixed ie the amt is not may not be pre determinable
→ eg Fixed assets (T.A & I.A), Equity shares, Investments, Inventories, etc

→ Spot Rate :-
The current exchange rate is called spot rate.

→ Closing Rate :-
The foreign exchange rate on B/S date is called closing rate.

→ Historic Rate :-
The original foreign exchange rate on date of transaction is called historic rate.

II Initial Recognition

→ The foreign currency transactions can be recorded using the spot rate on the date of transaction.

→ If the exchange rates are relatively stable, weekly / monthly avg. rates can also be used to convert all the items in a week / month.

III Subsequent Recognition (B/S date)

→ On B/s date the monetary items should be translated / converted / reported at closing rate.

→ On B/s date the Non-monetary items carried at the Historical rate should be reported at Historical rate. (No change)

For MCQ → In case of Non-monetary items carried at fair value (eg Land using revaluation modal or inventory at NRV) then it should be reported on B/S date using the exchange rate on the date when fair value was determined. (Land revalued)

→ Any profit or loss arising on conversion / translation / settlement of foreign currency items should be recorded as foreign exchange gain / loss & transf to Profit & loss A/c

IX Special case

1) Forex Gain / loss due to foreign exchange rate diff. on B/S date on long term loans (Monetory item)

option 1
Forex Gain / loss on loan should be transf to P&L A/C

option 2 [Para 46(A)]

General purpos loan

Forex Gain / loss to be transf to Foreign currency Monetory items Translation Diff. A/C (FCMITDA)

To be deferred over the tenure of loan & transf to P&L A/C

Specific loan for Depriciable Assets

Forex Gain / loss to be capitalised with asset.

Revised bal. of asset to be depriciated

Note :-

Ones an entity selects between option 1 & 2 then it can not change this option at a letter date (irrevocable)

2) Foreign Operation

→ Subsidiary, associate, J.V, branch of the reporting entity whose operations are based in a country other than the country of reporting entity are called foreign operation.

→ It is classified as ~~internal~~ integral & non-integral foreign operations.

→ Integral foreign operation carry on its business as if it were an extension of reporting entity's operations.

→ Non integral foreign operation is run independantly In the books of of reporting entity, share in Net Asset are shown as the net investment in an non-integral foreign operation.

→ The change in foreign exchange rates affect the Net inv. rather than the individual Monitory & non-monitory items held by not-integral foreign operation.

Foreign currency translation of financial statement of foreign operations.

(Branch, subsidiary, J.V)

Items	Integral	Non-integral
a) Monetory	closing rate	closing rate
b) Non-monetory		
→ At cost (Historic)	Historic rate	closing rate
→ At F.V / NRV	Rate on date when F.V. deter.	closing rate
c) Forex Gain / loss	P&L	Foreign Currency Translation Res A/c (FCTRA)
d) Incomes / Exp.	Rate on date of transaction / Avg. rate	Rate on date of transaction / Avg. rate

Note:-

→ Nothing is mentioned in Q then as per ICAI it is assumed to be integral op.

→ Goods sent to Branch / received from branch or HO or inter branch transactions should be recorded at actuals given in Q

→ Forex gain / loss in case of integral branch is cal. by converting Trial Bal. in terms of ₹ at applicable exchange rates & the bal. fig (diff between Dr & Cr) is recognised as forex gain / loss.

→ In case of non-integral operations the bal. in FCTR will be transf to P&L when the foreign operations are sold / disposed.

H.W

Illus – 4:

Trial Bal. as on 31-03-2019 of Integral Branch in Greenville, USA

Particulars	Monetary/ N-M	Rate(₹)	Dr ₹	Cr ₹
Fixed Assets	N.M	Historic 63	504000 → (8000×63)	
opening Inventory	N.M	Historic 65	52000 → (800×65)	
cash	M	cl. 67	46900 → (700×67)	
Goods received from HO	—	Actuals	(Adj. 4) 185500	—
Sales	Income	Avg. 66	(24050×66)	1587800
Purchase	Exp	Avg 66	778800 → (11800×66)	
Expenses	—	Avg 66	118800 → (1800×66)	
Remittance to HO	—	Actuals	162000 → (Adj → 5)	
HO Account	—	Actuals	(Adj → 6) → 284500	
Forex Gain (Bal. fig)			23800	
			1871800	1871800
closing stock	N.M	cl. rate 67	46900 → (700×67)	
Depreciation (504000×10%)			50400	

3) Accounting for Forward Contracts

→ The contract in which an entity agrees to buy or sell foreign exchange of a particular amt. at a particular rate on a particular future date is called forward contract.

eg → HP has purchased Goods of $100000 from IBM on 4 months Cr. on 01-01-24. $1 = ₹80 On this date HP enters into a forward contract with SBI for $100000 which it wants 01-05-24 at ₹ $1 = ₹83

The diff. = [(83-80) × $1 L = ₹3L is called the forward contract premium.

→ It can be classified into two catagories
→ Hedging → Speculation / Trading

→ Hedging →

There exists a foreign exchange receivable or payable in future.

Obj. is risk reduction.

→ In case of Hedging steps to be followed are:-

Step 1: Find forward exchange contract premium or discount.

Forward premium = (Forward rate mentioned in contract − spot rate i.e. exchange rate on date of inception of contract) × Foreign ex. value (Amt. in $)

eg (83-80) × $100000

Step 2: Such forward contract premium should be amortized (spread) as exp. or income over the life / tenure of contract. (time basis)

Step 3: Profit / loss on translation of monetary items on B/S date should be recognized separately & transf. to P&L A/c

Step 4: Profit / loss on cancellation or renewal of such forward contract should be recognized as income or exp. of the period & transf. to P&L A/c.

~~Trading~~

→ Speculation :-

There is no foreign exchange amt. receivable or payable in feture.

Obj. is to earn profit from fluctuations in foreign exchange rates.

→ In case of speculation / trading the steps to be followed are:-

Step 1: Find profit or loss on such forward exchange contracts on B/S date or settle date)

Profit/loss = (Forward rate on B/S date or settle date − Forward rate at inception of contract or forward rate used to measure p&L earlier) × amt. of foreign exchange ($)

In such cases No need to cal. forward contract premium.

Note: → Nothing mentioned in Q. the forward contract is assumed to be speculation.

→ Forward rate is the exchange rate on a specified feture date

cal. of Fard cont. prem. (Hedging)

(-) spot rate

diff

(x) Forex value $100000

∴ Forward contract pre for 4M. ₹00000

∴ For. cont prem transf to P&L (23-24) =

Imp. points for MCQ

→ FCMITDA should be shown in B/S on the Equity & liability side under the head "reserves & surplus" as a separate line item.
(Dr bal / Cr bal R&S mai hi aayega.)

→ Bal. in FCTR should also be shown as a separate component of shareHolders funds.

→ Contingent liability in foreign currency at B/S date is disclosed at Cl. rate

AS-16 → Borrowing cost

→ concept related to int. adj. due to diff. / fluctuation in forex rates.

→ Note:

→ Forex loss due to fluctuations in forex rates on B/S date on long term loans (M.I) (option → only) can be capitalized as Borrowing cost to the extent of savings in int.

Eg 1/4/23 loan taken by Rel. Ltd = $1L @3% option SBI = @10%. $1 = ₹80
31/3/24 $1 = ₹85

Step 1: Find actual int. paid
= Loan ($) × int rate × exchange rate
= $100000 × 3% × ₹85 = ₹255000

Step 2: Cal. Notional int based on Indian int. rate
= loan ($) × exchange rate (at inception) × int rate
= $100000 × ₹80 × 10% = ₹800000

Step 3: Find savings in int. (Max. int. adj.)
= $S_2 - S_1$
= ₹800000 − ₹255000 = ₹545000

Step 4: Find forex loss on translation of loan (Monetary item) on 31/3
= loan ($) × (Cl. rate − spot rate at inception)
= $100000 × (₹85 − ₹80)
= ₹5,00,000

Step 5: The amt of forex loss that can be capitalized as Borrowing cost will be limited to saving in int (S_3), any excess will be transf to P&L

Forex loss than can be capitalized
= lower of Savings in int & forex loss.
= lower of 545000 & 500000
= ₹500000

Step 6: Total Borrowing cost
= Actual int (S_1) + Forex loss Capitalized (S_5)
= 255000 + 500000
= ₹755000

Notes:-

→ In case the co. is following Para 46(A), then the above steps are not reqd

AS-7 → Construction Contracts

I Meaning of construction contract

→ Long term projects

→ Takes more than one year to complete the project

→ Final outcome is after no. of years of commencement of construction.

→ Entity who agrees to complete the construction is called Contractor

→ Customer who req. the construction to be completed is called contractee.

→ Allocation of revenue & cost to the accounting period in which the construction work is performed

→ can be for construction of an asset or combination of assets.

→ Construction contracts include:

→ construction of an asset or combination of assets that are closely interelated

eg Constru. of Bridges, Buildings, Dam, pipeline, ship, roads, tunnel, etc

→ Contracts for rendering of services related to construction of assets.

eg service of proj. managers, architects, etc

→ Contracts for destruction or restoration of assets.

II Combining & Segmenting Construction Contracts
(Single contract) (Separate contracts)

→ When a contract covers a no. of assets, the construction of each asset should be treated as a separate contract when:
→ Separate proposals have been submitted for each asset.
→ Cost & revenue of each asset can be identified
→ Each asset has been subject to separate Negotiation and they can be accepted or rejected separately
→ Group of Contracts should be treated as single contract when:
→ Group of contracts is negotiated as a single package
→ Also negotiated with overall profit margin.
→ Contracts are so closely interrelated like a single project

III Types of Contracts
Fixed Price Contract | Cost plus Contract
→ The amt of contract revenue is fixed (Pre-determined) | → Contract revenue is determined at cost plus an agreed profit margin.

IV Accounting for Contract Revenue (as per AS-7)
→ should be recognized on cummulative % completion method. (do not apply AS-9)
→ Contract revenue recognition

Fixed Price contract	Cost Plus contracts
→ In this case the cost & revenue for the entire contract can be reliably estimated (Outcome is measurable)	→ In this case cost & revenue for the entire contract can not be reliably estimated. (Outcome is not determinable)
→ cal. of revenue for current year.	→ Revenue to be recognized based on cost incurred (Cost incurred x agreed profit margin)
Revenue till date xx	
(-) Revenue earlier recorded (xx)	
Revenue for current year xx	

NOTES -
In first case, first find the stage of completion using cost method, prep. by ICAI

% of completion (Cumulative) = (Cost incurred till date / (Cost incurred till date + Estimated cost for further completion)) × 100

Cost incurred till date = Work certified + Work Uncertified

ICAI always assumes that the works certified & Uncertified given in Q of AS-7 is at cost/price only

→ These (are directly attributable costs incurred for constructing the asset.

→ It includes :-

→ Cost of material, labour (direct) exp., etc.

→ Produc^n / Construc^n OH directly associated to proj. & can be reasonably allocated to contract. (ex)

eg Power cost, construction equipment rent, etc.

Note

→ While calc. material cost, include material consumed not cost of material purchased.

→ Material consumed = op. stk + Purch. - Transf to other site - returned from site - material lying at site on closing date (cl. stk.)

→ Admin & selling Exp. should NOT be included in Contract cost.

Work certified mai % of rev. hoga so it will include Profit margin too.

∴ WIP cost pe valued nahi hua hai cost + profit pe record hua hai. for the purpose of Exam ICAI assumes Works certified + uncertified both are at cost.

VI Valuation of Contract WIP

→ As per AS-7 on construction contracts, Contract WIP value as on BS date will include cost of work certified & cost of work uncertified.

VII Contract Revenue

→ It includes :-

Agreed Price | Performance Incentives | Variation & Scope | Escalation

→ Fixed contract price

eg ₹100 cr

→ It is the add^n amt payable to contractor if standards are met or exceeded.

→ Proj. is at sufficiently adv. stage; &

→ Amts of incentive can be reasonably measured; &

→ It is virtually certain that incentive will be received.

→ The contract revenue due to variation in scope of work should be recognized only when it is agreed by both contractor & customer.

→ An escalation clause in included in contract, the customer will compensate the contractor for the ↑ in cost of inputs beyond the agreed limit.

→ It is generally to compensate for inflation.

Note:

→ Change in contract revenue due to any of the above reasons or satisfaction of negs condn should be done prospectively & not retrospectively as it is change in estimates (AS-5)

VIII Key points

→ Estimated Contract loss

→ In case a contract has an estimated loss on total basis, as per AS-7 the entity should create a provision for loss immediately after deducting any loss recognized in current yeard

JE Contract A/c Dr.
To Provision for loss A/c

eg for a contract that begins of 01/04/23 with contract price of ₹100 crs
cost incurred upto 31.03.24 = ₹40 crs.
Estimated further cost for compln = ₹80 crs.
find rev. to be reco. P&L for 23-24 & provin for loss if any.

Step 1 → Stage of Compln = 40/(40+80) × 100 = 33.33%

Step 2 → Rev. to be reco. for 23-24
= ₹100 crs × 33.33%
= 33.33 crs

Step 3 → loss for 23-24
= Revi to cost = 33.33 crs − 40 crs
= ₹(6.67 crs.)

Step 4 → Esti. total contract loss

Total contract price	100 crs.
(-) Total cost till compln (40+80)	(120 crs.)
∴ Total Esti. loss	20 crs.
(-) loss reco. in 23-24	(6.67 crs.)
∴ Provin for loss to be made	₹13.33 crs.

J.E 2014

1) Contract A/c Dr 40 crs
To Contract cost A/c 40 crs
(cost incu. in 23-24)

2) Contractee A/c Dr 33.33 crs
To Contract A/c 33.33 crs
(Rev. reco.)

3) Contract A/c Dr 13.33 crs
To Provi. for loss A/c 13.33 crs

4) P&L A/c 20 crs
To Contract A/c 20 crs
(Total loss i.e 100 − 120)

Cr	Contract A/c	Cr
	40 crs	33.33 crs
	13.33 crs	20 crs
	53.33 crs	53.33 crs

The contract is completed on 31-03-25
Cost incurred as estimated ie ₹80cr

Sol.

Step 1 → Stage of compl^n = 100%.

Step 2 → Rev. to be recog. till date (31-3-25)
(100 cr × 100%) — 100 cr
(−) Rev. recog. earlier — (33.33 cr)
∴ Rev. for 24-25 — 66.67 cr

Step 3 → loss = Rev − cost = 66.67 − 80 = ₹13.33 cr
This will lead to reversal of provi^n for loss.

JE Ye

1) Contract A/C Dr 80 cr —
To Contract cost (A/C (cost incu^n 24-25)) → 80 cr

2) Contractee A/C Dr 66.67 cr —
To Contract A/C (rev. recog.) 66.67 cr

3) Provi. for loss A/C Dr 13.33 cr —
To Contract A/C 13.33 cr

→ Methods for finding stage of complition.
→ Cost Method
→ survey of work performed method
→ compli^n based on physical proportion of contract work.

→ Disclosure in Financial Statement
→ The following needs to be disclosed in Notes to A/C :-
→ Contract Rev. recog. & method used.
→ Stage of compli^n. & method used.
→ Contract cost incurred.
→ Contract P/L recog.
→ Adv. received
→ Progress Billings (Bills raised → received yet receivable)
→ Retentions. (Prog. Billings unpaid until satisfaction of condi^n. in contract)

→ Gross Amt due from / to Customer.

	(₹)
Cost incurred till date	xx
(+) Profit recog. till date	xx
(−) loss recog. till date	(xx)
(−) Progress Billings	(xx)
∴ Gross amt due from / to customer	± xx

If +ve → from; If −ve → to

I Basic EPS

→ Basic EPS = N.P attributed to Eq. Shr. H. after pref. Div. / Weighted Avg No. of ESH (WANES)

→ Numerator

→ Profit for Eq. shr. H. is cal. after deducting

→ All Exp.

→ Taxes (current + Deffered)

→ Prior Period Items (AS-5)

→ Exceptional & Extraordinary Items (AS-5)

→ Prefo Div.

→ Denominator (WANES)

→ The No. of shr to be included in denominator is a time based weighted avg. where no. of days / months for which the shr are outstanding are to be taken as weights.

→ In case of partly paidup shr., we need to convert them into equivalent fully paidup shares. (Money received / Face value)

Note :-

→ In case of partly paidup shr. it will be included in WANES only when it is entitled to dividend. If nothi is said in Q, we assume it is entitled for dividend &

included in WANES as equivalent fully paidup shrs.

→ On Non-cummulative pref. shrs div. should be deducted from Net Profit only if provided in Books.

Case 1) Equity shrs issued for cash → Date cash is receivable.

2) Equity share on conversion of Debt. instrument (Conv. Deb.) → Date of conversion.

3) Equity shrs issued for settlement of liability → Date Settlement is effective

4) Eq. shrs issued for Acquisition of asset → Date acquisition is recognized

5) For rendering of services → Date services are rendered.

6) Eq shrs issued in lieu of int. / principal → Date int. / principal ceases / stops / cancelled

7) Amalgamation in Nature of purchase → Date of Acquisition

8) Amalgamation in Nature of Merger → Date from beginning of reporting period

→ Shares issued without consideration (Bonus shares / Shrs split)

→ Bonus shrs should be retrospectively adj. from the earliest reported date ie. 1st day of the earliest comparative 1 year presented

→ For presenting F.Y 22-23 the bonus shrs will be assumed to be existance on 1st April 21. Hence, no time adj. will be needed for bonus shrs if the date of their actual issue is irrelevant. Leads to better comparability

Illus → 3

As per AS 20 on Earnings Per shares, bonus shares should be retrospectively adjusted from earliest reported date.

Basic EPS

2016

Basic EPS = $\frac{\text{N.P for Equity share Holder}}{\text{WANES}}$

= $\frac{1800000}{2000000}$

= ₹ 0.9

2017 → Bonus shares = 4000000

Basic EPS = $\frac{6000000}{6000000}$ = ₹1

Restated EPS of 2016 = $\frac{1800000}{6000000}$ = ₹0.3

II Right Shares

→ In case of right shares, it is issued to the existing share Hol. in a particular ratio, at a price lower than mkt. price.

→ There is Hidden Bonus Element which needs to be adj. while finding EPS.

→ The steps to be followed are

→ Step 1 :- Find theoretical Ex-right price

→ = (cum-right price (right shr × shr. req. to buy one right share) + price × right shr) / shr needed for right share + right share

→ Step 2 :- cal. right adj. factor (RAF)

→ = cum right price (i.e fair v. prior to right issue) / Theoretical Ex-right price

→ Step 3 :- In the year preceeding the year of rights issue, RAF should be multiplied to the shr. outstanding for entire year in order to find WANES. Then the restated Basic EPS

In the year of rights issue, RAF will be multiplied to outstanding shr at beginning of period for period starting from 1st date of F.Y. till date of rights issue. & after rights

issue the total no. of shr. including rights will be multiplied by remaining period.

This WANES will be used for finding Basic EPS of that year

eg

	2022	2023
N.P	200000	300000
Eqr O/S	10000	10000

On 1/4/23 right shr are issued at 1:2 @₹15
cum right mkt price ₹45

2022 Basic EPS = 200000 / 10000 = ₹20

2023 Rights issue

Step 1 Theoretical Ex right price = (45×2) + (15×1) / 2+1

= ₹35

Step 2 RAF = 45/35 = 9/7

Step 3

2022 N.P → ₹200000

WANES = 10000 × 9/7 = 12857

Basic EPS (Restated) = 200000 / 12857 = ₹15.556

2023 NP → 300000

WANES = (10000 × 9/7 × 3/12) + [(10000 + 5K) × 9/12] ← right shr
(NO RAF)

= 11464

EPS = 300000 / 14464

= ₹20.74

Illus → 4

2016

Basic EPS = 1100000 / 500000 = ₹2.2

2017

Right issue → 1:5 at ₹15

cum-right price = ₹21

Step1 → Theoretical Ex-right price = (21 × 5) + (15 × 1) / 5 + 1

= ₹20

Step2 RBAF = 21/20 = ₹1.05

Step3 2016

N.P = ₹1100000

WANSH = 500000 × 1.05 = 525000

Basic EPS (Restated) = 1100000 / 525000 = ₹2.0952

2017

WANES = (500000 × 1.05 × 2/12) + [(500000 + 120000) × 10/12 × 1.25]

= 14350 715000 587500

Basic EPS = 1500000 / 14350 + 650000 + 587500 = 1500000 / 587500 = ₹2.55

III Diluted EPS

→ Diluted EPS is the worst / lowest possible EPS if all the potential Eq. shrs are converted into Actual Eq. shrs

→ The financial instruments issued by entity, that have the potential to become Eq. shrs are called Potential Eq. shrs

eg conv. pref shrs, conv. Debentures, Stock options/ warrant

→ Conversion of potential Eq. shrs should reduce / dilute the EPS. If it increases the EPS then it is Anti-dilutive & should be ignored for the purpose of diluted EPS.

→ Potential eq shrs are to be included in diluted EPS cal.:

→ From: Start of year OR date of issue whichever is later

→ For diluted EPS → First directly take Denomi. of Basic EPS
* Role of Diluted EPS → To find impact of potential

→ Upto : End of year or date of conv. whichever is earlier

→ Diluted EPS in case of Convertable pref. shares.

→ Diluted EPS
= PAT attributable to Eq shr H + Pref div (1 + DDT) / WANES of Basic EPS + shares on conv. of pref shr (Time factor to be considered)

→ DDT Not applicable from 2019

→ Diluted EPS in case of Convertable Debentures / Bonds.

→ Diluted EPS
= PAT Attributable to Eq. Shr + Int. (1 - t) / WANES of Basic EPS + Shares on conv. of Debentures

→ t = Income tax rate (if given)

Warrants / options

→ Warrants / options are issued by entity, whereby the option holder has a choice (option) of buying the Co. eq. shrs at pre-determind exercise price

→ NO int. / div. is payable to option holder till the time the options are to be considered as potential eq. shr

→ Diluted EPS = PAT Attrib to Eq. shr + Nill (No cost / savings) / WANES of Basic + Free Element in option

→ Free Element in option = Shares to be issued on option exercise less (No. of options × Exercise Price / Avg Mkt price)

→ Above cal. is based on understanding that if co. wants to Buyback its shr using the proceeds from the Issue Shares given to option holder on exercise, it can find free element which will potentially reduce EPS.

→ eg If co. had issued options for 1000 eq. shr @ ₹20 each. Estimated Avg mkt price = ₹50.
Amt received from option Hold. on exercise
= 1000 × 20 = ₹20,000
No. of Eq shr co. can buy-back using abv. proceeds
= 20000 / 50 = ₹400
∴ Free element in option = 1000 - 400 = 600

Illus → 5

Diluted EPS = 10000000 + (1200000 -

Diluted EPS = $\frac{\text{PAT attributable to Eq. Shr} + \text{Int}(1-t)}{\text{WANES in Basic EPS} + \text{Shares on conv. of Deb.}}$

$= \frac{10000000 + (1200000 - 360000)}{5000000 + (100000 \times 10)}$

$= \frac{10840000}{6000000}$

$= ₹ 1.81$

Dilutive since Basic EPS is ₹2.

Illus → 10

Basic EPS = $\frac{\text{PAT attributable to ESH}}{\text{WANES}} = \frac{7500000}{1000000} = ₹ 7.5$

Diluted EPS = $\frac{\text{PAT attri. to Eq Shr} + \text{Int}(1-t)}{\text{WANES on Basic EPS} + \text{Share on conv. of Deb.}}$

$= \frac{7500000 + 800000(1-0.3)}{1000000 + 100000} = ₹ 7.26$

Dilutive

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Illu → 11

Basic EPS = $\frac{\text{N.P for Eq Shr H}}{\text{WANES}} = \frac{10000000}{1000000} = ₹10$

No of Potential eq shr on conv of 10% conv. deb

= Deb : Eq
1000000 : 10
⟶ 100000

Diluted EPS = $\frac{\text{N.P for Eq Shr H + Int (1-t)}}{\text{WANES of Basic + No. of Shr of Potential}}$

$= \frac{10000000 + 500000(1-0.3)}{1000000 + 1000000 \times \frac{6}{12}}$

= ₹6.9 (Diluted)

Illus → 6

Basic EPS = $\frac{1200000}{500000} = ₹2.4$

Free element in option = 100000
= 100000 − (100000 × 15/20)
= 25000

Diluted EPS = $\frac{1200000 + 0}{500000 + 25000} = ₹2.2857$ (Diluted)

Illu → 16

As per the proxi. of AS 20 EPS, when N.P from continuing ordinary operations & discontinuing operations are given then the N.P/loss from discontinuing op. should be included in cal. of EPS only if Diluted EPS from continuing op. is dilutive.

In this case S.P from ordinary continuing op = ₹240000
o/s Eq. shr on 31-03-20X1 is equal to 1000 shr
∴ Basic EPS = $\frac{240000}{1000}$ = ₹240
Potential Eq. Shr = 200 shr ∴ Diluted EPS = $\frac{240000}{1200}$ = ₹200 (Dilutive)
∵ Diluted EPS from continuing ordi. operation is Dilutive, the N.P/loss can be in from discontinuing op. should be includ. in cal. of Basic & Diluted EPS.
Net L from op Discontinu. op = ₹360000
∴ Total Net L from Both op = ₹120000 (36L − 24L)
∴ Overall Basic EPS = $\frac{(120000)}{1000}$ = ₹(120)
∴ Diluted EPS = $\frac{(120000)}{1200}$ = ₹(100)

Assets

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AS 26 → Intangible Assets

I. Criteria for Intangible Assets

- Identifiable
  - Capable of being sold Separately
  - Arises due to license (Contractual / legal rights)
- Non-Monetory
  - cannot be conv. into a fixed / determinable amount of money (AS 11)
- Lacks Physical Substance.
  - cannot touch, fell, see

e.g. →

a) Telecom license is IA (All 3 conditions satisfied)

b) Patent to produce Crocin is IA (All 3 condin satis.)

c) Bank Balance is not IA (1 & 3 satis. but 2 not)

d) Deferred Revenue Expenditure (Big Adv. exp.)

→ It cannot be shown as IA as it does not satis. Condition 1. It should be expensed (Debited) to P&L A/c as & when incurred / advertisment is displayed.
This is irrespective of fact that the advertisment gives future economic benefits or not.

II. Recognition of Intangiable Assets.

Conditions to be satisfied

1) should meet the criteria of IA
2) should be Controlled by entity & should give future economic benefits (Features of an Assets)
3) Cost should be reliably measurable

key Points :-

a) Self generated goodwill is not recognised as an IA as its cost not reliably measurable.
Purchased goodwill is recognised as an I.A as its cost is reliably measurable.

b) In case of Human Resource it is not recognised as an I.A as the entity can not control them.
But the rights to use the services of these entities is recognised as an I.A.

III. Initial Recognition of IA

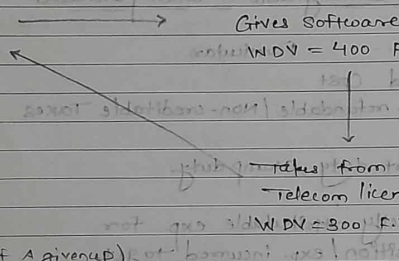
↳ IA should be initialy recorded at cost

→ Cost of Intangiable A when purchased

Particulars	₹
Purchased Cost	xxx
Add: Non-refundable / Non-creditable Taxes	xxx
eg. import duty, stamp duty.	
Add: Directly attributable exp. for aquisition / exp. incurred to get the asset to ready to use condi^n (eg: legal fees)	xxx
less: Trade Discount	(xxx)
∴ Initial Cost of IA as per AS-26	xxx

Special Case :- Barter
↳ In case of Barter / exchange the IA should be recorded at the fair value (mkt. value)
It is generaly the fair value of asset given up or F.V of asset received which ever is more reliable.
If nothing is mentioned about reliability then folowing order is used
First choise → F.V of asset given up.
Second choise → If F.V of asset given up is not given

then use F.V of asset received
Third choise → If F.V's are not given then use WDV of asset givenup.



(F.V of A givenup)
Telecom license A/c Dr. 500 ②
To Software A/c (WDV of A G) 400 ①
To Profit on Exchange A/c (P&L A/c) 100 ③

IV. Subsequent Expenditure

Regular Maintenance	Increases life / productivity beyond what is originally assessed
Expensed to P&L A/c	Capitalize with the I.A
Maintenance Exp A/c (P&L) Dr. To Bank A/c	I.A A/c (B/S A) Dr. To Bank A/c

V Research & Development

Research Phase → Development Phase

It is the ideation phase. The activity of creating/inventing a new product / process.

It follows successful research, it is the process of conv. the result of succ. res. into a mktable product.

Expensed to P&L A/c (As future econ. benefits are not certain)

Capitalized to I.A if:-
a) Technically posi.
b) Legally permissible
c) Financially feasible
d) Cost is measur.

Expensed to P&L A/c if any of the condition for capi. is not satis

VI. Amortisation

It refers to writing off the I.A over its useful life.
It is similar to Depri on T.A.

I.A has finite life	I.A has Infinite life
eg. legal life of a patent purchased for 8 yr.	JLR brand acquired by TATA. its usage is for ∞ period
Amortn on systematic basis based on eco. patt. benef.	If no sys. basis is aval. then on SL basis Over a finite life or 10 yr which ever is shorter	Syst basis if aval. over 10 yr	SL basis over 10 yr

Note 1 → 10 yr limit unless proven otherwise
AS 26 has a rebuttable prescription (cannot be changed unless proven by other party) that the useful life of an I.A cannot be > 10 yr.
∴ Unless an entity can specifically prove with evi. that the life of an I.A is > 10 yr., we always amortize the I.A over the prdt life or 10 yr whichever is shorter.

Note 2 → Subsequent change in estimate of useful life / method of Depri.
In case the estimate of useful life / method of Depri changes subsequently, then prospectively adj. the amortisation for future yr.
In case of change in useful life the amortisation will be based on remaining WDV & remaining useful life.

VII. Recoverable Value of an I.A.

An I.A is held for use in the ordinary course of business, unlike inven. which is meant for sale.
∴ The I.A is always valued at the ledger balance.
But if in the future expected cash flow is given along with the annuity factor then impairment testing should be done using the following steps.

→ Step 1: Cal. the recoverable value

Recov. value = Expected future cash inflow × Annuity factor

→ Step 2: Cal. ledger bal. of the I.A

→ Step 3: Value I.A at

a) Ledger bal. / or

b) Recoverable Value (whichever is lower)
→ ledger bal.

step 4: If cost is grater the reco. val. then
↳ Impair loss = ledger bal. − Recover val.
↳ the impair. loss should be trans. to P&L A/C.

step 5: If the ledger bal. is less than the recov. val. then
↳ No. impair. loss.

→ Impairment is defi. as reduction in the future earning capacity of the Asset (AS 28)

→ Impair. testing should be done only when their is an indicator.

→ eg. Decre. in value due to Technological change
↳ Technological ch. is an indicator of impairment.

eg. Redu in value of the license to sell chemicals followed by due to recent change in Law.

Q.9. →

Provo. → As per AS 26 on Intangiable Assets their is a rebuttable assumption that the life of an Intangiable Asset for the purpose of Amortisation cannot be grater than 10 years unless an entity can specifically prove with evi. that the life is grater than 10 years.

Appli → In this case Base ltd. has aquired an intangiable asset on 01-04-2008 & has amortized the asset on straight line bases considering useful life of 12 years., without any evi. therefor, the treatment done by Base ltd is wrong.

→ therefor, Base ltd should amortize the Asset on useful life of 10 years.

Calculation of ledger bal. as on 01-04-2011

Insti. cost as on 01-04-2008	112 L
less: Amortisation for 3yrs till 01-04-2011 $\left(\frac{112}{10} \times 3\right)$	33.6 L
Therefor ledger bal. as on 01-04-2011	78.4 L
Actual ledger bal. as on 01-04-2011 i	85 L

→ Therefor access amortisation to be charged for last 3 years.
= 85 L − 78.4 L = ₹6.6 L

→ This is an error as it is violation of the AS.
∴ the journal entry to be passed.
→ Prior Period Items (Amort.) A/C Dr 6.6 L —
To Intangiable Asset A/C — 6.6 L

∴ The Impairment loss of ₹41840 should be expensed to Statement of Profit & loss account

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III. 6

Since in question cost of capital, Annuity factor & future cash inflow are given, impairment testing should be done.

Steps to be followed

Step 1: Find recoverable value

Recoverable Value = Expected future cash inflow × Annuity factor

∴ = 200000 × 3.7908

= ₹758160

Step 2: Ledger Balance as on 01-04-13

= Cost − Amortisation

= 800000 − 0 = ₹800000

Step 3: Value of IA as on 01/04/13

ledger balance = ₹800000

or

Recoverable value = ₹758160

(which ever is lower

∴ Revised ledger balance of IA = ₹758160

Step 4: Impairment loss = ledger bal − Recov. Value

= 800000 − 758160

= ₹41840 — (P&L A/c)

AS-6 is merged → Depri.

AS-10 → Property, Plant & Equipment (PPE)

I. Conditions for PPE

a) Taggible (intangible assets cov. by AS-26)

b) Held for use under normal course of business like production, admin, selling, distribution, held for renting out, etc

c) Expected life > 12 months.

- key points

1) Items held for sale in ordinary course of business are to be taken as inventories (AS-2) & not PPE.

2) AS-10 applies to Material items of PPE. Insignificant / immaterial items should be expensed to P & L A/c

3) PPE also includes items like pollution control equipment (wastage treatment plant) & assets for employee benefit (Singhaniya school for children of Raymands mill workers). The PPE need not gen. rev. directly.

II. Scope Exclusions

1) Biological assets for agricultural activities (Except Bearer plants)

2) wasting / depleting assets (Mineral rights, exploratory & ivaluatory assets linked to mining operation)

3) If any other AS prescribes a specific accounting treatment then AS-10 will not apply. (e.g. AS-19 for financing lease)

III. Biological Assets For Agricultural Activities.

	Living Plants	Living Animals.
Bearer Plants	other than Bearer Plants	AS.10 does not apply.
AS-10 applies	AS-10 does not apply	

- Bearer plants are:

1) Plants which bear agri. produce other than itself for sale (Coconut Tree / Mango Tree).

2) Expected to bear produce over more than 12 months. Hence, annual crops like wheat grain plants, rice plan^n. whose produce are wheat & rice are not treated as bearer plants for AS-10 as they are uprooted after each cycle <12

IV. Stores & Spares

a) Meets PPE criteria especially life is more than 12 months
→ PPE (AS-10 apply)
eg. spare tyre in a car

b) If life < 12 months, does not meet PPE criteria
→ Treated as inventories (AS-2 apply)
eg. screws, nuts, etc

V Initial Recognition - Cost

1) When PPE is Purchased

Purchase Price (cost, non-cr taxes)	xx
(+) Directly attributable Exp*	xx
(+) Present Value of Decommissioning/ site restoration Exp.	xx
(-) Trade Discount / Rebate	(xx)
Total Cost	xx

2) When PPE is self constructed

Direct Material	xx
(+) Direct Exp	xx
(+) Direct labour	xx
(+) Prodn OH (Fixed / variable)	xx
(+) Non-Cr Taxes	xx
(+) Directly attributable Exp*	xx
(+) Present Value of Decommissioning / site restoration Exp.	xx
(+) Borrowing cost (if qualifying asset as per AS-16)	xx
(-) Trade Discount	(xx)
Total Cost	xx

* Directly attributable Exp. includes:
Exp. incurred to bring the asset to the condn & location necessary for it to be capable of operating in the manner intended by management.

a) Cost of site prep.
b) Initial del. & handeling cost
c) Installation & assembly cost
d) Costs of employee benefits arising directly from the construn / acquisition of item of PPE.
e) Cost of testing whether the asset is funcn properly after deducting the net proceeds from selling any item produced while bringing the asset to that

location & condin. (such as samples prod. when testing equip.)
f) Professional fees.

* Directly attributable Exp does NOT include

a) Inauguration Exp.
b) Relocation Exp.
c) Admin, selling & Distri.
d) Cost of training / retraining employees
e) Initial operating losses / Exp. after the asset is ready to use
f) Cost incurred while an item capable of operating in the manner intended by management has yet to be brought into use or is operating at less than full capacity.

VI Special Cases in Inital Recognition

Barter

It has commercial substance	It lacks commercial substance
The asset received should be recorded at: 1) fair value of asset given up 2) fair value of asset received 3) WDV of asset given up	Asset received should always be recorded at carring value (WDV) of asset given up

Note:

If nothing is mentioned in question then transaction is assumed to have commercial substance

VII Income earned during the period when asset is not ready for use

If directly attributable to construction expenses then reduce from cost of asset.	If not directly attributable to construction expenses then cr. to P&L A/C
eg. Income from sale of scrap.	eg. Income from usage as parking lot, rent from film set

VIII Losses

Normal	Abnormal
ADD to cost (capitalised)	Exp. to P&L A/C

IX. Subsequent Valuation at each B/S date

Valuation Model

Cost Model		Revaluation Model	
original cost	xx	Fair value at subsequent intervals	xx
(-) Acc. Depri	(xx)	(-) subseq. Depri	(xx)
Carring value	xx	Carring value	xx

1) Sellection of Model should be done for the entire class of PPE.
The entity can not use diff models within the same class.
eg. Building, Furniture, Land, Bearer Plants, etc.

2) Revaluation should be made at sufficient intervals or regularly.
It depends on changes in Fair value

If Volatile	If stable
Revaluation every year	Reval^n every 3-5 years

X. Accounting Treatement of Revaluation

When the entity follows accumulated depri. method then it has following two options:

Proportionate Method			Direct Method (Net off)	
	old	New	Acc. Dep^n A/c Dr	40 —
original c	100	150	To Asset A/c	— 40
	[WDV 60 40 OC 100 ?]			
(-) Acc. Depri.	(40)	(60)	Asset A/c Dr	30 —
	[WDV 60 90 Acc. dep 150 ?]		To Reval. Res A/c	— 30
Carring value	60	90		

In the above eg asset is revalued from ₹60 to ₹90

Asset A/c	Dr	30 —
To Acc. Depri. A/c		— 20
To Reval. Res A/c		— 30

XI Treatment of Effects of Revaluation

Initial upward Reval^n. (100 → 150)

+50 → Transf. to Reval^n Res / Surplus

Initial Downward Reval^n (100 → 80)

Subsequent upward Reval^n. (150 → 160)

+10 → Transf to Reval^n Res.

Subsequent downward Reval^n (150 → 130)

-20 → from Revl^n Res

(150 → 90)

-60

-50 Transf to Reval^n Res

-10 Transf to P&L

-20 Transf to P&L A/c

Sub. Downward Reval^n (80 → 50)

-30 → Transf to P&L

Sub. upward reval.^n, (80 → 90)

+10 Transf to P&L

(80 → 115)

+35

+20 Transf to P&L

+15 Transf to Reval^n Res

No component shall be depri. for more than life of whole asset.

→ change in estt. → Prospective
→ change in Alcing policy → Retrospective } AS

XII. Depreciation

1) Depri. should be applied from the date when the asset is ready for use & till the time it is disposed of, or it is fully written off to its residual value

Not when it is put to use.

2) selection of method of Depri. (SLM, WDV, units of prod.^n) is based on Pattern of Eco. Benefits that are exp. to be received

3) change in estt. useful life & Salvage value is treated as change in estt. hence, it should be prospectively applied. (AS-1)

4) change in method of Depri. due to change in pattern of eco. benefits is also change in estt. Hence, it is prospectively applied. (AS-1)

5) Component method of Depri.

a) It is used when:
→ the major components are identifiable &
→ they have diff. useful life compared to the life of main asset.

b) BIS presentation need not be separate for each component

c) Each component should be depri. separately consid^n its useful life

d) Same principle is used in case of major inspection / major overhaul.

eg. A Flat along with its furniture is worth ₹1.2 cr.
Cost of ~~the~~ Flat is ₹1 cr with life of 50 yr.
Furniture is for ₹0.2 cr, life of 10 yr.
∴ The Flat will be depri. over 50 yr
(1 cr. / 50 yr)
Furniture will be depri over 10 yr
(0.2 cr / 10 yr)

→ WDV on 1/4/23 — 18760000
(-) Selling price (Lease) — (4250000)
loss on sale — 14500000
Exp to P&L

Bal. in revln. res ₹6250000 (same as case 1)
will be transf to rev. res.

I → 23

1/4/18 : 25000000
(-) Depri. for 2 yr [2.5 cr / 10 yr × 2 yr] — (5000000)
1/4/20 — 20000000
(+) upward revln [3 cr − 2 cr] — 10000000 ← Revln. res.
Rev. carrying value 1/4/20 — 30000000
(-) Depri. for 3 yr [3 cr / 8 × 3] — (11250000)
WDV on 1/4/23 — 18750000
(-) S.P — (11250000)
loss — 7500000 ← Exp. to P&L

Bal. in revln. res on sale
Bal. 1/4/20 — 10000000
(+) Addi Depri due to upward revln for 3 yr [3 cr / 8 × 3 − 2 cr / 8 × 3] — (3750000)
Bal. in reval. res on sale — 6250000 (Transf to revenue res)

XIII

Subsequent Expenditure

Repairs & maintainence	Increase life or Efficiency beyond the originally assessed level	Major replace/ major inspection/ major overhaul
↓	↓	↓
Expensed to P&L A/c	Capitalized	WDV of Asset xx
↓	↓	(+) cost of New Part xx
(P&L) → Repairs & Mai. A/c Dr	Asset A/c Dr To Bank	(-) WDV of old (W.N→1) Part (xx)
To Bank		Revised WDV xx

eg. Cost of PPE = ₹10000 (yr=0) life = 10yr
Dis. factor (i) = 10%
New part pur at end of 4yr ₹3000
Scrap value of old part at end of 4yr = ₹500

Initial cost	10,000
(-) Depri. ($\frac{10000}{10} \times 4$)	(4000)
Carring value	6000
(+) cost of New part (PPE A/c Dr 3k / To Bank A/c 3k)	3000
(-) WDV of old part (Bank Dr 500 / Loss on sale 729 / To PPE 1229)	(1229)
Revised WDV	7771
Depri. for 5th yr ($\frac{7771}{6}$)	₹1295 p.a

W.N → 1
Cal. of WDV of old part

cost of New part (A) = ₹3000
cost of old part before 4 yr (P) = ?

No. of yrs (N) = 4 yr
Dis. factor (i) = 10% = 0.1

Formula:-

$A = P(1+i)^n$

$3000 = P(1+0.1)^4$

$3000 = P(1.4)^4$

$P = 2049$

∴ cost of old part before 4 yr = 2049
(-) Depri. for 4yr ($2049/10 \times 4$) = 820

∴ WDV of old Part ₹1229

*** As per AS-10 for finding cost of old part, following order of pref is used
1) Break-up in suppliers invoice
2) If 1) is not avail. then F.V of old part at the date of pur
3) If 1) & 2) are not avail. then use cost of New part, dis. factor given & find cost of old part using formula $A = P(1+i)^n$

Applicability Of Accounting Standard

I Applicability of AS

Companies	Non-company entities. (Sole proprietor, Partnership firms, HUF, LLP)
AS is Mandatory	AS is optional.
Sec 129(1) read with sec 133 of Co. Act, 2013 reqr. all co. to present their financial statements in accordance with AS.	If a firm decides to get its accounts audited by a CA then it will need to prep. its financial stat as per AS.

II Companies classified as

SMC (Small Medium co.)

Conditions:

1) Non listed / under proc of listing, &
2) Not a Bank, Fin. insti or an insurance co., &
3) Turnover should not be more than 250 cr., & During immediate preceeding year., &
4) loan taken should not be > 50 cr., &
5) Should not be parent / subs. of Non-SMC

NON-SMC

If an entity does not meet condi for being classified as SMC then Non-SMC.

Key Points:

1) If an entity is SMC then it can claim full / partial exemptions from applications of certain AS like:
3, 15, 17, 19, 20, 21, 25, 27, 28, 29

2) In case a non SMS subsequently becomes a SMC then it will not be entitled to the above exceptions / relaxations unless the co. remains at SMC for 2 consicutive years.
(PVR → Temp. sale down due to covid)
(KODAK → Perm. sale down due to technological.)

III In case of Non-co. entities

Level → 1	Level → 2	Level → 3	Level → 4
large size enti.	Medium size enti.	Small size enti.	Micro entity
1) listed / proc of listing, or	1) Turnover 50cr < x < 250cr (or)	1) Turnover 10cr < x < 50cr (or)	Non co. entities which are not
2) Bank, Fin. insti, Insu. comp. (or)	2) loan taken 10cr < x < 50cr (or)	2) loan taken 2cr < x < 10cr (or)	level 1 or 2 or 3.
3) Turnover (excl. other income) > 250cr. or	3) Parent / Subsi of level 2 entity	3) Parent / Subsi of level 3 entity	
4) loan > 50cr or			
5) Parent / sub. of level. 1 entity			

Key Points:

1) lvl → 1 entities are required to comply with All AS with full.

2) Certain exceptions have been provided to lvl → 2, 3 & 4 (Non-co. entities)

3) In case, a lvl → 1 subsequently becomes lvl → 2, 3 or 4., then it will not be entitled to above exemptions / relaxations unless the co. remains as lvl → 2, 3 or 4 for 2 consicutive years.

→ Sec 8 co.
→ Doing fully charitable. acti. → AS not apply
→ Doing any commercial acti → AS apply (Renting out)

n trade → F.G pcm. karta hai & bechta hai
trading not manufacturing) (Dmart)

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AS 2 → Valuation of Inventory

I. Meaning / conditions

1) Inventories includes assets held for the purpose of :-

a) Sale in ordinary course of Business, or

b) in the process of production for such sale, or

c) for consumption in the prodn of goods or services for sale.

It also includes maintenance supplies, consumables & other spares not covered under AS-10.

(eg: a) F.G, b) Stock-in-trade, b) WIP, c) RM, d) Stores & Spares, e) loose tools?)

2) AS-2 does not cover :-

a) WIP of construction contracts (AS-7)

b) WIP of service provi. like Software dev., medical ser., marchent banking, etc (AS-2 cov, only physical ones)

c) Shares, Deb., etc. held as stock in trade by stock trader (AS-13)

d) INV. of producers of livestock & farm prod (Milk from cow, fruit from plants, as it is diffi. to estimate its cost.

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II. Initial Recognition Cost

1) Purchased

Purchase Price	xx
(-) Trade Dis.	(xx)
(+) Non-cr Tax	xx
(+) Directly Attri. Exp. (incurred to bring the inv. in desired location & condn)	xx
Cost	xx

2) Manufactured / Conversion

Direct Materials	xx
(+) Direct labour	xx
(+) Direct Exp.	xx
(+) Variable Prod. OH	xx
(+) Fixed Prod. OH	xx
(+) Any other directly attri. Exp. (cost of design)	xx
(+) Non-cr taxes	xx
(+) Borrowing cost (if qualifi. asset → AS 16)	xx
Cost	xx

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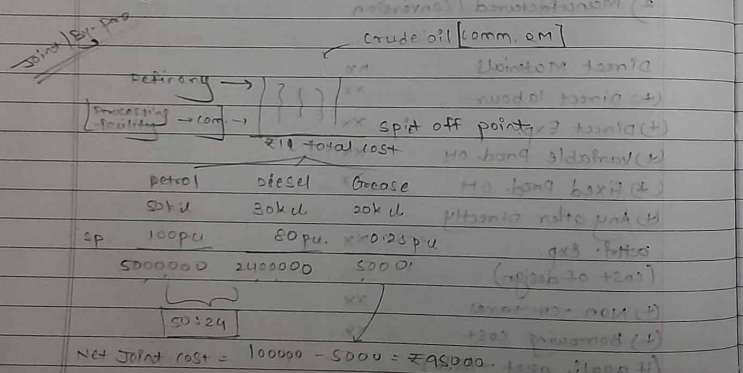
Key Points

1) Following will not be taken in cost of inventories :-

a) Abnormal loss
b) Storage cost (unless prodⁿ process req. such storage) eg. cheese, wine.
c) Admin OH
d) Selling & Distri. OH

2) Intangible assets used in prodⁿ. should be Amortised & included as part of inv. cost. eg. Patent right for prodⁿ of vaccins.



Actual output V/S Normal output whichever is Higher

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3) Net Joint cost should be allocated to the main prod. (Petrol & Diesel) in the ratio of their sale value at split off point. or sale value at complition or physical units.

Net Joint cost = Total Joint cost (100,000) − NRV of By-Prod. (5,000)

III. Calculation of fixed Prodⁿ OH absorption rate p.u to be included in the initial cost of inventories.

A) Normal loss

Should form part of Total cost for this purpose rate p.u is inflated.

Normal op. (NO) = Expected op. − Normal loss

fixed Prodⁿ. OH absorption rate = Total fixed prodⁿ / Normal op.

B) Abnormal loss / Abnormal Gain

(i) When actual op. < normal op. then thir is abnormal loss.

Abnormal loss units = Normal op. (NO) − Actual op. (AO)

Fixed prodⁿ OH absorption rate = Fixed Prodⁿ OH / NO (∵ it is higher)

Abnormal loss is transf to. P&L A/C

(ii) When actual op. is > normal op. then thin is Abnormal Gain

Abnormal Gain Units = AO - NO

Fixed Prodⁿ OH absorption rate = Fixed Prodⁿ OH / AO (∵ it is higher)

Whenever AO ≠ NO then for absorption rate always use Higher value

IV Cost Flow Assumptions (Methods of valuⁿ.)

1) Inventory not interchangeable
   - Specific Identification Method
     eg Painting, unique items

2) Inventory is interchangable
   - (i) General Method
     - a) FIFO b) Weighted Avg.
   - (ii) Special cases (optional)

Standard cost Method
- it is used by manufacturers.
- it is used when standard cost approximates actual cost

Retail sale price Method
- it is used by retailers
- Selling price xx
- (-) Gross Margin (xx)
- cost xx

Note:-
LIFO method is not permitted as per AS-2

V Valuation of inventories

1) Finished Goods / Stock-in-Trade / WIP.
   - it is always valued at cost or NRV whichever is lower.
   - cost is cal. by FIFO / Weighted Avg
   - NRV of F.G / Stock-in-trade = Estim. S.P − Estim. Selling Exp.
   - NRV of WIP = Estim. S.P − Estim. Selling Exp. − Estim. cost of compliition of WIP.

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2) RM

↳ F.G is Profitable
↳ RM is always valued at cost

F.G is loss making
↳ RM is valued at lower of cost / replacement cost
(aaj inka may kharidne jayega toh kitne mai milega)

∵ the firm does not sell R.M in ordinary course of Busi., It will be diff to find the selling price / NRV.
∴ Replacement cost is used

→ Replacement Cost → current purchase price of R.M

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Illus → 3

Input = 5000 MT
Normal loss = 5%
Actual loss = 300 MT

∴ AO = 5000 − 300
= 4700

Input = 5000 MT
(-) Normal = (250) MT
loss @5% [5000 × 5%]
Normal op. 4750 MT
(NO)
(-) AO (4700) MT
Abnormal loss units 50 MT

∴ Total cost of input = 5000 MT × 1000
= ₹ 50,00,000

Actual op. = 4700
Normal op. = 4750

Eff cost per unit = Total cost of input / AO | NO → Higher
= 50,00,000 / 4750 = ₹ 1052.63

Assuming nothing is sold

Val^n of cl. stock = AO × Eff cost pu
= 4700 × 1052.63
= ₹ 49,46,361

Val. of Abnormal loss = Ab. loss units × Eff c. pu
= 50 × 1052.63 = ₹ 52631.5

∴ the val. of Ab. loss will be exp. to P&L A/c

Framework for Preparation & Presentation of Financial Statements.

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I Fundamental Accounting Assumptions

→ While preparing financial stat, the following assumptions are implied.

a) Going Concern

b) Accrual

c) Consistancy

a) Going Concern

It refers to the situation where it is anticipated that the co. will continue its operations in the foreseeable future (4→5 yrs.)

All accounting treatments are usually based on Going concern assumption being valid

However, in case going concern assumption is violated ie if it will not be valid then the entire financial stat. are prepared on NRV basis

b) Accrual

(Goods sold / services rendered & right to rec the money is estab

It means the entity should record the income earned during the period irrespective of wheather it is received

or it is receivable

benefits enjoyed. It also means the entity should record the exp. incurred during the period irrespective of wheather it is ~~payed~~ paid or it is payable

c) Consistency

↳ It means the co. will follow the same set of accounting policies & princepals in the current period which it has been following in the las years.

↳ This will ensure Comparability
ie. interFirm & intra firm comparisions.

↳ the accounting policy can be changed only if it is
required by statutes.
required by accounting standards
required by the entity feels that it will lead to better presentation & transparancy of financial info. to users of the financial statements.

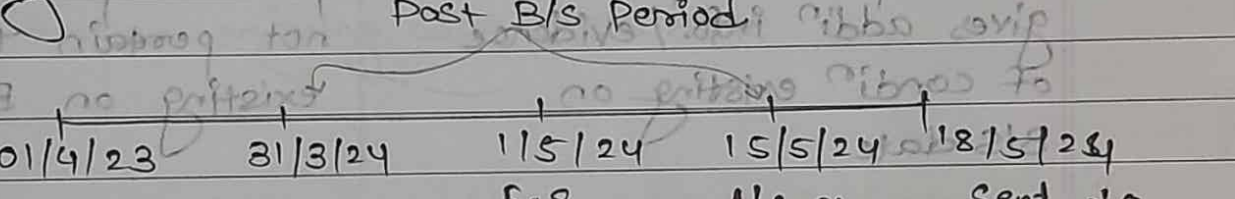
AS-4 → Contingencies & Events Occurring after Balance Sheet Date

I. Important Terms

A) Post Balance sheet Period

→ The period from the reporting date (B/S date) till the date of approval of accounts by the competent authority (BOD).

↳ eg.



B) Contingencies

→ It represents the possible obligation / resources that arise from past events & the outcome of which can be confirmed by future events which are beyond the control of entity.

rep. in AS-29 (conti. assets)

II Post B/S events.

↳ These are the events which occur during the post balance sheet period

↳ It is classified as:

Adjusting Events	Non-adjusting Events
→ Material events occuring in the post B/S period which gives addn info. / evidence of condn existing on B/S date.	→ Material events occuring in post B/S period which do not pertain to condn existing on B/S date.
→ Adjusted in accounts of the reporting period (period for which the reports are prepared)	→ Not adjusted in accounts of reporting period (period for which the reports are prepared)
→ It means adjustment to the assets & liabilities are required.	→ It means adjustment to assets & liabilities are not required.
→ Disclosure in financial statement is required	→ Material Non-adjusting events to be disclosed in the report of the approving authority (Director's report).

No adjustment of B/S in condn with

→ e.g.
Bankruptcy of debtors in post B/S period (Assuming uncertainty existed on B/S date) ↳ doubtfull

cash theft occuring before B/S date but detected in post B/S period

court verdict in post Bal/S period for an ongoing case

→ e.g.
Loss due to fire / natural calamities in post B/S period

Amalgamation agreed in post B/S period (Irrespective of fact that negociations were ongoing on B/S date)

Cheques collected after B/S date even if dated before B/S date

III Exceptions to Adjusting / Non-adjusting Events

A) New events occuring in post B/S period (Earthquake) which results in an entity changing the Going Concern assumption are considered as Adjusting Events even though they pertain to a situation after B/S date.

B) Dividend declared after B/S date but before the financial statements are approved, would be recorded in the year in which it is declared & not in the year for which it is declared.
It will not be treated as adjusting event as it is Proposed dividend & it will be disclosed in the Notes.

Eg → Div. decl. on 10/4/23 for the year 2022-23 will be recorn. in the books in 2023-24 & not 2022-23.

AS-5 → Net Profit / loss for the period, Prior Period items & Changes in A/c'ing Policies

Give prov. of Ex.O only baki sab O.

I Net Profit / loss for the period

a) Ordinary Items

↳ Ordinary items are connected with usual business activities including incidental activities.

Exceptional Items
→ Are material items connected with the ordinary activities of business but which req. a separate disclosure due to their frequency & size
→ eg. Payment under voluntary retirement scheme, P&L on sale of asset, cogge revision, etc

Others
→ the items grouped along with other items of similar nature under appropriate headings & donot req. a saperate disclosure.
→ eg. Purchases of R.M, cogges, salaries, adv., Int, etc

b) Extra Ordinary

↳ the items which are clearly distinct from the usual business activities.

↳ It needs to be separately disclosed in the statement of P&L as a saperate cline item

↳ eg. loss due to natural calamities, fire, refund of Govt. Grants, winning of lotery, etc

Exam Note

i) Extra Ordinary items are clearly distinct from regular business & they need to be disclosed saperately & identified.

ii) If the given case is of Ordinary items then we can write the following Note in Exam.

↳ "The given item is linked to the ordinary activities of the entity & will have to be separately disclosed if Material."

II Prior Period Items

→ These are errors / omissions / mistakes of the previouse years which are detected in the current year

→ PPI needs to be separately disclosed in the statement of P&L as a separet line item.

→ PPI is a clerical mistake & mistake of fact & does not involve any judgement or estimate

→ eg. Double counting of sales, omitting to record depn., detection of theft after >1 yr, etc

III Accounting Estimates (It involves judgement & predn)

→ It requires some level of judgement / prediction

→ When a new info. is obtained, a/c'ing estimate will change.

→ A change in accounting esstimate should be applied prospectively.

→ A change in accounting estimate is never considered to be a PPI.

→ eg Change in method of depri. due to change in pattern of Eco. benefits, change in estimated useful life of an asset, % for R.D.D, etc

III Accounting Policies

→ Accounting principles & rules followed in the preparation of the financial statements are called accounting policies.

→ eg Methods of stock valuation (FIFO, WAM, etc), Valuation Methods for PPE (cost / revaluation model), Methods for preparation of cash flow statements (direct / indirect method)

→ Accounting policies should be consistently followed every year.

→ Accounting policies should be changed .... chap → 2

→ It should be applied retrospectively

→ If impractical to apply retrospectively then a disclosure should be given in notes explaining the impracticability

→ Impracticability refers to the inability to retrospectively apply a change after putting all required efforts in doing so.
It may arise due to lack of availability of data
eg loss of data dere to Virus attack

→ A change in accounting policy refers to the application of a New policy to same set of transactions.

→ eg A firm used to give bonus on the basis of No. of months worked, now it has decided to give bonus on the basis of the targets achived
It is a case of change in accounting policy.

→ eg A firm was giving bonus to its employees on random basis., now it has decided to give bonus on the basis of No. of months worked
It is not a case of change in accounting policies.

→ When a new policy is applied to a new set of transactions, it should not be treated as a change in accounting policy & hence no retrospective application is needed.

→ eg If Reliance petro chemicals was following FIFO method for valuation of its inventories of petroliam products & for a new division Reliance Digital, the co. decides to follow WAM then it is not a case of change in accounting policy

AS 29 → Provisions, Contingent Liabilities & Contingent Assets

I Key terms

1) Liabilities → It represents the 'present obligation arising from past events, the sett. of which is expected to result in outflow of Economic Resources.
↳ eg Bank loan, cr, o/s exp.

(obligation / obligating event)

2) Contingent Liabilities → It represents the possible obligation that arises from the past events & outcome of which can be confirmed by future events which are beyond the control of entity
↳ eg ongoing case against the entity

3) Contingent Assets → It represents the possible resources that arises due to past events due to which future economic benefits may be received.
↳ Further the outcome here as well depends on future events which are beyond the control of the entity
↳ eg legal case filled by the entity, insurance claim lodged, etc

certain
documentary proof → 100% guarantee

4) Provisions → It represents a present obligation that probably requires an outflow of resources & a reliable estimate can be made of the amount of obligation.
(eg. Provision for warranty)

5) Obligation Events → This is an event that creates an obligation which results in an enterprise having no realistic alternative but to settle or pay
(eg. car purchase, loan taken, etc)

II. Contingencies

Contingent Liabilities (eg. ongoing legal case against co.)
(Prob of loosing)
- Probable (>50%) → Create Provision → Exp. A/c Dr. TO Provision A/c
- Uncertain (5% to ≤ 50%) → Disclosure in NOTES as Conti. liab.
- Remote (≤ 5%) → Ignore

Contingent Assets (eg. ongoing legal case by entity)
(Prob of winning)
- Probable (>50%) → Disclosure in Directors report
- Uncertain (≤ 50%) → Ignore
- Virtually certain (beyond doubt 100%) → Record Asset → Receivable A/c .. Dr. TO Gain A/c

→ Virtual Certainity
↳ it arises due to facts & it is not based on any opinion / estimation.
↳ Formal communication of the outcome is required for virtual certainity.

III. Reimbursements

1) Reimbursement Assets
↳ In case an expense has been agreed to be reimbursed then the entity will only record the net of reimbursement amount as exp.
↳ For the amt agreed to be reimbursed the entity will record the amt receivable as Reimbursement Asset.
↳ The reimbursement asset should be recognised only when it is virtualy certain that it will be received
↳ eg An audit firm has a contract with his client for reimbursement of travelling exp upto ₹20,000. Actual exp. incurred by audit firm are ₹25,000.

Travelling Exp. A/c (P&L) Dr	50000	—	
Reimbursement Asset A/c Dr	200000	—	(BIA → Short term loans & Adv.)
TO Bank A/c		250000	

↳ eg. Insurance contract to cover risks; idemnity clause in a contract; warranty provided by a supplier.

* ↳ When the enterprise is liable for the whole amt in question then a provision is recognised for the full amt of liability & a separate asset for the expected reimbursement is recognised.

↳ eg. For provision made by Chroma for warranty on LG televisions to be reimbursed by LG to Chroma. The entry will be

Reimbursement Asset A/C ..... Dr.
  To Provi. for warranty A/C

2) Reimbursement Assets & off settings

↳ As a gen. principle, Assets & liabilities needs to be separately recorded in the B/S i.e they can not be off settled unless the transaction is expected to be net settled.

↳ eg. In case of provision for tax & Adv. Tax, they can be off settled & the Net amt. is presented in the B/S as they can be Net settled.

∴ It means if the provi. for tax is ₹2,10,000 & the Adv. Tax paid is ₹2,00,000 then the entity needs to pay only ₹10,000 as Net self assesment Tax.

→ Mutual Debts, AS-22 - Deffer tax Asset / liab.

* Reimbursement asset & provi. for warranty are similar to Adv. tax & provi. for tax. If the terms of the contract allow for net settel, then they can be off settled in B/S

↳ eg. If an entity has taken Bank loan of ₹1 cr for the purchase of premises worth ₹1.5 cr then in the books of the entity, bank loan will appear under long term borrowing (B/S Liab.) & premises of ₹1.5 cr will appear under PPE Tangible Assets.

They can not be Net settled
∴ They can not be off settled

As per AS-4 Contingencies & Events occuring after B/S date, Material events occurring in post B/S period & which provides addⁿ info. of the condⁿ pertaining on the B/S date are called adjusting events. These events are adjusted in the accounts of reporting the period.

In this case the co is in the process of finalising its accounts for the year ended 31-03-17 (post B/S period) & it has entered into wage revision agreement in this period (May-17) for the wage increment from June-16 to Mar-17. This provides addⁿ info. of the condⁿ existing on B/S date i.e. wages for the services ~~entered~~ rendered in that period ∴ it should be adjusted in the accounts for the year ended 31-3-17.

Wage revision for the period 01-04-17 to 05-17 will be adj. in the accounting year 17-18.

IV Measurement of Provisions (to be recorded in the books) / Measurement of Contingencies (to be disclosed in notes)

1) Provision should be recorded by the entity on Best estimate basis.

Methods for Best est. of provi are

Expected Value Method

→ In case, there is a range of possi. outcomes, the entity should take the probability based weighted avg in order to measure the provison.

→ $E(x) = \sum P_i x_i$

Most likely Method

→ When there are only two possibilities, the entity uses this method in order to measure the provi.

→ The Most likely value can be directly used (without multiplying probabilities)

→ eg. 60% chance of losing, loss = ₹50,000
40% chance of losing, loss = ₹100000
∴ Provision = ₹50,0000

Bank A/c Dr 9000
TDS (Adv. tax) A/c Dr 1000 → B/S (Short term CA dr)
To Int A/c 10000 → P&L cr.
(Interest)

Bank A/c Dr 9000
To Int A/c 9000

2) Provision needs to be measured on Pre-tax basis (Gross value) & on undiscounted basis (without multiplying with discounting factor)
↳ only exception is Provision for Decommissioning & site restoration.

3) Provision should be reassessed on each B/s date & they should be remeasured in case circumstances indicate. (ref. As-10 → changes in. XV)

4) Provisions should be measured Based on entities own experience.
If that is not available then based on industry data
In extremly rare circumstances if amt. of provi. is not measurable at all, then disclosure should be given about the inability to measure it in the notes. (ref AS-4 Impract IV)
↳ eg provisions in case of entity in business of Hyper loope

5) In case of decommissioning & site restoration the obligating event is, the asset is ready to use hence provi. for decommissioning & site restoration should be done as soon as the asset is constructed & ready to use.

V. Restructuring

→ It refr. to sale or termination of a line of business or relocation of business activities from one country or region to another or changes in the management structure

→ Restructuring provisions should include only direct Exp. arising from restructuring.
↳ eg termination benefits to employees, legal fees, Consultation charges.

→ Restructuring provi. should not include exp. associated with the ongoing or future operations.
↳ eg retraining or relocating cost of continuing staff, Marketing of new venture, investments in new. systems & distri. networks.

rendering of servi.
utilization of resources

AS-9 → Revenue Recognition

Meaning

→ It is the gross inflow of cash or any other consideration in the ordinary course of business of an entity.
↳ it can be earned through sale of goods, rendering of services & utilization of resources.

→ Revenue can be recognized only if it is capable of the measured reliability & there is no uncertainty in the ability to collect consideration.

→ Uncertainty in ability to collect consideration

- Initial uncertainty
  - ↓
  - NO revenue recognised
    - ↓
    - Postponed revenue recognition till the time we get certainty in our ability to collect revenue
- Subsequently uncertainty
  - ↓
  - Revenue would have been initially recorded
    - ↓
    - Create provision for bad debts when uncertainty subsequently arises (Revenue already recognized not permited to be reversed)

II Revenue Recognition.

→ Rendering of services

↳ Proportionate Completion Method

↳ suitable for services which are not linked to a single crucial event

↳ Revenue to be recognized on proportionate/ time basis.

↳ Full Completion Method

↳ suitable for services which are linked to a particulars crucial event. eg Concerts; Brokerage

↳ Revenue would be recognized when the crucial event happens.

→ Utilization of Resources

↳ Interest → Time basis on the basis that is accrued

↳ Royalty → As per terms of contract

↳ Dividend → Right to receive dividend established (i.e. the date when shareholders approve the dividend)

→ Sale of Goods

↳ risk & reward incidental to ownership get transfered to buyer

III Special Cases

1) Consignment sales

↳ Revenue to be recognized when the consignment agent (consignee) sells goods to outsiders.

↳ NO rev. to be recog. when goods are delivered by the consignor (principal) to consignee

2) Sale subject to inspection

↳ Rev. to be recog when risk & reward of the goods are transf & inspection is completed.

3) Sales on approval basis (sale subject to return)

↳ rev. to be recog. when either:

→ Buyer communicated his approval; or

→ Buyer's doesn't act, implying he accepts the goods; or

→ Reasonable time period for rejection has elapsed

4) Revenue recognitions when delivery postponed at buyers request

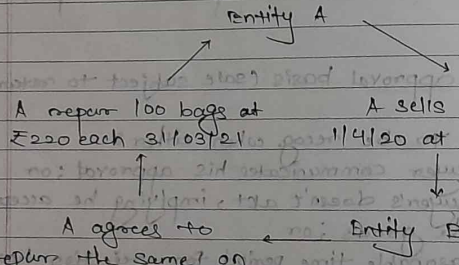
↳ Generaly when the buyers req. a postponement

of delivery because of his mobility to collect the goods, it is implied that the seller is holding the goods on behalf of buyer & hence the risk of goods is considered to have passed to buyer & hence rev. should be recog.

5) Insurance agent Commission

↳ to be recog from the effective date of policy

6) Sales & repurchase agreement



In such case record as loan insted of sale & a repayment of loan along with interest insted of repurr. The diff between the repurr price & sale price is treated as intrest which needs to be recorded on time basis

JE 1/4/20 Bank A/c Dr 20000 —
To loan A/c — 20000
(100 x 200)

2020-21 Int A/c Dr 2000 —
To loan A/c — 2000
(100 x 220 - 100 x 200)

31/3/21 loan A/c Dr 22000 —
To Bank A/c — 22000

7) Discount

Trade Discount (other than cash dis.) | Cash Discount (linked to early payment)

→ Reduce from selling price (record only net sales) | → shown separately as Exp.

→ Bank A/c Dr 90 — To sales A/c — 90

→ Bank A/c Dr 90 —
Dis. A/c Dr 90 —
To sales A/c 100

8) Price revision

→ In case the seller & buyer agrees to receive the price of sales which have already happed, then the rev. attributed to the price revision should be adj. / recorded in the year when the price revision is agreed / appl. & there is reasonable assurance that the price revision should be collected.
We should not adj the sale already recorded.

9) Property sales transactions

→ For a builder / real estate dev., sale of flat/ building is considered to be revenue. In case the legal regi. is pending the property does not get regi. in the name of buyer

→ But in substance, when the risk & reward is trans to buyer the seller should record

→ Hence the sale can be recorded when the following condin are met:
→ there is a written sale deed.
→ Consin is received or agreed to be received
→ The buyer takes possession of the property

→ In the such a case, rev. can be recorded irres. of the fact that the legal regis. has been comp. or not

AS-1 → Disclosure of Accounting Policies:

I Financial Statements
↳ BIS ↳ P&L ↳ cash flow ↳ changes in Eq ↳ Notes.

II Fundamental Accounting Assumption
→ Going concern
→ Accrual
→ consistency

If followed
↳ No disclosure needed

If not followed
↳ separate disclosure needs to be given in FS.

III Accounting Policies

→ Major consid^n. that Govern selection of a particular accounting policy are

↳ Prudence → Prudence ensures profits & assets are not over stated, losses & liabilities are not understated

↳ Substance Over Form → Transactions & events should be accounted & presented in the financial statements in accordance with their substance & financial reality & not merely by there legal form.

↳ Materiality → Financial statements should disclose all material items.

Material items is not always a matter of relative size

It is the information which might influence the decisions of the user of financial statement

In certain cases quantitative limits of materiality is specified like:

Entity should disclose in notes additional inform regarding any income or exp which exceeds 1% of rev. from operation.

Entity should dis. in notes share in co. held by shareholder holding more than 5% shares.

Imp.

IV In case of change in Alcing policy having,

Material effect in CP

Amt ascertained

Amt not ascertained.

Amt/impact due to new policy should be disclosed

the above fact that the entity is unable to ascertain the amt should be disclosed.

Material effect not in CP but ascertainable in later period

fact of such change in later period to be disclosed in CP.

Amt/impact determination not mandatory.

V Additional Points.

Exam note → All signi. Alcing policies adopted in preparation & presentation of F.S should be disclosed & should form a part of F.S & should be mandatorily dis. in one place in notes.

Incorrect pada to vapro → Mere dis. can not justify an incorrect accounting treatment

Eg LIFO for Valn of stock

AS 19 - Leases

I Lease

It is a contract where by the lessee gets the right to use the asset which are owned by lessor for a pe specified period of time (lease term), for a specific consideration.

It is classified as

Financial Lease (FL)	Operating Lease (OL)
→ In this case subsantially all the risk & reward incedintal to ownership are transfered to the lessee	→ In case lease is not a finance lease then it will be treated as operating lease

II If any one of the following condin are satisfied then the lease will be treated as Finance Lease

→ Ownership automatically gets transfered to the lessee at the end of lease term.
Eg Hire purchase

Or

→ Lessee has an option to buy the asset at the end of lease term at price which is substantialy lower than the Expected Fair Value

Or

→ Lease term covers a major part of the Economic life of Asset i.e lease term is ≥ 75% of the Economic life of Asset.

OR

→ Present Value of minimum lease payments (PV of MLP) substantialy covers Fair Value at the inception i.e PV of MLP is ≥ 90% of the Fair value of the asset at the start (Beginning of lease term)

OR

→ Asset is of Highly specialise Nature & can only be used by the lessee
↳ eg Rocket launcher specialy designed by HAL for ISRO

Key Terms

→ Lease term (Lockin period)
= Non cancellable period + Renewable period (only if sure at the inception that it will be renewed)

→ MLP for lessee
= Lease rent (fixed) + Guareented Resedual Value (GRV) by lessee + Purchase Price (if the option is at a substantialy lower price)

→ MLP for lessor
= Lease rent (fixed) + GRV by lessee / independent third party + Pur. price (if the op. to pur. is at a substantially lower price)

→ The following are not included in MLP
→ Contingent Rent (covid-19)
→ Refundable deposit
→ Expenses of lessee paid by lessor & subsequently reimbursed by the lessee & vise versa
→ Unguareented residual value (UGRV)
= Expected residual value − GRV.

→ GRV is the fair value of the asset agreed to be paid to the lessor at the end of lease term either by the lessee or by an independent party.

→ Initial Direct Cost (lease agree. ke binth ke time ka khareeda)
This refers to the directly attributable cost which are incurred at the time of acquiring the asset under lease eg → commission, legal fees etc

→ Interest rate implicit in the lease (Discounting factor)
Lease agreements usually do not include rate of int.

This interest rate would be inferred in the following order of preference
→ Lessor internal rate of return (IRR) i.e the actual rate earned by the lessor
→ If above is not possible take the lessee's incremental Borrowing rate. In case of lessee were to borrow., the bankers would charge a specific rate of interest for following

∴ It is assumed that in a finance lease, the lessor would be charging a similar rate

→ Inception of lease → lease shuru kabhi se hoga.
Earlier of
i) Date of lease agreement & ii) date of commitment by the parties to principal provi. of lease such actions which confirm to be upon agreed terms of lease are like.

→ Economic life (generating economic benefits) is always greater than the useful life of asset (depreciable life)
Period over which asset gen. eco benefits
useful life of leased asset → Period over which the lapsed asset is exp to be used by lessee

IV Specific Terms of Lessor

→ Gross Investment (GI) = Total MLP + UGRV of lessor

→ Net Investment (NI) = PV of Gross investment (Discounted Total MLP of lessor + Dis. UGRV)

→ Unearned finance lease income = GI − NI

V Depriciation of an Asset in case of finance lease

Finance Lease

Ownership transf at end of lease term (Circum.: 1 & 2)	Ownership NOT transf at the end of lease term (Circum.: 3, 4 & 5)
Part → II	Part → II
Depri. over useful life	Depri. over the lease term.

VI Lease Equalisation (Deferred rent) in case of an oper. lease

operating lease

→ A lease rental under OL should be recorded on straight line basis, unless any other systematic basis is clearly evident like inflation or increase in size of property

→ In on systematic basis & agreed lease rentals are

Yr	Rent
1	10
2	20
3	30
4	40
	100

→ Lease rent p.a = 100/4 = 25 p.a

Create lease equalization A/c

In the books of lessee

i) Rent A/c (P&L) Dr 25 —
To lease equalisation A/c — 15
To Bank A/c — 10

ii) Rent A/c (P&L) Dr 25 —
To lease equalisation A/c — 5
To Bank. — 20

iii) Rent A/c Dr 25 —
Lease equalisation A/c 5 —
To Bank A/c — 30

iv) Rent A/c Dr —
lease equalisation A/c —
To Bank A/c —

VII Accounting treatment (in the books of lessee)

	Finance lease (Borrowing & Buy)	Operating lease
a)	Initial recognition	Initial recognition
	Asset A/c Dr To loose liability A/c [PV of MLP : xx Fair value : xx whichever is lower]	No Entry

b) Annual Entries — Annual entries

i) Depriciation A/c Dr xx — Rent Exp. A/c Dr xx —
To Asset A/c — xx To. Bank A/c — xx
To lease Equalisation A/c — xx
(assuming rent is on systematic basis)

ii) Finance charges (Interest) Dr ① xx — P&L A/c Dr xx —
To Rent A/c — xx
Lease liabilities A/c Dr xx —
(Bal. fig) ③
To Bank ② — xx

VII Accounting treatment (in the books of lessor)

	Finance lease	Operating lease
a)	Initial recognition	Initial recognition
	Lease receivable A/c Dr xx — (Net inv.) To Asset A/c — xx (carring value) To Gain (P&L) — xx	No Entry

b) Annual Entries

Bank A/c Dr ① xx —
(P&L) To Finance income A/c — xx ②
To Lease receivable A/c — xx ③
(B/s. fig)

Annual Entries

i) Bank A/c Dr xx —
To Rent income (P&L) — xx
(assuming lease rental is on systematic basis)

ii) Depriciation (P&L) Dr xx —
To Asset A/c — xx

IX Sale & lease back

→ It results in Asset getting sold & same asset being taken back on lease

→ Intention
It is mainly a financial transaction.

Lease back is Finance Lease (FL)
↓
Deferred gain or loss on sale in ratio of Depri.
↓
Deferment in the ratio of lease rent

Lease back is operating Lease (OL)

SP > FV
Ab. Profit
SP − FV
(Unusual gain)
↓
Deferment in the ratio of lease rent

SP < FV
Normal Profit
FV − WDV (cost)
(Usual gain)
↓
Gain/loss immediately in P&L

Asset sale & lease back

Asset sale & lease back

a) Bank A/c Dr xx —
To Asset A/c — xx
(B/s) To Defe. Gain A/c — xx

a) Bank A/c Dr xx —
To Asset A/c — xx
To Defe. Gain A/c — xx
(Unusual gain)
To Gain on sale — xx
(P&L) (Usual gain)

Asset lease taking back

b) Asset A/c Dr xx —
To lease liab. A/c — xx

c) Depri. A/c Dr xx —
To Asset A/c — xx

d) Defer. Gain A/c Dr xx —
To Amortization — xx
of defer gain (P&L) A/c

X Applicability of As 19:

Applies to all assets other than:
→ Lease agreement for motion picture films, video recording, plays, manuscripting, patents & copyrights.
→ Lease agreement to use land → Ind AS-40
→ Lease agreement to explore for or use of natural resources (oil, gas, mineral rights)

XI For finding Implicit interest rate
PV of cash inflow = PV of cash outflow
PV of cash inflow → Annual lease rent, GRV & UGRV
PV of cash outflow → Fair value of assets & initial Direct cost

III 3 Parameters (suggestive in nature)

- Additional indicator for being classified as FL:

→ If lease can cancel the lease & lessor's losses on cancellation is born by lessee

→ lessee can continue the lease for a secondary period at a rent which is substantially lower than the market rent

→ Gains or loss from fluctuations in residual value accrue to lessee.

Lease liability of lessee = PV of MLP or fair value whichever is lower

PV of MLP = PV of lease rent + PV of GRV.

cal. of PV of MLP

Yr	Lease rent	Dis. factor @15%	PV of MLP
1	625000	0.8696	543600
2	625000	0.7561	₹472562.5
3	625000	0.6575	410937.5
4	750000	0.5718	428850
			1855850

∴ PV of MLP = ₹1855850

Fair value of asset = ₹2000000

∴ Lease liability of lessee = lower of ~~PV~~ ₹1855850 & ₹2000000

= ₹1855850

Extra

Lease receivable of lessor = PV of MLP + PV of UGRV

= 1855850 + (250000 × 0.5718)

= ₹1998800

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Cal. of P.V of MLP:

Yr	lease payment	Dis. fac @12%	PV of MLP
1	40000	0.89	35600
2	40000	0.79	31600
3	40000	0.7	28000
4	40000	0.622	24880
5	54000	0.552	29808
			149888

~~Cal.~~ of finance charges

Lease liab. = PV of MLP or fair value which ever is lower

= 149888 or 150000

= ₹149888

Cal. of finance charges p.a [op bal. - (lease pay - fin chr) → cl. Bal.

Yr	op. bal. of lease liab.	Finance ch @12.8%	lease payment	cl. Bal.
1	149888	18886	40000	128774
2	128774	16225	40000	104999
3	104999	13230	40000	78087
4	78230	9857	40000	30143
5	48087	5913	54000	—
		(8.8)		

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J.E in books of lessee

Y0 Asset A/c Dr 149888 —
To lease liab. A/c — 149888

Y1 Finance charges A/c Dr 18886 —
Lease liab. A/c Dr 21114 —
To Bank A/c — 40000

Y1 Depri A/c Dr 29978 —
To Asset A/c (149888/5) — 29978

Y2 Finance charges A/c Dr 16226 —
Lease liab. A/c Dr 23774 —
To Bank A/c — 40000

AS-16 → Borrowing Costs

I Terms

i) Qualifying Assets

↳ Necessarily takes substantial period of time to be ready for their intended use

↳ Nothing said then substantial period is 12m.

↳ The Manag decides the substantial period of time based on the industry it operates, the products produced.

↳ ∴ the substantial period can be longer / shorter than 12m.

↳ It includes Tangible / Intangible assets & also Inventories if it takes substantial period of time

↳ It does not include finacial assets like investment in share / Debentures / Bonds, etc as they are ready to use from the date of purchase.

↳ Always consider Normal Time to get the asset in ready to use condition & not Actual Time taken.

2) Borrowing costs

↳ It includes

- Interest
- Amortization of Premium / Discount on Borrowings. eg Premium on Redemp^n. of Debentures, zero coupon bonds
- Transaction cost. eg Processing fees
- Financial charges in case of Finance lease (AS-19)
- Foreign Exchange differences to the extent they are treated as adjustments to int. cost. (AS-11)

II Accounting for Borrowing Cost

Incurred for acquisition / construction of Qualifying Assets	Incurred for other than Qualifying Assets
Capitalize to Qualifying Assets	Expensed to P&L A/c
(Borrowing cost) Asset A/c Dr To Bank A/c.	(P&L A/c) Borrowing cost A/c Dr To Bank A/c

III Timing of Capitalisation

Commencement
↳ Start capi. of Borrowing cost.
↳ later of:
→ Date when the loan costs taken
or
→ Date when the Expenditure costs incurred
or
→ Date when the activities to get the asset ready have started

Suspension
↳ Stop capitalisa of Borrowing cost temporarily
↳ When active dev. is interrupted:
→ For an extended period of time
&
→ Due to abnormal factors which are beyond the entities control
→ eg. Covid-19
→ then capitali. is not allowed & the Borrowing cost is expensed to P&L A/c
→ eg in case of halt due to heavy rainfall for 2days then their will be no suspension of Capi. of Borrowing cost

Cessation
↳ Capitalisation of Borrowing cost is stoped Permanently
↳ When substantially all the activities to get the asset in ready to use condi^n are completed then capitalisation of Borrowing cost is stoped Permanently & it will be Expensed to P&L A/c.

IV Types of Borrowings

Specific	General
→ Borrowing taken specifically for acquisition/ construction of Qualifying asset	→ They are General purpose Borrowings & not specifically taken for Qualifying asset only
→ Net Borrowing cost to be capitalized = Actual Borrowing cost from commencement date − Income on temp. inv. of surplus funds	→ No defined purpose → eg General purpose Debentures. → If utilized for any qualifying asset then it will be charged to that asset using Weighted Avg Borrowing Rate (WABR) for the specific period → If not used for any Qualifying asset then it will Expensed to P&L A/c.

V Capitalisation of Borrowing Cost in case of Specific & General Borrowings

Step 1: Cal. Net Borrowing cost to be capitalized out of Specific Borrowings if any

Step 2: Cal. Weighted Avg Borrowing Rate (WABR) for General Borrowing

$$WABR = \frac{\text{Total Int. on Gen Borrowings}}{\text{Time weighted Gen. Borrowing}} \times 100$$

Step 3: Eligible General Borrowing cost
= Exp. incurred out of Gen. Borrowings × WABR × $\frac{\text{No of Months}}{12}$

Step 4: For General Borrowing to be capitalize, Compare Actual Int (Step 2 - Numerator) & Eligible Gen. Borrowing cost (Step 3), select whichever is lower

Step 5: Total Borrowing cost to be capitalised
= Net Borrowing cost on specific Borrowing (Step 1) + General Borrowing cost (Step 4)

Eg. 1-4-23 : Construction Started ₹100
loan taken for construction ₹80 @10% p.a

1-4-23 → 25
⋮ Expenses
⋮

Temperory income from the loan invested = ₹3 (80×10%)

Borrowing cost to be capitalised = ₹5 (8-3)

Eg. 1-4-23 : construction started = ₹100
: Specific loan taken for construction
= ₹30 @10% p.a

General Borrowings :
12% Bonds = ₹40 15% Deb = ₹200

1-4-23 25 → Sp. B

1-5-23 10 → 5 Sp. B, 5 Gn. B.

1-7-23 30 → Gen. B.

1-1-24 25 → Gen. B.

Find the Borrowing cost to be capitalised

31-3-24 10 → Gen. B
100

Temp. income from loan inv = ₹1

Sol.

Step 1 : Borrowing cost on special Borrowings = 30×10%
= ₹3

(-) Temporary income (₹1)
₹2

Step 2 : Weighted Avg. Borrowing rate

$= \frac{40 \times 12\% + 200 \times 15\%}{40 + 200} \times 100$

$= \frac{(4.8 + 30)}{240} \times 100$ (compare) (which ever is lower)

= 14.5 %

Step 3 : Borrowing cost on General Borrowings

1-4-23	25	= 0
1-5-23	(10-5) × 14.5% × 11/12	= 0.6645
1-7-23	30 × 14.5% × 9/12	= 3.2625
1-1-24	25 × 14.5% × 3/12	= 0.90625
31-3-24	10 × 14.5% × 0	= 0

Borrowing cost on Gen. Borrowing (4.83) (compare)
(+) Borrowing cost on Sp. Borrowing 2
Total Borrowing cost ₹6.83