

CA Revision Companion – Summarised AS & Chapters (Based on Aakash Kandoi Notes)



A Small Note from Me

Hi everyone,

I've created these notes by summarising Aakash Kandoi Sir's board notes — combining all the Accounting Standards and chapters into a more concise, organised, and exam-friendly format. The idea behind this was simple: to make revision easier and help fellow students like me who might find the original notes a bit lengthy during last-minute prep.

All credit for the original content goes to Aakash Kandoi Sir — these notes are just a simplified summary meant purely for easy revision and better understanding. I'd highly recommend using these notes along with Aakash Sir's revision lectures — that combo will really strengthen your understanding and save time during revision.

It took quite a lot of time and effort to compile everything carefully, but if it helps even a few of you study better or feel a little lighter in your preparation, I'll truly feel it was worth it. 🧡

Let's keep helping each other — because in this journey, when one CA student helps another, we all move one step closer to becoming CAs together. If these notes helped you, please share them with others, so more students can benefit and we can grow as a community that lifts each other up.

Wishing you all the best for your exams — stay consistent, stay kind, and never stop believing in yourself. We're all in this together. 🌸

– From one CA aspirant to another, **Paksh Mehta**

Applicability of Accounting Standards (AS)

Applicability of Accounting Standards (AS) - Companies vs. Other Entities

Category	Corporate Entity	Other than Company (Non-corporate Entity)
Type	Company	Non-corporate Company (e.g., Partnership firm, Limited Liability Partnership (LLP), Mutual Undivided Family (HUF), Co-operative Societies, Sole proprietorship, Trust etc.)

Applicability of AS to Corporate Entities

1. Non Small and Medium Sized Company (Non-SMC) (Big Company)

- **AS Applicability:** Apply All Accounting Standards (AS).
- **Specifics:** Indian Accounting Standards (Ind AS) (AS 1 to AS 29) are applicable.

2. Small and Medium Sized Company (SMC)

- **AS Applicability:** Apply All Accounting Standards (AS), but a few exemptions and relaxations are available.
- **Note:** AS 6 and AS 8 are deleted.
- **Exemption (Full AS Maaf):**
 - Full exemption from AS 17.
- **Relaxation (AS ke kuch parts / concepts se chutti):**
 - Relaxation available for AS 15, AS 19, AS 20, AS 28, and AS 29.
 - AS 25 applies only if the company elects to apply it (else it is exempt to SMC).

Definition of Small and Medium Sized Company (SMC)

A company is considered an SMC if it meets **All** of the following conditions:

1. It should **not** be listed, nor should it be in the process of listing, on any stock exchange.
 - (e.g., Non-Banking Financial Company (NBFC), Mutual Fund, Bank, Insurance Company, Financial Institution).
2. It should **not** be a Bank, Insurance Company, Financial Institution.
3. Turnover (excluding other income) does **not** exceed ₹250 crores in the Previous Financial Year.
4. Borrowings does **not** exceed ₹250 crores in the Previous Financial Year.
5. It should **not** be a holding or Subsidiary Company of a Non-SMC (Big Company).

Definition of Non-SMC

Companies **not** falling within the definition of SMC are considered to be Non-SMCs.

Important Note for Existing Companies: An existing Company which was previously a Non-SMC can become an SMC **only** if it meets the Definition of SMC for **2 Consecutive Years**.

Applicability of Accounting Standards (AS) to Other than Company (Non-corporate Entity)

Non-corporate entities are categorized into four levels (Level I, Level II, Level III, and Level IV) based on the following criteria:

Criteria for Classification of Non-corporate Entities

Particular	Level I	Level II	Level III	Level IV
① Turnover (Revenue) (excluding Other Income) in Previous Financial Year	Exceeds ₹50 crores	Exceeds ₹10 crores but upto ₹50 crores	Exceeds ₹1 crore but upto ₹10 crores	Upto ₹1 crore
② Borrowings in Previous Financial Year	Exceeds ₹50 crores	Exceeds ₹10 crores but upto ₹50 crores	Exceeds ₹2 crores but upto ₹10 crores	Upto ₹2 crores
③ Holding / Subsidiary Condition	If any entity is holding or subsidiary of Level I, then it also becomes a Level I entity.	If any entity is holding or subsidiary of Level II, then it also becomes a Level II entity.	Same	Same
④ Other conditions	Banking/Insurance, Financial Institution (e.g., Co-operative Banks), Listed/Listing process on any stock exchange.	-	-	-
AK's Note: Ideally this condition should not be there in non-corporate entity.				

Exemptions & Relaxations to Non-corporate Entities

Sr. No.	Particulars	Level I	Level II	Level III	Level IV
1	Full Exemption (i.e., Apply All AS)	None (i.e., Apply All AS)	AS 9, 17, 20, 21, 23, 25, 27	AS 3, 17, 18, 20, 21, 23, 24, 25, 27	AS 3, 14, 17, 18, 20, 21, 23, 24, 26, 27, 28
2	Relaxation (Partial Exemption) (i.e., Apply All AS)	None (i.e., Apply All AS)	AS 15, 19, 28, 29	AS 10, 11, 15, 19, 28, 29	AS 10, 11, 13, 15, 19, 22, 26, 29

Note on Charitable Organisations:

- If the organization is **100% charitable**, there is **no need to follow** Accounting Standards (AS).
- Even if **1% business activities** are commercial, the organization must **Follow AS on full organization**.

Extra Part - Indian Accounting Standards (Ind AS) Applicability

Indian Accounting Standards (Ind AS) Applicability to Normal Companies (Mandatory Basis)

	Phase I (01.04.16)	Phase II (01.04.17)
Applicability	All Listed/Unlisted Companies having a Net Worth of ₹500 crores or more.	1. All Listed Companies. 2. Unlisted Companies having Net Worth of ₹250 crores or more.
Net Worth:	Share Holders' Funds (Share Capital + Reserves)	

Note: If our Parent/Subsidiary Company follows Ind AS, then Ind AS is also applicable to us.

Indian Accounting Standards (Ind AS) Applicability to Non-Banking Financial Companies (NBFC's)

Note: For NBFC's, only Mandatory applicability is considered. Voluntary adoption is not allowed.

	Phase I (01.04.18)	Phase II (01.04.19)
Applicability	All Listed/Unlisted NBFC's having Net Worth of ₹500 crores or more.	1. All Listed NBFCs. 2. Unlisted NBFC'S having Net Worth of ₹250 crores or more.

Note: If our Parent/Subsidiary Company follows Ind AS, then Ind AS is also applicable to us.

Indian Accounting Standards (Ind AS) Applicability to Banking Companies and Insurance Companies

Note: Ind AS implementation is **deferred until further notice**.

General Notes on Ind AS

- Indian Accounting Standards (Ind AS) once applicable, are **always applicable**.
- If Ind AS is **not** applicable to any company, then it must **follow Accounting Standards (AS)**.

AS 1: Disclosure of Accounting Policies

1. Accounting Policy

- **Accounting Policy** refers to specific accounting principles and methods of applying those principles in the preparation and presentation of Financial Statements (Fin. Stat.).
- **Examples** (Note: This list is NOT exhaustive):
 - **Inventories:** FIFO or Weighted Average (Choosing between these two is a choice of Accounting Policy).
 - **Maintaining Books of A/cs:** Cash Basis or Accrual Basis.
 - **PPE (Subsequent Measurement):** Cost Model or Revaluation Model.
 - **Cash Flow Statement (AS 3):** Direct Method or Indirect Method.
- For every item of asset, liability, revenue, expenses, the company needs to evaluate a method to adopt these policies.
- This method of forming and applying accounting principles is known as accounting policies.
- **Note:** Selection of Depreciation method is not an accounting policy; it is an accounting estimate (as per AS 5).

2. Selection of Accounting Policy

@ Primary Consideration

- Financial Statements (FS) prepared should portray a **True & Fair view** of the performance and affairs of an enterprise.

Secondary/Major Consideration for Selection of Accounting Policy

I. Prudence	II. Substance Over Form	III. Materiality
Profits should be recognised when realised (relevant for those profits which are NOT anticipated to be realised).	Transactions should be accounted based on their substance and not merely by their legal form.	FS should disclose all material items , i.e., items whose knowledge might influence the decision of users.
But, Provision for all known liabilities & losses should be created even though the amount cannot be determined with certainty (i.e., in such cases, provision should be created with the best estimate).		Materiality of transaction can be judged by its size or its nature.
Also, create provision only when the probability of losing is more than 50%.		

- **Note:** All **Significant Policies** adopted should be disclosed in one place.
- It should also form part of the Financial Statements (Disclose in Notes to A/cs).

3. Disclosure of Changes in Accounting Policy

(When change can be made will be discussed in AS 5)

Change in Accounting Policy	Treatment and Disclosure
Material in Current Period	
Amount ascertained	Amount to be disclosed.

Change in Accounting Policy	Treatment and Disclosure
Amount NOT ascertained	Fact to be disclosed.
Not material in current period but impact is material in later years.	Fact of such change in later period should be disclosed in current period.

4. Fundamental Accounting Assumptions

I. Going Concern	II. Consistency	III. Accrual Basis
FS are normally prepared on the assumption that an enterprise will continue its operation in foreseeable future nor there is a need to shut down the business.	The enterprise should follow a practice of using the same accounting policy for similar transactions.	Transactions are recorded as soon as they occur or when income or expenses are accrued, whether or not payment is actually received or paid.
	An Accounting Policy can be changed if:	
	a) It is required by Law	
	b) It is required by AS	
	c) It results in better presentation of FS.	

Note

- **If Followed ↓ Fundamental Accounting Assumptions:** Not required to be disclosed.
- **If Not Followed ↓ :** Disclosures required in FS.
- ① **Disclosure** is NOT a remedy for wrong or inappropriate treatment in accounting.
- ② **Changing the calculation of provision for any expense/losses** (e.g., Debtors Prov 5% → 10%)
 - Calculation change ho raha hai → Change in Accounting Estimate (Acc. Est.).
- ③ **If Previously provision was calculated on accrual basis & now Company decided that no provision will be created instead expense/loss will be booked as & when incurred** (e.g., Warranty Prov 5% on Sales → Now stop creating Prov)
 - Change in Accounting Policy (Acc. Policy).

AS 2 - Inventories

1. Definition

Inventories Assets which are:

- Held for sale in the ordinary course of business (Finished Goods).
- Used in the process of production for such sale (Work in Progress).
- In the form of materials to be consumed in the production process (Raw Materials).

Note: If plan is ready, Finished Goods (covered under AS 2) must be business.

2. Scope

Following are excluded from the scope of AS 2:

i) Work in progress arising under construction contracts (covered under AS 7). ii) Shares, Debentures and other financial instruments held as stock-in-trade (covered under AS 13). iii) Producers of livestock, agricultural and forest products (Not under AS, mentioned as being under AS 41 in the margin). iv) Mineral oils, ore and gases (Not under AS).

3. Measurement

Lower of:

- COST
- Net Realisable Value (NRV)

4. Cost of Inventories

Trading Business

Cost of Purchase of Raw Materials/Finished Goods:

- Purchase Price (less Trade discounts).
- Duties and Non-Refundable Taxes (If taxes are refundable they will **not** form part of the cost of Inventory).
- All Directly Attributable Expenses (e.g.: Handling cost, Freight/Transport Expense, Insurance of Purchase, Brokerage/Commission paid to Buying Agent etc.).
- Basically all direct expenses which are necessary to bring inventory to its present location and condition.

Manufacturing Business

Cost = Cost of Purchase of Raw Materials/Finished Goods + Cost of Conversion + Other Expenses

Cost of Conversion:

- Direct Cost (Direct Material, Direct Labour, Direct Expenses).
- Variable Overheads (Based on Actual capacity).
- Fixed Overheads (Based on Normal capacity **or** Actual capacity whichever is higher).
 - This is to calculate Fixed cost per unit.

Fixed Overheads Allocation:

- Fixed cost per unit is calculated based on Normal capacity.

- If Actual capacity is less than Normal capacity: The unabsorbed cost (Fixed Cost Incurred minus Allocated Cost of Inventory) is transferred to the Profit/Loss Account (as an Expense).
- If Actual capacity is equal to Normal capacity: The balancing figure is NIL.
- If Actual capacity is higher than Normal capacity: The balancing figure is NIL (Allocation is based on fixed cost per unit using Normal capacity, which limits the cost included in inventory to the total fixed costs incurred).

Exclusions from cost of Inventories

i) **Abnormal wastage** (Abnormal loss is transferred to the Profit/Loss Account). ii) **Storage cost** (But if storage is a part of production, then storage cost is considered in the cost of Inventories e.g.: Wines, pickles). * **Note:** This refers to cost incurred after inventory is made. iii) **Administrative Overheads** (e.g. Salary to employees who are not involved in manufacturing). iv) **Selling and Distribution Overheads** (e.g. Advertisement to market). v) **Interest charges** (Interest is transferred to the Profit/Loss Account. Do Not add to cost of Inventory).

Abnormal Wastage Calculation

- Total loss is divided into Normal loss and Abnormal loss.
- Normal loss is considered in computing the revised per unit cost of goods.
- Abnormal loss is transferred to the Profit/Loss Account.
- Revised cost per unit = Total cost divided by (Total units minus Normal loss units)
- Abnormal loss amount transferred to Profit and Loss Account = Abnormal units × Revised cost per unit
 - If there is no abnormal loss, then no need to do the above calculation, the full amount paid will be allocated to the cost of Inventory.
 - Fixed Overhead allocation and Abnormal loss calculation are two different concepts.

5. Costs Formula

Formula	Used when	Details
FIFO (First in first out)		
WAM (Weighted Average Method)		Average Cost per unit = Total Cost / Total units
Specific Identification Method	Used when inventory are not interchangeable (e.g.: Jewellery).	Here, which item is sold can be clearly identified along with cost.
Standard Cost Method	Used when actual cost incurred cannot be identified easily.	It takes into account normal levels of materials, labours and capacity utilization.
Retail Method	This method is often used when items are rapidly changing and have a similar gross margin.	Cost of Inventory = Sell Price of Inventory less: Gross Margin

- **Cost of Goods Sold (COGS):** The cost of inventory sold.
- **Closing Stock (Clg Stk):** The cost of inventory on hand.
- **Note:** LIFO is prohibited under AS 2.

6. NRV (Net Realisable Value)

Finished Goods (FG) - NRV

Estimated Selling Price (-) Estimated cost to make the sale (e.g. Commission, Brokerage, Packaging, Delivery cost) = **NRV of Finished Goods**

Work in Progress (WIP) - NRV

NRV of Finished Goods (-) Estimated cost of completion (-) Estimated cost to make the sale (e.g. selling etc.) = **NRV of WIP**

Raw Material (RM) - NRV

Valuation of Raw Material is Dependent on Finished Goods (purchased Raw material to consume in Finished Goods, i.e. not for Sale).

If Finished Goods (FG) is sold at cost or above cost	If Finished Goods (FG) is sold Below Cost
Measure Raw Material at Cost	Measure Raw Material at Replacement cost

- **Replacement cost** is the amount that an entity would have to pay to replace the asset at the present time according to its current worth.

7. Allocation of cost of Joint Products and By products

i) In case of Joint Products

- When the cost of conversion of each main product cannot be identified separately, they need to be allocated in the Sales ratio = Total units × Selling price per unit
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ii) In case of Byproduct

- Most Byproducts are immaterial, therefore they are measured at NRV.
- NRV of Byproduct will be deducted from the total cost of conversion, and after deducting, the Net cost of conversion will be allocated to the main products.
- In questions, sometimes profit from Byproduct/scrap will also be given, but remember that, we do not need Profit, we need NRV. (Ignore Profit).

Valuation of Closing Stock

- According to AS-2 (Inventories), inventory shall be valued at **cost or NRV whichever is lower**.

Valuation Principles (Summary)

- **Finished Goods:** Will be valued at cost or NRV whichever is lower.
- **Work in Progress (WIP):** Will be valued at cost or NRV whichever is lower. To find NRV of WIP we take: Selling Price of Finished Goods (-) Cost of completion (-) Cost of sale.
- **Raw Materials (RM):**
 - Will be valued at cost if Finished Goods is sold above or at cost.
 - Will be valued at replacement cost if Finished Goods is sold below cost.

Note on Raw Material Cost: Cost Price includes all directly attributable costs like Freight, Unloading, and is computed after deducting refundable taxes like GST (Input Tax Credit).

Cash Flow Statement (Accounting Standard 3)

1. Elements of Cash and Cash Equivalents

Cash and Cash Equivalents (CCE) includes:

1. Cash in Hand.
2. Demand Deposits with Bank (Savings Account, Current Account).
3. Deposits (Fixed Deposits) with short maturity of three months or less (three months or less).
4. Short term, highly liquid investments which are subject to an insignificant risk of changes in value (meaning their value does not fluctuate significantly easily).

Note: Equity shares are never Cash and Cash Equivalents if they have a significant risk of changes in value.

2. Classification of Cash Flow Activities

Cash flows are classified into three activities:

1. Operating Activities
2. Investing Activities
3. Financing Activities

A. Operating Activities

These are the principal revenue generating activities of the enterprise.

Examples:

- Cash receipts from the sale of goods and services.
- Cash receipts from royalties, fees, commission and other revenue.
- Cash payments to suppliers for goods and services.
- Cash payments to employees.
- Cash payments or refunds of income taxes relating to operating activities etc.

General Examples:

- Inflows: Fees, Book Sale Revenue.
- Outflows: Employee Salary, Printing cost, Administration Overheads.

B. Investing Activities

Cash flows from the acquisition and disposal of long term assets and other investments not included in cash equivalents.

Examples:

1. Cash payments to acquire Property, Plant and Equipment (PPE), Intangibles, Investment Property etc.
2. Cash receipts from Sale of Property, Plant and Equipment (PPE), Intangibles, Investment Property etc.
3. Cash payment to acquire investments in shares, investment in debentures, investment in preference shares or any other investment.
4. Cash receipts from Sale of investments in shares, investment in debentures, investment in preference shares or any other investment.
5. Cash advances and loans given.
6. Cash receipts from repayment of loans given.
7. Any income generated from Investment Activity, for example, interest income, dividend income, rent income on investment property, interest income on loans and advances given etc., will also be treated as cash flow from investing activity.

C. Financing Activities

These are activities that result in changes in the owner's Capital and borrowings of the enterprise.

Examples:

1. Cash proceeds from issuing shares, or any other equity instruments.
2. Cash payments on buy back of shares.
3. Cash proceeds from issuing debentures, issuing preference shares, issuing bonds etc.
4. Cash repayment on redemption of debentures, redemption of preference shares, redemption of bonds.
5. Cash proceeds from loan or borrowings taken.
6. Cash repayment on such loan and borrowings taken.
7. Any dividend paid/interest paid on raising of funds is also a financing activity.

3. Other Important Points

A. Loans Advances given and Interest earned

The classification depends on the nature of the institution:

Institution Type	Loans given and Interest earned	Classification
Non Financial Institution	Loans given and Interest earned	Investing Activity
Financial Institution (e.g. Banks)	Loans given and Interest earned	Operating Activity

Note: Loans given to employees or suppliers, and the interest earned on them (for both Non-financial and Financial institutions) → will be treated as Operating Cash Flow.

B. Investments made and Dividend earned

Institution Type	Activity	Classification
Non Financial Institution	Investment made and Dividend earned	Investing Activity
Financial Institution	Investment made and Dividend earned	Operating Activity

C. Loans Advances taken and Interest paid

Institution Type	Activity	Classification
Non Financial Institution	Loans taken and Interest paid	Financing Activity
Financial Institution	Loans taken and Interest paid	Operating Activity

Note: Loans taken from customers or suppliers, and the interest paid on them (for both non-financial and financial institutions) will be treated as operating cash flow.

D. Issue of shares and Dividend paid

Institution Type	Activity	Classification
Non Financial Institution	Issue of shares	Financing Activity
Financial Institution	Issue of shares	Operating Financing Activity
Institution Type	Activity	Classification
Non Financial Institution	Dividend paid	Financing Activity

Institution Type	Activity	Classification
Financial Institution	Dividend paid	Operating cash flow

Note: Share issue can never be your business; it is Financing for all.

E. Summary of Classification based on Institution

Non Financial Institution	Financial Institution (e.g. Banks)
Loan given to 3rd party → Investing	Loan given and Interest earned → Operating
Interest earned → Investing	Loan taken and Interest paid → Operating
Investment purchased → Investing	Investment purchased → Operating
Returns on Investment → Investing	Issue of shares and Dividend paid → Operating/Financing Activity* (See note on share issue)
Loan taken from 3rd party → Financing	
Interest paid on loan → Financing	
Issue of shares → Financing	
Dividend paid → Financing	
Loan given to employees/suppliers → Operating	Loan given to employees/suppliers → Operating
Interest earned from employees/suppliers → Operating	Interest earned from employees/suppliers → Operating
Loan taken from customers/suppliers → Operating	Loan taken from customers/suppliers → Operating
Interest expense to customers/suppliers → Operating	Interest expense to customers/suppliers → Operating

F. Income Taxes

Tax paid on Operating Income	Tax paid on Investing Income/TDS deducted	Taxes paid on Financing Cash flows
Income Tax will also be Operating cash flow	Such Tax will also be Investing cash flow	Tax will also appear as Financial cash flow

Note: If nothing is mentioned about income tax in the question, then consider it as Operating cash flow.

G. Insurance Claims Received

1. Insurance claim received against loss of stock/Inventory → Operating cash flow (along with AS 5).
2. Insurance claim received against loss of fixed Assets → Investing cash flow.

Note: As per AS 3, Insurance claim received is an extraordinary cash flow. Separate disclosure will be required of the same in the statement of Cash flow.

H. Non-Cash Transactions

Transactions that do not require the use of cash or cash equivalents should be excluded from the cash flow statement. *Examples:* Issue of Bonus Shares, Property, Plant and Equipment acquired in exchange of shares, etc.

I. Reporting of Cash Flow on Net Basis

AS 3 prohibits netting of receipts and payments of cash flows, i.e., they should be shown on a gross basis. *Example:* Acquisition of Machine for ₹ 50,000/- and Sale of furniture for ₹ 10,000/-. They should be shown separately.

J. Purchasing Shares of Subsidiaries (Investment in Subsidiaries)

- Investment in Subsidiary Shares/Debentures etc., and Interest/Dividend received from Subsidiaries → Investing activity (for non-financial as well as financial institutions).
- Investment in shares can be business: Operating. But investment in shares of subsidiary can never be business: Always Investing.

4. Format for Cash Flow Statement

Cash flow statement can be prepared using either the Direct Method or the Indirect Method. The answer under both the methods will be the Same.

Direct Method Format (for Operating Activities)

Cash Flow Statement of [Company Name] for the year ended [Date]

Activity	Details	Amount
A) Cash flow from Operating Activities		
(+) Cash received from sale of goods (Cash Sales) / Cash received from Trade receivables		XX
(+) Cash received from sale of services		XX
(-) Cash purchases / Payment to Trade payables		(XX)
(-) Payment for operating Expenses (e.g. wages, salaries, rent, electricity, overheads, other Business related expense)		(XX)
(-) Payment of income tax		(XX)
Cash flow from operating activities Before Extraordinary items		XXX
(+/-) Adjustment for extraordinary items		XX
Net Cash flows from operating Activities	A	XX

Investing Activities Format

Activity	Details	Amount
B) Cash Flow From Investing Activities		
Purchase of Property, Plant and Equipment		(XX)
Sale of Property, Plant and Equipment		XX
Purchase of Investment		(XX)
Sale of Investment		XX
Interest received		XX
Dividend received		XX
Rent income on investment property etc.		XX

Activity	Details	Amount
Cash flow from investing activities Before extraordinary items		XX
(+/-) Adjustment for extraordinary items		XX
Net cash flows from investing activities	B	XX

Financing Activities Format

Activity	Details	Amount
C) Cash flow from Financing Activities		
Issue of shares		XX
Buy Back of shares		(XX)
Issue of Preference Shares		XX
Redemption of Preference Shares		(XX)
Issue of Debentures		XX
Redemption of Debentures		(XX)
Loan taken		XX
Loan repaid		(XX)
Interest paid		(XX)
Dividend paid etc.		(XX)
Cash flow from financing Activities	C	XX

Final Reconciliation

Item	Amount
Net cash flows during the year (A+B+C)	XX
Opening Cash and Cash Equivalent	XX
Closing Cash and Cash Equivalent	XX

5. Cash Flow Statement (Indirect Method)

A. Cash flow from operating Activities

Calculation of Profit Before Tax and Extraordinary Items (If not available directly):

Item	Amount
Closing Balance of Profit/Loss (as per Balance Sheet)	XX
Less: Opening Balance of Profit/Loss	(XX)
Add: Transfer to Reserves (e.g. Closing Balance of General Reserve less: Opening Balance of General Reserve)	XX
Add: Appropriation of Profits (e.g. Dividends)	XX
Add: Current year Income Tax Accrued in Profit/Loss	XX

Item	Amount
Add/Less: Extraordinary effects (if any) (to get before extraordinary items)	XX/(XX)
Profit Before Tax and Extraordinary items	XX

Adjustment for Non-Cash and Non-Operating Items:

Adjustment	Amount
(+) Reversal of Non Cash Expense	XX
(-) Reversal of Non Cash Income	(XX)
(+) Reversal of Non-Operating Expense	XX
(-) Reversal of Non-Operating Income	(XX)

Adjustment for Changes in Working Capital:

Working capital includes Inventories, Debtors (Trade Receivables), Creditors (Trade Payables), Outstanding expenses, Prepaid expenses.

Change	Adjustment to Cash Flow	Relation to Cash	Hint
Increase in Current Asset (Inventories, Trade Receivables, Prepaid expenses)	Deducted in cash flow	Inverse relation: ↑ in Asset is deducted	
(+) Decrease in Current Asset	Added in cash flow		
(+) Increase in Current liability (Trade Payables, Outstanding expenses)	Added in cash flow	Direct relation: ↑ in liability is added	
(-) Decrease in Current liability	Deducted in cash flow		

Item	Amount
Cash flows from operating activities Before Income Tax	XXX
(-) Payment of Income Tax	(XX)
Cash flows from operating activities Before extraordinary items	XXX
(+/-) Adjustment for extraordinary items	XX
Net cash flows from operating activities	A

The remaining format (Investing and Financing Activities, and Final Reconciliation) is the same as the Direct Method.

Additional Notes on Indirect Method

- Whenever in such an account the amount credited to Profit/Loss is different from the amount actually paid, then the amount credited to Profit/Loss (if non-operating) will be reversed in Operating Activities Cash Flow and the amount actually paid will be adjusted in Investing/Financing Activity cash flow (e.g., Interest expense and Capital Grant).
- If Profit Before Tax (PBT) is not available, start with the closing balance of Profit/Loss and adjust for appropriations (like dividends) and current year's tax provision to calculate PBT.
- If Income Tax provision is given, and nothing is mentioned, the assumption is that the Previous Year's Provision for tax is paid in the Current Year. The Current Year's Provision is booked to Profit/Loss.
- In the context of a Sole Proprietor:
 - Profits are transferred to Capital Account.

- Drawings are treated like Dividend paid → Financing Activity.
- Hidden Adjustments (e.g., Interest on Debentures/Loans and Interest Income on Investments): If the rate is given and the interest expense/income is missing in the question, calculate the interest as a hidden adjustment. The calculated Interest Expense is reversed from Profit Before Tax (since it's a non-operating expense) and the actual amount paid is a Financing cash outflow. The calculated Interest Income is reversed from Profit Before Tax (since it's a non-operating income) and the actual amount received is an Investing cash inflow.
- Undervalued Inventory: If opening inventory is undervalued, the difference must be added back to the Profit/Loss Reserve to correctly calculate PBT for the purpose of cash flow. The total current asset value must also be adjusted for working capital changes.

AS 4 - Contingencies and Events Occurring after the Balance Sheet date

Introduction

- The entire discussion in this standard is whether the events occurring after the Balance Sheet (BLS) date (i.e., date of approval by Board of Directors (BOD)) should be recorded in the Previous Financial Year (FY) or in the next Financial Year.

Contingency

- **Definition of Contingency:** It is a condition or situation, the ultimate outcome of which will be determined by the occurrence of one or more uncertain future events.
- **Treatment under AS 4:** All contingencies have been withdrawn from this Accounting Standard as they will be discussed in AS 29. Only contingencies related to Trade Receivables, i.e., Provision for Bad and Doubtful Debts, will continue to be covered under AS 4.

Events Occurring After the Balance Sheet Date

i) Definition

- These are significant events, both favourable and unfavourable, that occur between:
 - The Balance Sheet Date
 - And the Date on which the Financial Statements are approved by the Board of Directors (BOD).
 - *Note:* The BOD is the approving authority. Shareholder approval is a later event and not the cutoff date for AS 4.

Types of Events

The events occurring after the Balance Sheet date are classified into:

1. Adjusting Event
2. Non-Adjusting Event

Adjusting Events

- **Definition:** These are events that provide further evidence of conditions that existed on the Balance Sheet date.
- **Treatment:** Such an event will be adjusted in the Financial Statements of the Previous Year.
- **Examples of Adjusting Events:**
 - Theft / fraud which happened in the Previous Year, but detected in the Next Year.
 - Debtors on whom a case was done before year end, are declared insolvent after year end.
 - *Condition:* An indication of the debtor becoming insolvent must have existed before the year end.
 - Sale / Purchase of Property, Plant, and Equipment (PPE) done before year end, but documentation done after Year end.
 - Value of Inventory gone down after year end, for which conditions existed Before Year end.
 - Favourable events (e.g., Debtor Shivam won the case where Provision for Bad Debts was already made) are also considered. If a condition (like Provision for Bad Debts) existed before the year end, a favourable outcome after the year end (like winning the case) is an Adjusting Event.
 - If the terms and conditions of a transaction were finalised before the Balance Sheet date, and the transaction is done after the Balance Sheet date, it is an Adjusting Event.

Non-Adjusting Events

- **Definition:** No evidence of such events existed on the Balance Sheet date.
- **Treatment:**
 - Such events will **not** be adjusted in the Previous Year.
 - But can be disclosed in the report of the Approving Authority (BOD) if the event is material/significant.
- **Examples of Non-Adjusting Events:**
 - Fire / Earthquake / Tsunami that occurred after year end.
 - Market value of Investment / Inventory gone down after year end, for which no condition existed on Balance Sheet date.
 - Cheques received from customer after year end.
 - Dividend declared after Balance Sheet date. (No condition/liability to declare the dividend existed on Balance Sheet date).
 - **Specific Disclosure Note:** All Significant Non-Adjusting Events are disclosed in the report of the Approving Authority, but Dividend declared after year end is disclosed in the Notes to Accounts of the Financial Year 2024-25.
 - If only negotiations for a transaction occurred before the Balance Sheet date, it is not treated as a condition existing, and the transaction done afterwards is a Non-Adjusting Event.

Special Cases

Going Concern Assumption

- Non-Adjusting Events that affect the going concern assumption are to be treated as **Adjusting Events**.
- The Financial Statements of the previous year will be prepared on **Liquidation/Realisation Basis** instead of Accrual Basis (Going Concern Basis).
- If the going concern is not valid (e.g., due to major destruction from an earthquake), the Financial Statements of the previous year need to be adjusted and prepared on a liquidation/realisation basis.
- If going concern is valid, then no need to adjust the financials, but the material event can be disclosed in the report of the approving authority.

Events Occurring After Approval by BOD

- If an event occurs after the Financial Statements are approved by the Board of Directors, it is out of the scope of AS 4.

Summary of Answer Presentation (for questions based on AS 4)

1. **Name of Standard:** State "AS 4 Contingencies and Events Occurring after the Balance Sheet date".
2. **Define Events after the Balance Sheet date:** Give the definition which is relevant for that question.
3. **Define Adjusting Event** and/or **Non-Adjusting Event** as relevant to the situation.
4. **Conclusion:** In 2-3 lines, state the conclusion as per AS 4.

A. Net Profit or Loss for the Period

The net profit or loss for the period consists of:

- i) Ordinary Activities
- ii) Ordinary But Exceptional items
- iii) Extraordinary items

1. Net Profit or Loss for the Period

- All items of incomes and expenses should be part of the P/L A/c.
- **Exception:** If any AS suggests a different treatment of expense/income, then follow that AS.
 - (e.g: Interest Exp. on Machine → Capitalised as per AS 10, Interest Exp. on Qualifying Asset → Capitalised as per AS 16 etc.)
- The following components discussed below should be **disclosed on the face of P/L A/c**:
 - **i) Profit or loss from (Ordinary) Activities:** Any activity which is undertaken as a part of business and related activities which are incidental or arising from main activities.
 - (e.g: Sale of goods, revenue from providing services, Int. Inc/Exp, Salaries, etc.)

2. Ordinary But Exceptional items

- The following items are **ordinary activities**, but their **size or nature** is such that they require **separate disclosure**.
- Such items are known as "**Exceptional items**".
 - (Examples were excluded)

3. Extraordinary items

- These are incomes or expenses that arise from events or transactions that are **clearly distinct from ordinary activities AND** therefore are **NOT expected to occur frequently or regularly**.
- The **nature & amount** of each extra-ordinary item should be **separately disclosed** in P/L A/c such that its impact on current P/L can be perceived.
 - (Examples were excluded)

B. Prior Period Item (PPI)

- **PPI** are income or expense which arise in current period as a result of **Errors** or **Omissions** in FS of one or more prior period.
- **Errors** may occur as a result of:
 - Mathematic mistake
 - Mistake in applying accounting policy.
 - Misinterpretation of facts **OR**
 - Oversight (failure to Notice)
- **Omission** means reliable information was available at the time of prep of FS but the info was **NOT considered**.
- The **nature & amount** of PPI items should be **disclosed separately** in P/L such that its impact on current period can be perceived.
- PPI ka separate head P/L mein nahi hai. If there is PPI item in C.Y., we will have to create a **separate head**.
- P&L EXTRACT
- Incomes

– Expenses

= Profit Before PPI

– PPI

= Profit After PPI

C. Changes in Accounting Estimates

- **Accounting Est** is an **approximation** where proper measurement cannot be made.
 - *(Examples were excluded)*
 - An **Acc. Est may change** when:
 - **i) New Infon is available**
 - **ii) Experience gained.**
 - **iii) Subsequent developments.**
 - **Change in Acc. Est** should be accounted **PROSPECTIVELY**.
 - Change in Acc. Est:
 - is **NOT** a **PPI**
 - is **NOT** an **Extraordinary Item**
 - The **nature & amount** of change in **Acc. Est** which has a **material effect** in the current period or later periods should be **disclosed**.
 - If it is not possible to **quantify the amount**, this **fact** should be disclosed.
-

D. Changes in Acc. Policy (Refer AS 1)

- **Acc. Policy** refers to specific accounting principles & methods of applying those principles in prep & presentation of Fin. Stat.
 - *(Examples were excluded)*
- **Acc. Policy can be changed only when:**
 - **i) Required by law**
 - **ii) AS**
 - **iii) If it results in Better Presentation of FS**

Disclosure of changes in Acc. Policy

	Material in current period	Not material in current period but impact is material in later years
Amount ascertained	Amount to be disclosed	Fact of such change in later period should be disclose in current period.
Amount NOT ascertained	Fact to be disclosed	Fact of such change in later period should be disclose in current period.

- **Change in Acc. Policy** is accounted **Retrospectively**.
- **Iska matlab** in FS of Curr. Year we will change the comparative figure of Prev Year. as per new Acc. Policy.

What are NOT changes in Acc. Policy

1. The adoption of a new policy for events or transactions that **differ in substance** from previously occurring events or transactions.
 - *(Example was excluded)*
 2. The adoption of a new policy for events or transaction which **did NOT occur previously** or were **immaterial**.
 - **(First time adoption of Policy)**
 - *(Example was excluded)*
-

Conclusion

- As per AS [5] Define / Explain - **PPI / Acc Est / Acc Policy / Exceptional / Extraordinary**.
-

AS 7 - Construction Contracts

1. Introduction

- AS 7 prescribes accounting for construction contracts in the Financial Statements of the contractor.
- The main objective of this AS is to determine when the contractor should recognise contract Revenue & Contract Cost in the Statement of P&L.
- **Contractor:** Performs construction.
- **Contractee / Customer:** Hires for construction.
- **Construction:** Of buildings, roads, highways, bridges, towers, etc.
- AS 7 is applicable to contractors (e.g., Kandoila or Builders).

2. Combining & Segmenting (Separating) Construction Contracts

Separate Contracts (Segmenting)

A contract covers a number of assets. The construction of each asset should be treated as a separate contract if:

a) Separate proposals have been submitted for each asset. b) Each asset is subject to separate negotiation & the Contractor or Customer can accept or reject any part. c) Cost & Revenue of each asset can be identified separately.

Combined Contracts

A group of contracts should be treated as a single contract when:

a) The group of contracts is negotiated as a single package. b) The contracts are closely interrelated. c) The contracts are performed concurrently or in a continuous sequence.

3. Contract Revenue & Contract Cost

Contract Revenue

Contract Revenue comprises:

- Agreed contract price (XX)
- (+) Agreed cost escalation (xx)
- (+) Claims (only those which customer will accept & can be measured reliably)
- (+) Incentive Payments (usually received for early completion & will be included only when it is probable that the specified target will be met & can be measured reliably)
- (+) Any other payment due to variations in the contract
- (-) Penalties (usually for late completion) deduct from revenue only when it is probable that penalty will have to be paid.

Contract Costs

Contract Costs comprise of:

1. Costs that relate directly to the specific contract
 - Eg: Site labour costs, site supervision cost, cost of materials used in construction, Depreciation of plant & equipment used on the contract, cost of transportation of PPE from & to the contract site, cost of design & technical assistance that is directly related to the contract, etc.
2. Cost that are attributable to the contract activity in general & can be allocated to the contract.
3. Other costs as are specifically chargeable to the customer.

Costs that are excluded from cost of construction (cannot be attributed to contract activity or cannot be allocated to a contract):

- General/Admin Overheads for which reimbursement is not specified in the contract.
- Selling costs.
- Depreciation of plant which was idle & not used in construction.

4. Types of Construction Contracts

Fixed Price Contract

- Contractor agrees to a fixed contract price.
- A fixed price contract might also be subjective to incentives, escalations & claims.

Cost Plus Contract

- Contractor is reimbursed for allowable or otherwise defined costs plus a percentage of these costs.

5. Percentage Completion Method (PCM)

- Also known as Stage of Completion Method.
- Revenue in case of construction contracts is to be recognised annually in proportion of work completed every year.

Determination of Percentage of Work Completed (Stage of Completion)

Percentage of work completed may be determined by following methods:

a) Surveys of work performed (e.g., Surveyor is appointed, he checks & gives certificate of % of work completed). b) Completion of physical proportion of contract work. c) Actual costs incurred till date / Total Estimated cost $\times 100$. (also known as Contract WIP (Work in Progress)).

Formulas for Percentage of Completion:

Percentage of completion can be calculated in 2 ways:

Method 1:

Percentage of completion = Actual cost incurred till date divided by Total estimated cost $\times 100$

Method 2:

Percentage of completion = Actual cost incurred till date divided by (Actual cost incurred till date + Future estimated cost) $\times 100$

Recognition of Revenue:

Revenue to be booked = Total contract revenue $\times$ Percentage of completion

6. Loss Making Contract

- As per AS 7, whenever total contract cost is expected to exceed the contract Revenue, the full loss should be recognised as an expense immediately.

7. If Final Outcome of the Contract Cannot be Measured Reliably

- Revenue should be recognised only to the extent of Contract cost incurred.
 - (Relevant when % completed is not sure if contract can be fulfilled or not).

8. Changes in Estimates

- % of completion is applied on a cumulative basis in each year to the current estimates of revenue & contract cost.
- Any change in estimate of contract revenue & contract cost is to be treated as change in accounting estimate, i.e., do prospective accounting.

9. Calculation of Amount Due from Customer / Amount Due to Customer

Status Determination (Conceptual)

Status of Payment vs. Revenue	Resulting Balance	Classification
Contract Revenue Accrued > Customer paid	Receivable from customer	Asset (Amt due from customer)
Contract Revenue Accrued < Customer paid	Advance from customer	Liability (Amt due to customer)

Format for Calculation (Gross Amount Due from/to Customer)

Metric	Amount
Costs incurred till date	XXX
(+) Recognised Profit	XXX
(-) Recognised losses	(XXX)
(-) Progress Billings (Progress Payments received + Amount billed by Contractor but not yet paid by customer)	(XXX)
Result	XXX

- If the result amount is positive (Asset) → Gross Amount due from customer.
- If the result amount is negative (Liability) → Gross Amount due to customer.

Note on Progress Billings in calculation:

- Progress Billings include: Payments received (Amt paid by customer) and Amount Billed by Contractor but not yet paid by customer. (This is included in the Progress Billings line item).

1. Scope

AS 9 does not deal with the following aspects of Revenue Recognition:

- i) Revenue from construction contracts (AS 7) ii) Revenue from lease agreements iii) Revenue from government grants iv) Realised/unrealised gain from sale of Non-current assets (e.g., PPE, Intangible). - **Note:** If Fixed Asset sale is the business (i.e., it is inventory), such sale in the ordinary course of business is covered in AS 9. v) Realised/unrealised gain resulting from changes in foreign exchange rates (AS-11).

2. Definition of Revenue

Revenue is the gross inflow of cash or receivable arising from the ordinary course of activities.

Source of Revenue	Description
Revenue from Sale of goods	Gross inflow
Revenue from Rendering of Services	Gross inflow
Revenue from other sources (Like Interest, Royalties, Dividends)	Gross inflow

i) Revenue Booking in case of Sale of Goods

In a transaction involving the sale of goods, revenue should be booked only when:

- a) The seller of goods has transferred the property in the goods to the Buyer. b) All significant risks & rewards of ownership have been transferred to the buyer & seller retains no effective control of the goods transferred. c) There is no uncertainty regarding the amount of consideration that will be received from the sale of goods.

ii) Revenue Booking in case of Rendering of Services

Methods of recognition of Revenue:

1. Proportionate completion Method

- Revenue is recognised proportionately by reference to the service completed.
- Normally we use proportionate completion method for continuous service (e.g., Teaching Service).

2. Completed Service contract Method

- Revenue is recognised when the sole or final act takes place.
- Normally we use this method when it is a one-time service (e.g., Installation service, repair service).

iii) Revenue Booking in case of income from other sources

Interest:

- Interest Revenue is recognised on time proportion Basis.

Royalties:

- Recognised on accrual Basis in accordance with the terms of the relevant agreement.

Dividends:

- Dividend income is recognised when the owner's right to receive is established.
- Generally, the right to receive dividend is established when the dividend is declared by the Company.

3. Effect of uncertainty on Revenue Recognition

Uncertainty of collection of revenue existed @ the time of Sale:

- Revenue Recognition is postponed.
- In such cases, revenue should be booked on cash Basis or when the uncertainty is resolved.

Uncertainty of collection of revenue arises subsequent to Sale:

- Do Not Reverse the sale already Booked.
- Create a provision for Bad debts.

4. Special Cases

i) Principal vs Agent

- In case of Principal & Agent relationship, the revenue of the principal is the gross amount of goods or service.
- But revenue of the agent is only the amount of commission.
- The Principal is the person who is primarily responsible to fulfill the contract.
- **Notes on GST:** GST is amount collected from customer & paid to Govt. It should not form part of Revenue for either the Principal or the Agent.

ii) Bill & Hold (Delivery is delayed @ buyer's request & buyer takes title & billing is done)

- The Buyer may purchase goods & ask the seller to hold the delivery for storage even if physical possession has not been transferred.
- In such cases, revenue can be booked on the date of billing.

Conditions to be met to Recognise sale in case of Bill & Hold: a) Goods delivery is delayed @ Buyer's request. b) Goods cannot be transferred to another customer. c) Goods are ready to be delivered to the buyer. d) Buyer has taken title (ownership) and billing is done.

iii) Sale on approval

- Revenue should not be recognised until the goods by the buyer have been formally accepted or the time period for rejection has lapsed.
 - Recognise Revenue on Date of Acceptance or when rejection period lapses.

iv) Goods sold subject to inspection / installation

If Goods are easy to install:

- Book Revenue of Goods on Date of Sale.
- If customer does not accept the goods until installation is complete:
 - Recognise revenue of Sale & revenue of Installation after installation is complete.
- If customer accepts the goods before installation:
 - Recognise revenue of sale of goods on date of acceptance of goods.
 - But recognise revenue from installation after installation is complete.

If installation of Goods is complex/difficult:

- Revenue of Sale & Installation Revenue Both - Book After installation is complete.
- Customer accepts ownership only after installation.

v) Sale & repurchase agreement

- Sale and repurchase agreements are treated as a **loan arrangement** (with the property kept as collateral).
- The transaction is not recognised as a Sale.
- The original seller (who repurchases) is involved in a Financing/loan arrangement.

vi) Trade discounts

- Trade discounts should always be deducted from Revenue.
- Sales are recorded net of Trade discount.
- Trade discount is the discount given to everybody.

vii) Cash discount

- Revenue is recognised at Gross Amount.
- Cash discount is recorded as an Expense (in P&L).
- Cash discount is the discount given for prompt payment (Jaldi paisa dene waala).

viii) Consignment Sale

- Revenue should be booked only when the goods have been sold to the ultimate customer.

ix) Interdivision Sales

- This is Not a Sale (Transfer of goods).
- No Revenue should be recognised.

Summary of Theory Content from AS 10 - Property, Plant & Equipment (PPE) Notes

1. Introduction and Scope

Core Content Areas of AS 10 - PPE:

1. Definition of PPE / Bearer Plant
2. Scope (What is not covered)
3. Recognition criteria
4. Measurement (Initial and Subsequent)
5. Subsequent cost incurred
6. Land & Building
7. Depreciation
8. Component Accounting
9. Changes in Depreciation Method, Useful Life, or Residual Value
10. Other Miscellaneous Points

I. Definition (AS 10 – Property, Plant & Equipment)

- **Property, Plant & Equipment (PPE) are:**
 - Tangible items.
 - Held for use in the production or supply of goods/services, for rental to others, OR for administrative purposes.
 - Expected to be used for more than one period (more than 12 months).
- **Bearer Plant:**
 - A living plant (like a tree).
 - Used in the production or supply of agricultural produce (e.g., a mango tree used to bear mangoes).
 - Expected to bear produce for more than 12 months.
 - *Note:* The agricultural produce itself (e.g., the mangoes) is **not** covered by AS 10.
- **Biological Assets:** Animals and plants are generally excluded from AS 10, except for Bearer Plants.

II. Scope (Not covered in AS 10)

- Assets taken on lease (covered by AS 19, Leases).
- Intangible Assets (covered by AS 26).

2. Recognition and Initial Measurement

III. Recognition Criteria

An asset (PPE) is recorded in the Books of Accounts if and only if both criteria are met:

1. Future Economic Benefits are probable (expected for more than 12 months), **AND**
2. The Costs can be measured reliably.

IV. Measurement

- **Initial Measurement:** Recorded at Cost on the day of acquisition.
- **Subsequent Measurement:** Recorded at the end of every financial year using either the:
 - Cost Model, **OR**
 - Revaluation Model.

A. Initial Measurement (@ Cost)

The cost of a purchased or self-constructed asset includes:

1. **Purchase Price:** (Less Trade Discounts).
2. **Non-Refundable Taxes:** (If the tax is refundable/Input Tax Credit is available, do not consider it in the cost of the asset).
3. **Directly Attributable Expenses:** All direct costs necessary to construct/bring the asset to the location and condition necessary for it to be capable of operating in the manner intended by management.
This includes:
 - Delivery costs.
 - Installation costs.
 - Employee costs (only if employees were directly involved in construction/acquisition).
 - Net cost of testing (cost of testing minus any income generated during the testing process).
 - Consultancy/Professional fees taken for constructing/acquiring the asset.
4. **Borrowing Costs:** (If the asset is a Qualifying Asset) – As per AS 16.
5. **Cost of Decommissioning/Dismantling/Site Restoration:** Included at its **Present Value (PV)**.

Exclusions from Cost of PPE (Transfer to P&L):

- Inauguration expenses.
- Advertising and promotional costs.
- Training costs (for employees).
- Administrative and general overheads.
- Initial operating losses.
- Cost of relocating the entity's operations.
- Cash Discount (if any) – Do not reduce from the cost of PPE.
- Miscellaneous income not related to the construction of the asset.
- Interest Expense (except for Borrowing Cost capitalised as per AS 16).

Deferred Payment Note: If an asset is purchased on deferred credit terms, the difference between the cash price equivalent and the total payment is treated as **Interest Expense** (transferred to P&L), provided the asset is not a Qualifying Asset.

Initial Measurement of Asset Acquired by Way of Exchange

A. If Transaction Has Commercial Substance:

- This happens when the future cash flows of the entity are expected to change as a result of the exchange.
- **To record the Incoming Asset (in order of preference):**
 1. Fair Value (FV) of the Asset Given Up.
 2. FV of the Asset Acquired.
 3. Carrying Amount (C.A.) of the Asset Given Up.
- Profit or loss on exchange is recognized and transferred to P&L.
- **Note:** Any asset given up is always recorded at its Carrying Amount in the journal entry.

B. If Transaction Has No Commercial Substance:

- This happens when assets of the same nature, same value, and same type are exchanged (no profit motive).
- **To record the Incoming Asset (Only 1 Preference):**
 1. Carrying Amount (C.A.) of the Asset Given Up.
- **No** profit or loss on exchange is recognized.
- **Note:** If nothing is mentioned in the question (or no hint is available regarding commercial substance), always assume that the transaction **HAS commercial substance**.

PPE Acquired Together at a Consolidated Price:

- Bifurcate the total payment among all assets acquired in the **ratio of their Fair Values**.

Land & Building (L&B):

- These are separable assets and must be accounted for separately.
- **Land:** Has infinite life and is **Non-Depreciable**.
- **Building:** Has finite life and is **Depreciable**.

3. Subsequent Measurement: Cost Model

B. Subsequent Measurement: Cost Model

- The company can choose to use the Cost Model.
- Under the Cost Model, the asset is carried at its cost less accumulated depreciation and accumulated impairment losses.

V. Subsequent Cost Incurred

- **Repairs & Maintenance:** Charge this expense to P&L.
- **Major Part Replaced:** Capitalise (treat as a major replacement/component accounting).

4. Subsequent Measurement: Revaluation Model

B. Subsequent Measurement: Revaluation Model (Fair Value Model)

The asset is carried at a revalued amount, being its fair value at the date of revaluation, less subsequent accumulated depreciation and subsequent accumulated impairment losses.

1. Frequency of Revaluation:

- If changes in the value of the asset are significant and volatile: Revalue **Annually**.
- If changes are insignificant: Revalue **Every 3 to 5 years**.

2. Treatment of Accumulated Depreciation (Acc. Deprn) on the Date of Revaluation:

- **Method 1: Eliminate Acc. Deprn against Gross Block of Asset (Net Method):**
 1. Debit Acc. Deprn A/c and Credit Gross Block A/c (PPE A/c) to eliminate the accumulated depreciation.
 2. Debit PPE A/c (Net Block) and Credit Revaluation Gain A/c (Revaluation Reserve) for the revaluation gain needed to reach the fair value.
- **Method 2: Do Not Eliminate Acc. Deprn (Gross Method):**
 1. Calculate the Revaluation Gain Percentage: $\frac{\text{Revaluation Gain}}{\text{Net Block}} \times 100\%$.
 2. Apply this percentage to:
 - Increase Gross Block (PPE A/c Dr).
 - Increase Accumulated Depreciation (Acc. Deprn A/c Cr).
 3. The balancing figure is the Revaluation Gain (Revaluation Reserve Cr).

3. Revaluation to be Applied to Entire Class of Assets:

- If one item of PPE is revalued, the entire **class** to which the asset belongs shall also be revalued.
- **Class of PPE:** Assets having a similar nature, similar use, and similar characteristics (e.g., all office buildings are one class; all factory buildings are another class).

4. Treatment of Revaluation Gain/Loss (Unrealised):

Event	First-Time Revaluation	Subsequent Revaluation (Previous Event: Gain)	Subsequent Revaluation (Previous Event: Loss)
Gain	Transfer to Revaluation Reserve (RR) (under Reserves & Surplus)	Transfer to Revaluation Reserve (RR)	Current Gain adjusts previous loss (Trf to P&L to the extent of previous loss). Excess Gain is Trf to RR .
Loss	Transfer to P&L (Debit P&L)	Current Loss adjusts previous gain (Trf to RR to the extent of previous gain). Excess Loss is Trf to P&L .	Transfer to P&L (Debit P&L)

5. Transfer of Revaluation Reserve to Retained Earnings:

- **Mandatory:** When the useful life of the PPE is over, **OR** when the PPE is sold/de-recognised.
 - *Journal Entry:* Reval Reserve A/c Dr. to Retained Earnings A/c.
- **Optional:** The company has an option to transfer **Excess Depreciation** from Revaluation Reserve to Retained Earnings annually.
 - *Excess Depreciation* = Depreciation after Revaluation – Depreciation before Revaluation.
 - *Journal Entry:* Reval Reserve A/c Dr. to Retained Earnings A/c.

5. Depreciation, Component Accounting, and Changes in Estimates

VII. Depreciation

- **Methods:** SLM (Straight-Line Method), WDV (Written Down Value Method), Units of Production Method.
- **Residual Value / Scrap Value / Salvage Value:** The estimated value of PPE at the end of its useful life. (Note: Residual value is irrelevant in the WDV method).
- **Depreciation Period:**
 - **Start Date (Commencement):** When the asset is **Available for Use**.
 - **End Date (Cessation):** When life is over, or the asset is sold.
- **Note:** If the Carrying Amount (C.A.) of the asset reaches its Residual Value, no further depreciation is charged.

VIII. Component Accounting / Major Replacement / Major Inspection / Overhaul

- Each significant part of PPE having a different useful life should be **depreciated separately**.
- When a significant component is replaced:
 - The **New Cost** of the component is **added** (Capitalised).
 - The **Old Carrying Amount (C.A.)** of the old component is **reduced** (De-recognised).

IX. Changes in Estimates

- Changes in Estimate of Depreciation method, Useful Life, or Residual Value are considered **Changes in Accounting Estimates** (as per AS 5).
- These changes require **Prospective Accounting** (affecting current and future periods only).

6. Other Miscellaneous Points

X. Other Miscellaneous Points

- **Investment Property:** Covered in AS 13, but its accounting (Subsequent Measurement) is done using the **Cost Model** of AS 10.
- **Insurance Claim Received on Damage of Assets:**
 - Record the claim as **Income** in P&L in the year in which the claim is **certain to be received**.
 - The loss on damage of the asset and the income from the insurance claim must be shown **separately**; do not net them off.
- **Spare Parts / Tools / Servicing Equipment:**
 - If they meet the definition of PPE (expected to be used for more than 12 months), they are covered in **AS 10**.
 - If they do not meet the definition of PPE, they are covered in **AS 2 - Inventory**.

De-Recognition of PPE (Books se Bahar Karna)

- **De-recognise the asset when:**
 1. It is sold, **OR**
 2. The life of the PPE is over.
- Gain or loss on the sale of PPE is a **Realised Gain/Loss** and will be transferred directly to **P&L**.
- On De-Recognition of PPE, any remaining balance in the **Revaluation Reserve** must be transferred to **Retained Earnings** (mandatory).

Changes in Existing Decommissioning/Dismantling/Site Restoration Provision

This change may result from a change in timing, amount, or discount rate.

Asset Status	Asset is @ Cost Model	Asset is @ Revaluation Model
Treatment	Adjust the change in Provision for Decommissioning from the Cost of the Asset .	Adjust the change in Provision for Decommissioning from Revaluation Reserve (Gain/Loss).
Increase in Provision	PPE A/c Dr. to Prov. for Decommng A/c	Revaluation Loss A/c Dr. to Prov. for Decommng A/c
Decrease in Provision	Prov. for Decommng A/c Dr. to PPE A/c	Prov. for Decommng A/c Dr. to Revaluation Gain A/c

Important Note for Exams: If any question of AS comes in the exam, write 2-3 lines of the relevant concept in your own words along with the AS Name and Number.

AS 11 - The Effects of Changes in Foreign Exchange Rates

1. Scope

Accounting for the following is discussed in AS 11:

1. Foreign currency transactions.
2. Translating the Financial Statements of foreign operations. (Discussed in Branch Accounts)
3. Accounting for forward exchange contracts.

2. Definitions

- **Reporting Currency:** It is the currency in which Financial Statements are prepared.
- **Foreign Currency:** It is the currency other than the reporting currency.
- **Monetary Items:** Monetary items are those assets and liabilities, which are to be received or paid in fixed or determinable amounts of money.
 - *Examples:* Cash and cash equivalents, Trade receivables or Debtors, Trade payables or Creditors.
- **Non-Monetary Items:** Non-monetary items are assets and liabilities, other than monetary items.
 - *Examples:* Property, Plant, and Equipment (PPE), Inventories, Share Capital, Investments in Equity shares, etc.
 - *Note:* Monetary / Non-Monetary concept is only for Balance Sheet items.

3. Accounting for Foreign Currency Transactions

- A foreign currency transaction is a transaction which is denominated or requires settlement in a foreign currency.
- *Examples of foreign currency transactions:*
 - Purchase or sale of goods and services in foreign currency.
 - Borrowing or lending of funds in foreign currency.
 - Purchase or sale of Property, Plant, and Equipment (PPE) denominated in foreign currency.

Summary of Foreign Currency Transactions

Measurement Stage	Initial Measurement	Subsequent Measurement (at year-end)
Measurement Rule	Recognize using Rate on Date of Transaction	Monetary Item: Remeasured @ Closing Rate
		Non-Monetary Item:
		Carried at Historical Cost → No need to Remeasure at year-end.
		Carried at Fair Value or Net Realizable Value (NRV) → Remeasure @ Closing Rate at year-end.

- *Examples for Non-Monetary Items:*
 - PPE @ Cost Model
 - Inventory @ Cost
 - Investments @ Cost
 - PPE @ Revaluation Model
 - Inventory @ NRV
 - Investments @ Market Value

Foreign Exchange Rate Difference

- The difference arising from remeasurement of monetary items or settlement of foreign currency transactions is **Transferred to Profit and Loss (P/L) Account**.

Shortcut for Foreign Exchange Gain/Loss (for Monetary Items)

Item	Asset (e.g., Trade Receivable)	Liability (e.g., Trade Payable)
Exchange Rate increases (↑)	Exchange Rate ↑ → Loss	Exchange Rate ↑ → Gain
Exchange Rate decreases (↓)	Exchange Rate ↓ → Gain	Exchange Rate ↓ → Loss

4. Exception to charging Exchange Gain/Loss to Profit and Loss (P/L) Account (Para 46A)

- This option is available when a company has a **Long Term foreign currency monetary item** (e.g., Long term foreign loan).
 - *(Do not apply this for Debtors/Creditors/Short term loans etc.)*
- Once the option is exercised, it is **irrevocable**.

Treatment of Exchange Difference on Long Term Foreign Currency Monetary Item

Situation	Treatment of Exchange Difference (Ex Diff)
Related to a depreciable Asset (Long term foreign loan taken for depreciable Asset)	Ex Diff on long term loan can be adjusted from the cost of Asset .
	Ex Loss → Add to cost of Asset
	Ex Gain → Less from cost of Asset
NOT related to depreciable Asset	Ex Diff shall be transferred to a separate account in the Balance Sheet named "Foreign Currency Monetary Item Translation Difference Account" (FCMITD A/c).
	The balance in the FCMITD A/c will be transferred to Profit and Loss Account over the period of the remaining loan term .

5. Translation of Financial Statements of Foreign operation

A) Classification of Foreign operation

- Integral Foreign Operation (IFO)
- Non-Integral Foreign Operation (NIFO)

B) Translation of Financial Statements

- Already covered in Branch Accounts.

C) Treatment of Exchange Difference

- IFO → Profit and Loss (P/L) Account
- NIFO → Foreign Currency Translation Reserve (FCTR)

D) Indicators for identification of Non-Integral Foreign Operation

- Non-integral foreign operation should have a **significant degree of independence** in its activities.
- Transactions with the head office are in **very low proportion**.
- Transactions and activities of foreign operation are **mainly financed from its own operations or local borrowings**.

- Cost of labour, material, and other components are **primarily paid in local currency** of foreign operation.
- Foreign operation sales are **mainly in their own currency**.
- Sales prices are **determined by local competition** of foreign operation.
- There is an **active local sales market** for foreign operation's products.

E) Changes in classification of foreign operation

Change	Treatment
Integral → Non-Integral	Exchange Gain/Loss (Ex G/L) from the date of reclassification is transferred to FCTR .
Non-Integral → Integral	Ex G/L from the date of reclassification is transferred to P/L Account .
	<i>(Old Ex Diff will continue to stay in FCTR)</i>

6. Accounting for Forward Exchange Contracts

Forward Exchange Contract entered for managing risk (Hedging)	Forward Exchange Contract entered for trading or speculation
Hedging	Speculation
Loss / Gain	Profit / Loss
Premium or discount arising at the inception of such forward contract should be amortized over the life of the contract .	Here the Profit / Loss is computed by comparing forward rate and sale rate , and such profit/loss is recorded in P/L Account .
<i>Method:</i> Compare Forward rate and Spot rate → (+) Forward Contract Book Ex G/L over the contract period	<i>Method:</i> Compare Forward rate and Sale rate Book Profit / Loss on sale date.
<i>Examples:</i> Purchase of Plant/Goods	<i>Example:</i> Only forward contract (no underlying transaction)

AS 12: Accounting for Government Grants

1. Definition of Government Grant

- It is assistance by government, in cash or kind, for past or future compliance with certain conditions.

2. Scope

- AS 12 does not apply to:
 - Grants such as tax holiday period, tax exemption, etc.
 - Government participation such as investment by government in a company as an equity shareholder.

3. Recognition of Government Grants

- A government grant is **NOT recognised** until there is **reasonable assurance** that:
 - The enterprise will comply with the conditions attached to the grant **AND**
 - The grant will be received.

4. Accounting Treatment of Government Grants

The approaches for accounting are:

- **Capital Approach** (Capital Grant)
- **Income Approach** (Revenue Grant)

5. Types of Government Grants

- **Monetary Grants** (Received in Cash)
- **Non-Monetary Grants** (Received in Kind)
 - **Received Asset at concessional rate**
 - Record at **acquisition cost**.
 - The company will provide depreciation on the recorded cost.
 - **Received Asset free of cost**
 - Record at **Nominal value** (Immaterial value).
 - The credit side is to **Government Grant (Capital Reserve)**.

6. Grant Relating to Fixed Assets (Property, Plant, and Equipment - PPE)

This is a **Monetary Grant**.

- **First Method: Reduce from the cost of Asset**
 - The grant is reduced from the cost of the asset.
 - The net value of the asset is the cost minus the grant.
 - Depreciation is calculated on the net value of the asset.
- **Second Method: Treat the Grant as Deferred Income**
 - Treat the grant as **Deferred Income** (Deferred Government Grant - DGG).
 - Recognise the income in proportion to the Depreciation or Life of the Asset.
 - Journal Entry for Grant: Bank Account Debit to Deferred Government Grant.
 - Journal Entry for Transfer: Deferred Government Grant Account Debit to Profit and Loss Account (Other Income) in proportion to the depreciation/life of the asset.
 - Depreciation is calculated on the full cost of the asset.

7. Grant Relating to Revenue Nature

These grants are received to reimburse expenses of the company (e.g., Salary Expense, Employee Training Expense, etc.).

- **Grant received to reimburse expenses of one year**
 - **First Method: Show Expense and Income Separately**
 - Show the full expense in the Profit and Loss Account (Debit side).
 - Show the grant as **Other Income** in the Profit and Loss Account (Credit side).
 - **Second Method: Adjust the Grant from Expense**
 - The grant amount is deducted from the expense itself in the Profit and Loss Account.
- **Grant received to reimburse expenses of multiple years**
 - Treat this grant as a **Deferred Government Grant (DGG)**.
 - Transfer the DGG to the Profit and Loss Account over the number of years for which the expense is being reimbursed.

8. Grant in the Nature of Promoter's Contribution

- **Related to Fixed Assets (PPE)**
 - **Non-Depreciable Asset** (e.g., Land)
 - **Method 1: Reduce the Grant from cost of Asset**
 - The grant is reduced from the cost of the asset.
 - The net value of the asset is cost minus grant.
 - No Depreciation is charged as it is a Non-Depreciable Asset.
 - **Method 2: If the Company does NOT want to reduce Grant from Cost of Asset**
 - **Grant is unconditional** (No conditions to be fulfilled):
 - Treat this like a **Promoter's Contribution**.
 - Credit the grant to **Government Grant (Capital Reserve)**.
 - **Grant is conditioned** (e.g., Company cannot sell the land for next 5 years):
 - Treat the grant as **Deferred Government Grant (DGG)**.
 - Transfer the DGG to the Profit and Loss Account over the period of the condition.
- **General Hint** that grant is in nature of promoter's contribution: Grant received to set up Business/Plant/Machinery in a Backward/Notified area/region.

9. Refund of Government Grant

- **Note:** Refund of Government Grant is treated as an **Extra-ordinary item** as per AS 5.
- **If Grant received was adjusted against Cost of Asset:**
 - Refund of Grant will also be **adjusted against the cost of the asset**.
 - Journal Entry: Refund Account Debit (or PPE Account Debit) to Bank Account.
 - After this entry, the **Carrying Amount of the asset increases**.
 - Depreciation for subsequent years will also **increase** (i.e., **prospectively**, No Retrospective effect).
- **If Grant received was transferred to Deferred Government Grant (DGG) as deferred income:**
 - Refund of Grant will be done **from DGG up to the balance in DGG**.
 - **Excess refund, if any**, will be adjusted against the **Profit and Loss Account**.
 - Journal Entry for Refund (when refund amount exceeds DGG balance):
 - Deferred Government Grant Account Debit (Balance amount)
 - Profit and Loss Account Debit (Balancing Figure - B/F)
 - To Bank Account (Full Refund Amount)

- There will be **no change in the cost of Fixed Asset** and the amount of Depreciation (i.e., Depreciation charged will be on the same basis as charged in earlier years) because the grant was not adjusted against the asset cost initially.

- **If Grant received was transferred to Capital Reserve:**

- Refund will also be **adjusted from Capital Reserve**.
- Journal Entry: Capital Reserve Account Debit to Bank Account.

10. Grant Relating to Revenue Nature (General Principle for Multi-Year Reimbursement)

- Grant received to reimburse expenses of multiple years.
 - Treat the grant as a **Deferred Government Grant (DGG)**.
 - The DGG is transferred to the Profit and Loss Account over the years.
 - **Refund Treatment:**
 - The refund is adjusted from the DGG balance.
 - If the refund exceeds the DGG balance, the excess is debited to the Profit and Loss Account.

AS 13 - Accounting for Investments

1. Forms of Investment

Fixed Income (Interest Income)	Dividends	Rentals	Capital Appreciation
Fixed Deposits	Equity Shares	Property	Land/Property
Debentures	Preference Shares		Gold
Bonds			Shares, Debentures, Bonds etc.

Note: Investments are assets held by an enterprise for earning income by way of Interest, dividends, rentals, or capital appreciation.

2. Scope

This standard does not deal with:

- The basis of recognition of interest, dividends, rentals earned on investments (covered by Accounting Standard 9).
- Operating or finance lease (Accounting Standard 19).
- Investments on retirement benefits plans (Accounting Standard 15).
- Investments in enterprises like Insurance companies, Mutual funds, venture capital funds & asset management companies like banks, financial institutions, etc.

3. Classification of Investments

Current Investment (Temporary Investment)	Long Term Investment
Held for less than 12 months	Other than current investment (Intention to hold for 12 months or more)
Current Investment Measurement	Long Term Investment Measurement
Measured at: Cost OR Market value (whichever is lower)	Measured at Cost
Any decrease will be recorded in Profit and Loss Account.	Only other than temporary decrease (i.e., permanent decrease) will be recorded.
Journal Entry for loss: Profit and Loss Account Debit To Investment Account	Such permanent decrease will be recorded in Profit and Loss Account.
	Examples of Permanent Decrease:
	Cash operating losses
	New Regulations having negative impact etc.

Example of Loss Recording (Current Investment):

Cost	Market Value	Measured at	Journal Entry for loss
100	110	100 (Cost)	
100	80	80 (Market Value)	20 Profit and Loss Account To Investment Account 20

Example of Loss Recording (Long Term Investment):

Cost	Market Value	Case	Recorded at	Journal Entry for loss
100	90	Decrease is Temporary	100	-
100	90	Decrease is NOT Temporary	90	10 Profit and Loss Account Debit To Provision for Diminishing Investment 10
Balance Sheet View	Investment 100 Provision for Diminishing Investment (10) 90			

4. Reclassification of Investment

Current to Long Term	Long Term to Current
Measured at: lower of cost or Market value of the date of transfer.	Measured at: lower of cost or carrying Amount in Books at the date of transfer.

Hint: Current to Long Term (New Category) → Apply the criteria of old category.

Note: If nothing mentioned about Gold & Silver, always assume it to be long term.

5. Accounting for Investments in Debentures/Bonds

- **Note:** Interest payment on purchase of Debenture is mandatory.
- Interest is always calculated on **face value**.

Concepts related to Interest:

- **Ex-Interest (Excluding Interest):** The price quoted is for the principal amount only, and the buyer separately pays the interest accrued up to the date of transaction.
- **Cum-Interest:** The price quoted includes the interest accrued up to the date of transaction. The buyer pays a single price, and the seller has to calculate the separate cost of the debenture (Ex-Interest Cost) and the accrued interest paid.

Important Accounting Points for Debentures Ledger:

- Interest column Balance is Transferred to Profit and Loss Account.
- Face value and Amount (Cost) columns are Transferred to Balance carried down.

Acquisition Cost (Brokerage, Stamp duty, other direct cost incurred while purchase/sale of debenture):

Transaction	Treatment of Costs
Incurred on Purchase of Investment	Add to cost of Investment
Incurred on Sale of Investment	Less from Selling Price of Investment

Partial Sale of Investment:

- Where investments were purchased at different dates and now part of it are sold, the Carrying Amount/cost of Debenture will be calculated using **Weighted Average Method** (as permitted by AS 13).
- But if the question specifically mentions to follow the **First In First Out (FIFO) method**, then use the FIFO Method.

Accounting when Interest Due Date $\neq$ Year End:

- On purchase of Debenture, calculation of Interest will be done from **last due date of Interest till date of purchase**.
- On year end, first calculate **Interest Accrued** from last due date of Interest till year end (write in By balance carried down Interest column).
- Then close the ledger:
 - Interest column Total is Transferred to Profit and Loss Account.
 - Nominal Value and Amount column are Transferred to balance brought down.
- On Opening Balance, **Interest Accrued** will also appear in Balance brought down.

6. Accounting for Investment in Equity Shares

- **Note:** Unlike Debenture, in equity shares, there is **No fixed Return**.

Sale of Equity Shares:

- If nothing is mentioned, Accounting Standard 13 prescribes to use the **Weighted Average Method** for calculating the cost/carrying amount of shares sold.

Bonus Shares received on Investment in Equity Shares:

- When the company promises to give **free equity shares** to the existing shareholders.
- As Bonus shares are received for free, the **cost of these shares is NIL**.
- **Note:** Bonus shares will also be considered while calculating the **weighted average cost**.

Rights Shares received on Investment in Equity Shares:

- The company gives an option to existing shareholders to subscribe (Buy) more shares at a lower/discounted price.
- **Renouncement:** Investor has the option to either **Subscribe (Buy)** more shares or **Renounce (transfer this right to a third party)** for a small consideration.
- If the right is renounced/sold to a third party, the consideration received is **credited to the Profit and Loss Account** (not the Dividend Column in the ledger).
- The cost of subscribed right shares is the actual amount paid for them.

Dividend (Final Dividend) - Return on Investment in Equity Shares:

- Dividend is always paid on **face value** of shares.

Type of Dividend	Accounting Treatment	Ledger Impact
Pre-Acquisition Dividend (Dividend on Opening Shares and Dividend on Current Year Purchases which is related to the period before acquisition)	Recovery of Cost.	Record in Amount column (reduces cost of investment).
Post-Acquisition Dividend (Dividend received on shares purchased in the Current Year which is related to the period after acquisition, or dividend received on Bonus/Right Shares)	Dividend Income.	Record in Dividend column (transferred to Profit and Loss Account).
Dividend on Bonus/Right Shares	Not Applicable (This is a point/hint, as bonus and right shares received in the current year do not have pre-acquisition or post-acquisition dividend in the same year).	

Note on Sale/Purchase on Interest Due Date:

- Whenever a Sale/Purchase Transaction is on the same day as the Interest due date, then:

1. First, do the Transaction of Sale/Purchase.
2. Second, then record Interest on the due date.

Note on Valuation of Investment:

- Cost or Market Value (whichever is lower) is to be done **only when information of Market price is available** (specifically for Current Investments at the year end).

AS 14 - Amalgamation of Companies

1. Introduction

Amalgamation	Absorption	External Reconstruction
Two or more companies are wound up and a new company is formed to take over the business.	In this case, an existing company takes over the business of one or more existing companies.	In this case, a newly formed company takes over the business of an existing company.
<i>Example: A Limited and B Limited amalgamate to form C Limited. (A Limited and B Limited are wound up.)</i>	<i>Example: A Limited takes over the business of another existing company B Limited. (B Limited is wound up.)</i>	<i>Example: B Limited is formed to take over the existing company A Limited. (A Limited is wound up.)</i>

- **Transferor company (Selling Company):** The companies which are going to be liquidated or sold are known as selling companies or vendor companies or transferor companies.
 - **Transferee company (Purchasing Company):** The company which is going to take over the liquidated companies is known as purchasing or vendee or transferee Company.
-

2. Purchase Consideration (PC)

- **Who gives:** Purchasing Company (Transferee)
 - **To whom gives:** Selling Company (Transferor) → Owners (Shareholders)
 - **What is given:** Cash, Assets, Equity Shares, Preference Shares, Debentures, or other securities.
 - **AS 14 Definition:** Purchase consideration is defined as the **aggregate of shares, cash, assets, or any other securities** given by the transferee company to the **shareholders of transferor companies**.
 - **Note:** Purchase consideration does not include anything which is payable to the Debenture-holders or creditors of the transferor company.
-

3. Methods to Calculate Purchase Consideration

A. Lump-sum method

- In this method, the amount of PC is already available in the question (what is given and how much is given is already available).

B. Net Payment method (Transferee)

- In this method, the company gives Cash, Equity shares of purchase or transferee, Preference shares, Debentures, Any other assets, etc.
- The question already specified what is given in PC and how much is given in PC.

C. Net Asset Method

- In this method, normally the amount of PC is **not available** in the question.
- Calculation:

Assets taken over at agreed value / market value / fair value XX Less: Liabilities taken over (XX) Purchase consideration XX

D. Intrinsic Value method

- **Formula for Number of Shares to be given in PC:** Number of shares of transferor × Share price of transferor, divided by share price of transferee.
- **Note:** In the exam, the method for calculation of PC will be used according to data available in the question.

E. Calculation of Purchase Consideration to Preference Shareholders (to maintain same amount of dividend):

- **Amount of dividend to be maintained** = Face Value of Preference Shares of Transferor Company × Rate of Dividend of Transferor Company
- **Value of Preference Shares to be issued** = Amount of Dividend to be Maintained / Rate of Dividend of Transferee Company
- **Number of Preference Shares** = Value of Preference Shares to be issued / Face value per share

F. Calculation of Purchase Consideration to Preference Shareholders (based on return on Net Assets):

- **Return on Net Asset** = Total value of Net Assets acquired of transferor company × Return Percentage
- **Value of Preference shares to be issued** = Return on Net Asset / Rate of Dividend of Transferee Company

4. Accounting in the Transferee company (Purchasing Co.) (As per AS 14)

A. Amalgamation in the nature of merger Amalgamation in the nature of merger will have to satisfy all the following conditions:

1. All assets and Liabilities (along with reserves) of the transferor company, after amalgamation will become the asset and liability of transferee company.
2. Shareholders at least holding 90% of Face Value of equity shares of the transferor company will become equity shareholders of transferee company.
3. Consideration will be wholly by the issue of shares except that cash must be given in respect of fractional shares.
4. Business of transferor company is intended to be carried on, after the amalgamation by the transferee company.
5. All Assets and Liabilities will be taken over at **Book Values** instead of fair values.

B. Amalgamation in the nature of purchase

- If any one or more of above conditions are not satisfied, then it will be amalgamation in the nature of purchase.

5. Journal Entries in the Books of Purchasing Co. (Transferee Co.)

Particulars	Purchase Method (In the nature of Purchase)	Pooling of Interest Method (In the nature of merger)
1. PC due	Business Purchase Account Debit (XX) To Liquidator of Transferor (XX) (Amount of PC)	Business Purchase Account Debit (XX) To Liquidator of Transferor (XX) (Amount of PC)
2. Assets, Liabilities & Reserves taken over	Assets taken over Account Debit (@Fair value/Market value/Agreed value) Goodwill (Balancing Figure) Account Debit To Liabilities taken over Account (@Fair value/Agreed value) To Business Purchase Account (PC) To Capital Reserve (Balancing Figure) Account (If PC is less than Net Assets)	All Assets Account Debit (@Book Value) Reserves Account Debit (Balancing Figure) To All Liabilities Account (@Book Value) To All Reserves Account (@Book Value) To Business Purchase Account (PC) To Capital Reserve Account (Balancing

Particulars	Purchase Method (In the nature of Purchase)	Pooling of Interest Method (In the nature of merger)
		Figure) (Only if difference remains after adjustment with Reserves)
<i>Note on Purchase Method (Point 2):</i> If PC is more than Net Assets (NA), the difference is Goodwill (We paid more). If PC is less than Net Assets, the difference is Capital Reserve (We paid less).	<i>Note on Merger Method (Point 2):</i> The difference between (Assets - Liabilities - Reserves) and PC is adjusted against the Reserves of the transferor company first. If any balance remains, it is transferred to Profit and Loss Account or General Reserve or Capital Reserve.	
3. Payment of PC to liquidator	Liquidator of Transferor Account Debit To Cash / Bank Account To Equity Share Capital (Face value) To Securities Premium (Premium on Equity shares) To Preference Share Capital (Face value) To Securities Premium (Premium on Preference shares) To Any other PC	Liquidator of Transferor Account Debit To Cash / Bank Account (Only for fractional shares) To Equity Share Capital (Face value) To Securities Premium (Premium on Equity Shares) To Preference Share Capital (Face value) To Securities Premium (Premium on Preference shares) To Any other PC
4. Settlement of old Debentures of Selling Co.	Old Debentures (Debenture holders) Account Debit To New Debentures Account To Securities Premium (if any)	Same: Old Debentures (Debenture holders) Account Debit To New Debentures Account To Securities Premium (if any)
5. Liquidation expenses borne by purchasing	Goodwill / Capital Reserve Account Debit (XX) To Cash / Bank (XX)	Reserves Account Debit To Cash / Bank
6. Inter Company Owings (Elimination)	Creditors / Bills Payable Account Debit To Debtors / Bills Receivable Account (XX)	Same: Creditors / Bills Payable Account Debit To Debtors / Bills Receivable Account (XX)
7. Recording of Statutory Reserves of Selling Co. (for Amalgamation in the nature of Purchase)	Amalgamation Adjustment Reserve Account Debit To Statutory Reserves Account (Statutory Reserve is shown under Reserves and Surplus as positive balance & Amalgamation Adjustment Reserve is also shown under Reserves and Surplus as negative balance. This is just an adjustment entry i.e. it has no effect on calculation of PC and Net Assets) List of statutory Reserves: Export Profit Reserve, Investment Allowance Reserve, Foreign Project Reserve, Site Restoration fund etc.	No such adjustment required in merger as we are already taking over all reserves.
8. Elimination of Stock Reserve (unrealised profit on Inventory)	Goodwill / Capital Reserve Account Debit To Inventory	Reserves Account Debit To Inventory

- **Note:** Elimination of unrealised profit on inventory (Stock Reserve) is to be done only in the Books of Purchasing Company.

Important Note on Settlement of Debenture Holders

- **Settlement Value** = Amount to be paid to Debenture holders (Face value + Premium paid to Debenture holders).
- **Number of Debentures Issued** = Settlement Value / (Face Value per Debenture - Discount or + Premium on issue of new Debenture).
- The journal entry for settlement of debenture holders is:

Old Debentures (Debenture Holders) Account Debit Discount on Issue of Debentures Account Debit (if new debentures are issued at discount) To New Debentures (Face Value) To Securities Premium (if new debentures are issued at premium) *Note: The premium/discount paid to old debenture holders to settle their account is accounted for in the Debenture Holders account, while the premium/discount on the issue of new debentures is recorded in the Journal Entry.*

AS 15 - Employee Benefits

The Accounting Standard 15 deals with four types of employee benefits:

1. Short term employee Benefits
2. Post Employment Benefits
3. Other long term Benefits
4. Termination Benefits

General Principle: Book Expense in the year in which it accrued, Payment date does not matter.

Employee:

- The term employee is not defined under AS 15 but states that an employee may provide services to an entity on a full time, part time, permanent, casual, or temporary basis.
- For the purpose of this standard, employees include directors and other management personnel.

I. Short Term Employee Benefits

- Short term employee Benefits (other than termination Benefit) are payable within 12 months from the end of the period in which service is rendered.
- Types of Short Term Employee Benefits:
 1. Salary / Wages
 2. Bonus
 3. Leave compensation

Accounting for Salary / Wages:

- If accrued but not paid:
 - Journal Entry (J-E): Salary Expense Account Debit to Outstanding Salary (Payable)
- If paid:
 - Journal Entry (J-E): Salary/Wages Expense Account Debit to Cash In Bank

Accounting for Bonus:

- Bonus expense is accrued in the period (e.g., Year X1-X2) when the employee earns it (e.g., based on Profit target) even if payment is made later (e.g., Year X2-X3).
- Journal Entry (J-E): Bonus Expense Account Debit to Bonus Payable (Liability)
- Later when you pay off your outstanding liability (e.g., Year X2-X3):
 - Journal Entry (J-E): Bonus Payable Account Debit to Cash In Bank

Accounting for Leave Compensation (Earned leaves):

1. **Accumulating (Carry forward is permitted):**
 - **Vesting:** Leaves can be encashed.
 - **Non-Vesting:** Leaves cannot be encashed but such unused leaves will be carried forward to the next year.
 - In the year the employee earns the leaves (e.g., Year X1-X2), the payment has accrued.
 - Journal Entry (J-E): Leave Compensation Expense Account Debit to Payable / Outstanding
 - In the next year (e.g., Year X2-X3) when outstanding liability is paid:
 - Journal Entry (J-E): Payable Account Debit to Cash In Bank (For the liability accrued in X1-X2)
2. **Non-Accumulating (Carry forward is Not permitted):**
 - Unused leaves will lapse.
 - No accounting treatment is required.

Note on Booking Expense and Liability for Leave Compensation:

- When Booking Expense and Credit for leave compensation, consider **estimates** regarding how many leaves the employee will be able to utilize in the future.
- The company will book leave Compensation Expense only for the estimated number of days the employee is expected to utilize in the future from the leaves earned in the current year.
- Journal Entry (J-E): Leave Compensation Expense Account Debit to Provision for Leave Compensation (Provision only for estimated days)

II. Post Employment Benefits (Retirement Benefits)

- Post Employment Benefits are those benefits which are paid to the employee on the event of retirement from the company.
- Post employment Benefits can be of 2 types:
 1. Defined Contribution Plan (DCP)
 2. Defined Benefit Plan (DBP)

1. Defined Contribution Plan (DCP)

- These are post employment benefit plans under which an enterprise pays fixed contribution to a separate fund, and that fund will provide the benefit to the employee on retirement (e.g., Provident Fund).
- After contribution by the Company to the fund, there is **no risk** on the company (Actuarial risk and Investment risk fall on the fund).
- If the contribution is accrued but not paid by the balance sheet date:
 - Journal Entry (J-E): Provident Fund Expense Debit to Provident Fund Payable (Liability)
 - If payment is due after 12 months from the balance sheet date, the liability must be booked at the **Present Value (discounted value)**.
 - Interest Expense (Unwinding) will be booked in the subsequent period:
 - Journal Entry (J-E): Interest Expense (Profit and Loss) Debit to Provident Fund Payable

2. Defined Benefit Plan (DBP) (e.g., Gratuity)

- These are post employment benefit plans other than Defined Contribution plans.
- In Defined Benefit plans, the **risk** (Actuarial risk / Investment risk) falls on the **company itself**.
- The benefit is paid by the company, not a separate fund.
- **Important Terms for Defined Benefit Plan (Accounting done as per Projected Unit Credit Method):**
 1. **Current Service Cost (CSC):** Expense → Profit and Loss
 2. **Interest Cost:** Expense → Profit and Loss
 3. **Defined Benefit Obligation (DBO):** Liability → Balance Sheet (Liability)
 4. **Actuarial Gain / loss on DBO:** Gain / Loss → Profit and Loss
 5. **Past Service Cost (Vested / Unvested):** Expense → Profit and Loss (Only Vested portion is immediately recognized in Profit and Loss)
 6. **Plan Assets (PA):** Asset → Balance Sheet (Asset)
 7. **Expected Return / Interest Income on Plan Assets:** Income → Profit and Loss
 8. **Actuarial Gain / loss on Plan Assets:** Gain / Loss → Profit and Loss
 9. **Curtailment / Settlement:** Expense / Gain → Profit and Loss

Current Service Cost (CSC):

- The estimated benefit (e.g., Gratuity) which will be paid after the retirement period is accrued over the period of service using the Projected Unit Credit Method.
- The estimated annual accrued cost is then discounted to its **Present Value** to calculate the Current Service Cost for the year.
- Journal Entry (J-E): Gratuity Expense (Current Service Cost) Debit to Defined Benefit Obligation (DBO)

Interest Cost:

- Interest cost is calculated each year on the **Opening Balance of Defined Benefit Obligation** at the discount rate.
- Journal Entry (J-E): Interest Expense Debit to Defined Benefit Obligation (DBO)

Actuarial Gain/Loss on DBO:

- These are gains/losses in DBO which result from **changes in estimates** (e.g., change in increment percentage, completed years of service, Discount Rate, number of employees, etc.).
- If Present Value of DBO increases: **Actuarial Loss on DBO** (Profit and Loss)
 - Journal Entry (J-E): Employee Benefits Expense Debit to Defined Benefit Obligation
- If Present Value of DBO decreases: **Actuarial Gain on DBO** (Profit and Loss / Other Employee Benefits Income)
 - Journal Entry (J-E): Defined Benefit Obligation Account Debit to Actuarial Gain on DBO

Past Service Cost (PSC):

- This results from a **Plan Amendment**. The Balance of DBO will also increase due to the Plan Amendment. (e.g., Gratuity percentage increases).
- **Vested PSC**: (Expense related to past years that changed due to amendment) → Recognized immediately in **Profit and Loss** Account.
- **Unvested PSC**: (Expense related to future years that will change due to Plan Amendment) → Deferred and amortized over the **remaining service period** (Asset in Balance Sheet).
- Journal Entry (J-E for Plan Amendment that increases DBO):
 - Vested Past Service Cost (Profit and Loss) Debit
 - Unvested Past Service Cost (Asset) Debit
 - To Defined Benefit Obligation

Plan Assets (PA):

- These are investments specifically done to fund our Defined Benefit Obligation.
- Journal Entry (J-E for Contribution in Plan Assets):
 - Plan Assets Account Debit to Cash In Bank Account

Expected Return on Plan Assets:

- The Expected Return on Plan Assets (Rate will be same as Discount factor used for DBO for Present Value) is treated as an income (reduction of expense) in the Profit and Loss Account.
- Journal Entry (J-E): Cash In Bank Account Debit (OR Plan Assets Account Debit) to Expected Return on Plan Assets (Profit and Loss - Negative Employee Benefits Expense)

Actuarial Gain / Loss on Plan Assets:

- Plan Assets are always measured at **Fair Value**.
- **Actual Return on Plan Asset** = Expected Return (+) Actuarial Gain (-) Actuarial Loss on Plan Assets.
- **Actuarial Gain on PA** is the amount by which the Fair Value of Plan Assets at the year-end exceeds the calculated balance (Opening Balance + Expected Return + Contribution - Benefits Paid). This gain is transferred to the **Profit and Loss** Account.

Curtailment and Settlement:

- **Curtailment**: Cancellation of a plan (e.g., Total DBO was reduced without any settlement payment).
 - Journal Entry (J-E): Defined Benefit Obligation Account Debit to Gain on Curtailment
 - When curtailment reduces DBO, a portion of the unamortized unvested Past Service Cost (PSC) related to the curtailed portion is also written off.
 - Journal Entry (J-E for Curtailment):
 - Defined Benefit Obligation Account Debit
 - To Unvested Past Service Cost
 - To Gain on Curtailment (Balancing Figure)
- **Settlement**: Occurs when the entity settles the Plan Before the due date (e.g., DBO settled for less than the obligation amount).
 - Journal Entry (J-E for Settlement):
 - Defined Benefit Obligation Account Debit
 - To Cash In Bank Account
 - To Gain on Settlement

Note on Actuarial Valuation:

- AS 15 states that Actuarial valuation should be conducted once in every 3 years, provided there are no major changes in estimates.

III. Other Long Term Benefits

- These are employee Benefits (other than retirement Benefits) which are paid **after 12 months** from the end of the reporting period.
- **Examples:**
 - Long term compensated absences such as Sabbatical leaves.
 - Long term disability benefits.
 - Any other compensation to be paid after 12 months.
- **Accounting:** Accounting is the same as the **Defined Benefit Plan**.

IV. Termination Benefits (e.g., Retrenchment Scheme, Voluntary Retirement Scheme - VRS)

- Termination Benefits are recognized as an expense and liability **only when:**
 - A detailed formal plan for the termination is duly approved **AND**
 - A reliable estimate can be made of the amount of obligation.
- **When termination benefits fall due within 12 months after Balance Sheet date:**
 - Book Liability at **undiscounted value**.
 - Journal Entry (J-E for Accrual): Expense (VRS) Account Debit to Payable
 - Journal Entry (J-E for Payment): Payable Account Debit to Cash In Bank
- **When termination benefits fall due after 12 months from Balance Sheet date:**
 - Book Liability at **discounted value** (Present Value).
 - Journal Entry (J-E for Accrual): Expense (VRS) Account Debit (at Present Value) to Payable
 - Interest Expense (Unwinding) will be booked in the subsequent period:
 - Journal Entry (J-E): Interest Expense Debit to Payable
 - Journal Entry (J-E for Payment): Payable Account Debit to Cash In Bank

AS 16 - Borrowing Costs

1. Definitions

- **Borrowing Costs:** These are Interest and other costs incurred on borrowing of funds.
 - Borrowing costs incurred on **Qualifying Assets** will be **Capitalised** (i.e., Added to the cost of the Asset).
 - Normally, Borrowing Costs are charged to the Profit and Loss Account (Expense).
- **Qualifying Asset (QA):**
 - An asset which takes a **substantial period of time** to get ready for its intended use or sale.
 - Generally, a period of **12 months or more** is considered to be substantial for a qualifying asset, but in some cases, a shorter period of less than 12 months can also be considered substantial, if justified.
- **Mandatory conditions for AS 16 Applicability:**
 - Loan लेना पड़ेगा (A loan must be taken).
 - Qualifying asset पर खर्चा करना पड़ेगा (Expenditure must be incurred on a qualifying asset).
 - If these two things are mandatory, then AS 16 - Borrowing Cost is Applicable, and Interest Expense will be capitalised to the cost of the asset.

2. Types of Borrowing Costs Covered in AS 16

Interest Charges on Borrowings	Amortisation of Premium/Discount on Borrowings	Ancillary costs relating to Borrowings (e.g., loan raising fees, loan processing fees etc.)	Finance charge on asset acquired on Finance lease (Discussed in AS 19)	Exchange loss on foreign loan (Discussed later in this chapter)
Yes	Yes	Yes	Yes	Yes

3. Borrowings Not Covered Under AS 16

- Borrowing funds by issuing equity share capital.
- Borrowing funds by issuing preference share capital.

4. Examples of Qualifying Assets

- Property, Plant, and Equipment (as per AS 10).
- Intangible Assets (as per AS 26).
- Investment property.
- Inventories (which take a substantial period of time to produce).
- Readymade investments purchased, like investment in equity shares, are **Not** a Qualifying Asset.
- If an asset is purchased in ready-made condition, it is **Not** a Qualifying Asset.

5. Borrowing Cost Eligible for Capitalisation

- If Borrowing cost is **Directly related** to the acquisition, construction, or production of Qualifying Assets → **Capitalised**.
- If Borrowing cost is incurred for assets **other than** Qualifying Assets → **Transferred to Profit and Loss Account**.

6. Types of Borrowings and Capitalisation

Type of Borrowing	Description	Borrowing Cost Eligible for Capitalisation
Specific Borrowings (SB)	These are Borrowings specifically taken for qualifying assets.	Actual Borrowing Cost during construction period Less: Income on Temporary Investments of idle funds of these Borrowings.
General Borrowings (GB)	All Borrowings that are not specific are general Borrowings.	Calculated as follows (Capitalisation Rate method is used as the Qualifying Asset is funded from a pool of general Borrowings):
		Step 1: Calculate Capitalisation Rate (CR) / Weighted Average Cost of Capital (WACC) / Weighted Average Capitalisation Rate (WACR): Total interest (weighted average) divided by total borrowings (weighted average) $\times 100$.
		Step 2: Calculate Borrowing Cost to be Capitalised: Expenditure amount $\times$ Capitalisation rate $\times$ (Number of months that expenditure was outstanding $\div 12$ months).

7. Period of Capitalisation

A. Commencement (Start)	B. Suspension (Halt)	C. Cessation (Stop)
Commencement of capitalisation begins when All three conditions are satisfied:	Capitalisation should be suspended during an extended period if active development is NOT taking place.	Cease capitalisation when Substantially all the activities necessary to prepare the Qualifying Asset (QA) are complete .
1. Expenditure on QA has been incurred.	Note: Capitalisation is NOT suspended if temporary delay is a necessary part of construction (e.g., High tide / letting a bridge dry as a normal part of the process).	If minor modifications such as decoration are pending, it will still indicate that substantially all the activities are complete.
2. Activities that are necessary have been started (Such activities not only include physical work, but also include technical work, registration work, site preparation planning, etc.).		When construction of QA is completed in parts, cease capitalisation of each part which is completed, provided such part can be used separately (e.g., Construction of a multi-tower building, cease capitalisation on Tower A and B if they are ready and can be used, even if C and D are not).
3. Borrowing Cost is incurred.		
<i>Example:</i> If Expenditure incurred on 01/04/X1, Borrowing Cost incurred on 01/05/X1, Registration work begins on 01/06/X1, Physical work on 01/07/X1. The Capitalisation of Interest starts on 01/06/X1 (as all conditions are met).	<i>Example:</i> If construction starts 01/04/X1 and a strike occurs from 01/11/X1 to 30/11/X1 (1 month), then Interest is charged to the Profit and Loss Account for 1 month (suspended), and Interest is Capitalised for the remaining months (23 months, assuming a 24-month construction period ending 31/3/X3).	

8. Capitalisation of Exchange Loss on Foreign Currency Loan for Qualifying Asset

- **Maximum Exchange Loss that can be capitalised** is the Difference between the Interest that would have been incurred in India and the Interest on the Foreign Loan.
 - $\text{Maximum Exchange Loss Capitalised} = (\text{Interest if loan was taken in Indian currency}) - (\text{Interest on foreign loan})$
- **Total Capitalised Cost** = Interest on foreign loan + Exchange loss capitalised.
- The balance of Exchange Loss is transferred to the Profit and Loss Account.
- **Note:** If there is an **exchange gain**, the above concept is **not applicable**. The Exchange Gain is **Directly transferred to the Profit and Loss Account**.

9. General Notes/Special Points (from Illustrations)

- If expenditure incurred is, suppose, 100 lakhs, but the loan is only 70 lakhs, then interest will be capitalised on the amount of Borrowing, i.e., 70 lakhs.
- If the question specifically says 6 months/10 months is **not** substantial, then it won't be a Qualifying Asset.
- If in a question, planned expenditure and actual expenditure both are given, then calculate Borrowing Cost as per **actual expenditure**.
- If in any month there are **surplus funds** and there is no overdraft, that means a loan has not been taken; therefore, **ignore Interest** for that month/period.
- If Interest is calculated on a monthly basis, then **compounding will be applicable** (i.e., Interest on Interest).
- Date of expenditure in the case of **Specific Borrowing is NOT relevant** for calculating the Borrowing Cost to be capitalised; capitalize full Interest on specific Borrowing during the capitalisation period.
- If a loan is used for multiple purposes (Qualifying Asset and Non-Qualifying Assets), the total Interest incurred is allocated to the Qualifying Asset based on the proportion of the amount utilized for the Qualifying Asset to the total loan amount.

AS 17 - Segment Reporting

1. Types of Segments

A segment can be divided into 2 types:

1. **Business Segment**
2. **Geographical Segment**

2. Business Segment

- It is a distinguishable component that is providing an individual product or service that is subject to risks and returns that are different from other Business Segments.

Factors to be considered:

Factor	Explanation
i) Nature of products or services	
ii) Nature of production process	
iii) Types or class of customers	
iv) Methods of distribution	If they are different
v) Nature of regulatory environment	Segment

3. Geographical Segment

- It is a distinguishable component that is engaged in providing products or services within a particular economic environment that is subject to risks and returns that are different from other economic environments.

Factors to be considered:

1. Similarity of economic and political conditions
 2. Relationships between operations in different geographical areas
 3. Proximity of operations
 4. Special risks associated with operations in a particular area.
- A geographical segment may be a single country, a group of two or more countries, or a region within a country.

4. Identifying Reportable Segments (Quantitative Thresholds)

Step 1: Apply 10% (Materiality Test) (Any 1 test is to be met)

A. Revenue Test:

- Revenue (External + Internal) of the segment is 10% or more of Total Revenue of All Segments.

B. Profit/Loss Test:

- If segment profit or loss is 10% or more of:
 - Combined profit of all segments **or**
 - Combined loss of all segments
 - whichever is greater in absolute Amount.

C. Asset Test:

- Segment Assets are 10% or more of the total assets of all segments.

Step 2: 75% External Revenue Criteria (To be done after above Test)

- Out of total External Revenue, at least 75% of External Revenue should be under reportable segments.
- If not, then additional segments should be identified as reportable, even if they do not meet the 10% threshold, until at least 75% of External Revenue is included in reportable segments.

5. Important Points

1. **If a segment was identified as reportable in the previous year**, then in the Current year, it will have to be reported even if the 10% criteria is not met.
 - **Hint:** Check the 10% Test every year. And whenever you meet it, by default you will become reportable for two years (current year and Next Year).
2. **Management at its discretion** may report more segments as reportable even if they are not meeting the thresholds.
3. **Check 10% criteria every year.**

6. Important Definitions

A. Segment Revenue

It includes:

- Directly attributable Revenue
- Revenue allocated to the segment on a reasonable basis
- Revenue from transactions with other segment.

Does Not include:

- Extra-ordinary items as per AS 5
- Interest / dividend income (unless the segment's primary activity is of a financial nature)
- Gains on sale of Investment (unless the segment's primary activity is of a financial nature)

B. Segment Expense

It includes:

- Directly attributable Expense
- Expense allocated to the segment on a reasonable basis
- Expense from transactions with other segment.

Does Not include:

- Extra-ordinary items as per AS 5
- Interest expense (unless the segment's primary activity is of a financial nature)
- Loss on sale of investment (unless the segment's primary activity is of a financial nature)
- Income tax Expense.
- General Administration expense, Head office Expenses, other expense incurred for the company as a whole.

C. Segment Result (Segment Profit / Loss)

- Segment Revenue less Segment Expense.

D. Segment Assets

It includes:

- Directly attributable assets

- Assets that can be allocated on a reasonable basis.

Do Not include:

- Loans, investments (unless the segment's primary activity is of a financial nature)
- Income Tax Asset (Deferred Tax Asset) As 22.

Note:

- Assets used for general purpose by Head office.
- Assets are determined after deducting related allowances, provisions.

E. Segment Liabilities

It includes:

- Directly attributable liabilities
- Liabilities that can be allocated on a reasonable basis.

Does not include:

- Loans, Borrowings, (unless the segment's primary activity is of a financial nature)
- Income tax liabilities (e.g. Deferred tax liabilities) As 22

7. Special Case (AS 16)

- In case interest is included as a part of the cost of inventories as per AS 16 (Borrowing cost) and those inventories are a part of segment assets, then such interest should be considered as a segment expense.

8. Primary & Secondary Segments

- **Business Segments**
- **Geographical Segments**
- If risks and returns are affected by differences in products or services, then **Business Segment** would be the primary segment.
- But if risks and returns are affected by the fact that it operates in different geographical locations, then the primary segment would be the **Geographical Segment**.

Note:

- Segment information is given in primary reporting format and secondary reporting format.
 - If the Business segment is identified to be primary - Then primary format will be adopted by Business Segments and secondary format will be adopted by Geographical Segments.
-

AS 18 - Related Party Disclosures

1. Related Party Relationships

Accounting Standard 18 deals with the following types of related party relationships:

A. Enterprises that directly or indirectly control, or are controlled by, or are under common control with the reporting enterprise (This includes holding companies, subsidiaries, and fellow subsidiaries). * **Control (as per Accounting Standard 21)**: More than 50% ownership. * *Example: If Ak Limited is the Parent (75% control) of B B Limited (Subsidiary) and B B Limited is the Subsidiary of S K Limited, then B B Limited and S K Limited are related fellow subsidiaries.*

B. Associates and joint venture of the reporting enterprise. * **Significant Influence (as per Accounting Standard 23)**: 20% to 50% ownership. * *Example: If Ak Limited has 35% control over X Limited (Associate), Ak Limited and X Limited are related.*

C. Individuals having control or significant influence over the enterprise and relatives of such individual. * *Example: If Shubham has 70% control over X Y Z Limited, Shubham and his relatives are related to X Y Z Limited.* * **Relatives**: Spouse, Son, daughter, brother, sister, father, and mother.

D. Key managerial personnel (KMP) of the enterprise and relatives of such KMP. * *Example: If Amit is a KMP in Relative Limited, Amit and his relatives are related to Relative Limited.* * **Key Managerial Personnel (KMP)**: Managing director, whole-time Director, Manager, or any other appointed person. * KMP are those persons who have the authority and are fully responsible for planning, directing, and controlling the activities. * **Note**: Non-executive director is not considered as KMP.

E. If one enterprise is controlled by a person, and that same person is a KMP in another enterprise, then those two enterprises are also related. * *Example: If Shubham has 70% control over Reliance Limited and Shubham is KMP in Infosys Limited, then Reliance Limited and Infosys Limited are related.*

2. Who are NOT Deemed to be Related Parties (Exclusions)

A. Two companies are NOT related simply because they have a KMP in common. * *Example: If Shubham is KMP in both P C Limited and Infosys Limited, then P C Limited and Infosys Limited are NOT related.*

B. Fellow associates, co-associates are NOT treated as related parties. * *Hint: 2 A's (Alpha) are never related.*

C. A single customer, supplier, franchiser, distributor, or general agent with whom an enterprise transacts a significant volume of business will NOT be related parties.

D. The parties listed below are also NOT related in the course of their normal dealings with the enterprise: * Providers of Finance * Trade Unions * Public utilities * Government departments

3. Disclosure Requirements

- **Relationship of Parent - Subsidiary:**
 - Disclose even if there is **no transaction** with the related party.
- **All other relations:**
 - Disclose **only if there is a transaction** with the related party during the year.

In respect of disclosure requirements, the enterprise should disclose the following information:

1. Name of related party
2. Relationship

3. Nature of transaction
4. Volume of transaction
5. Amount outstanding
6. Amount written off as Bad debts
7. Any other element.

Notes on Disclosure:

1. Remuneration paid to KMP should be considered as a related party transaction requiring disclosures.
2. Remuneration paid to non-executive director should **not** be considered as a related party transaction.

4. Exemption from Related Party Disclosures in Certain Situations

A. Related party disclosure requirements do not apply where providing such disclosure would be in conflict of **confidentiality** as required by any statute or any regulator or similar competent authority. * *Example: Banks maintain confidentiality of their customers. * (Note: Any other commercial contract between the parties to maintain confidentiality won't be considered for this purpose.)*

B. State controlled Enterprises are **not** required to follow disclosure requirements. * *Example: If Maharashtra Government controls Indian Oil and BSNL, Indian Oil and BSNL are related but exempt from disclosure requirement.*

AS 19 - Leases

1. Definition of Lease

- A lease is an agreement whereby the **lessor** (legal owner) conveys to the **lessee** the right to use an asset for a period of time in return for a payment or series of payment (**Lease Rentals**).

2. Scope

This standard applies to all leases other than:

- Lease agreements to explore or use natural resources such as oil, gas, metals, minerals, etc.
- Licensing agreements for items such as motion picture films, video recordings, plays, manuscripts, patents, and copyright.
- Lease agreement to use Lands.

3. Important Definitions

- Lease Term:**
 - It includes Non-cancellable period **plus** Renewal period (if reasonably certain to exercise the option).
- Lease Payments / Lease Rentals / Lease Charges (Minimum Lease Payments):**

Lessor	Lessee
1. Fixed Lease Rentals	1. Fixed Lease Rentals
2. Guaranteed Residual Value (GRV) given by lessee	2. Guaranteed Residual Value (GRV) given by lessee (more important for lessee)
3. Guaranteed Residual Value (GRV) given by independent third party	
4. Renewal option/Purchase option payment (If reasonably certain to exercise)	3. Renewal option / Purchase option payment (If reasonably certain to exercise)

4. Types of Lease

- Operating Lease:** More like a normal rental agreement. It **does not** transfer the risk and reward of the asset.
- Finance Lease:** More like a loan agreement. It **transfers** the risk and reward of the asset.

5. Indicators of Finance Lease

If **Any one** of the following five conditions is met, then it is a Finance Lease:

- Ownership:** If the lease transfers ownership of the asset to the lessee at the end of the lease term.
- Purchase Option:** If the lessee has an option to purchase the asset at a price which is expected to be lower than Fair Value (Bargain Purchase Option) **and** it is reasonably certain that the option will be

exercised.

3. **Lease Term (75% Rule):** If the lease term is for the **major part** of the economic life of the asset. (The notes imply that 75% or more is considered a major part).
 4. **Present Value (PV) of Minimum Lease Payments (MLP) (90% Rule):** At the inception of the lease, if the present value of MLP **substantially covers** the fair value of the asset, then it is a Finance Lease. (The notes imply 90% or more is substantial coverage).
 5. **Specialised Nature:** The leased asset is of a **specialised nature** such that only the lessee can use it without major modifications being made.
- *Note:* If none of the above five indicators are met, then it is an Operating Lease.
-

6. Accounting for Finance Lease

A. Lessee Books

- **Initial Measurement (Day 1):**
 - Asset Account Debit
 - To Lease Liability Account
 - The Asset and Lease Liability are recorded at the **Lower of: (Present Value of Minimum Lease Payments OR Fair Value of Asset)**. (This amount is also known as the Lease Liability).
- **Subsequent Entries (Year End):**
 - Interest Expense Account Debit
 - To Lease Liability Account (For interest accrued on opening lease liability balance)
 - Lease Liability Account Debit
 - To Cash in Bank Account (For payment of lease rent)
 - Depreciation Account Debit
 - To Property, Plant, and Equipment Account
 - Depreciation is calculated over the **Lease Term or Useful Life**, whichever is **lower**.
 - **Extra Entry (Transfer to Profit and Loss Account):**
 - Profit and Loss Account Debit
 - To Depreciation Account
 - To Interest Expense Account

B. Lessor Books

- **Initial Measurement (Day 1):**
 - Lease Receivable Account Debit
 - To Property, Plant, and Equipment Account
 - The amount recorded is the **Net Investment**.
- **Subsequent Entries (Year End):**
 - **No Depreciation** (as the asset has moved out of the lessor's books).
 - Lease Receivable Account Debit
 - To Interest Income Account (For interest earned on opening lease receivable balance)
 - Cash in Bank Account Debit
 - To Lease Receivable Account (For receipt of lease rent)
 - **Transfer to Profit and Loss Account:**
 - Interest Income Account Debit
 - To Profit and Loss Account
- **Important Terms for Lessor (Finance Lease):**
 1. **Gross Investment (without Present Value):**
 - Minimum Lease Payments **plus** Unguaranteed Residual Value (UGRV).
 - Residual Value = Guaranteed Residual Value (GRV) + Unguaranteed Residual Value (UGRV).

2. **Net Investment:**
 - Present Value of Minimum Lease Payments **plus** Present Value of Unguaranteed Residual Value (UGRV).
 - Net Investment is the Present Value of Gross Investment.
 3. **Unearned Finance Income:**
 - Gross Investment **minus** Net Investment (Represents upcoming years' interest).
- **Special Case 1: Annual Lease Rent is Not given (Lessor Books)**
 - The Fair Value/Cost of the Asset is assumed to be equal to the Present Value of Minimum Lease Payments **plus** Present Value of Unguaranteed Residual Value.
 - The Annual Lease Rent (if equal) is calculated as:
$$\text{Annual Lease Rent} = \frac{\text{Present Value of MLP}}{\text{Annuity factor}}$$
 - **Special Case 2: Interest Rate is Missing**
 - In this case, the **Internal Rate of Return (IRR)** must be found. IRR is the Interest Rate Implicit in the Lease.
 - IRR is the rate at which the Present Value of Future Lease Rentals and Present Value of Unguaranteed Residual Value equals the Fair Value/Cost of the Asset on Day 1.
-

7. Accounting for Operating Lease

A. Lessee Books (Normal Rental Agreement)

- **Day 1:** No entry.
- **Year End:**
 - Lease Rent Expense (Profit and Loss) Account Debit
 - Lease Equalisation (Current Asset/Liability in Balance Sheet) Account Debit/Credit (Balancing Figure)
 - To Cash in Bank Account
 - AS 19 suggests to book lease rent on a **Straight Line Method (SLM) Basis** unless any other basis is more appropriate.
 - **No Depreciation** is charged by the lessee.

B. Lessor Books (Normal Rental Agreement)

- **Day 1:** No entry.
 - **Year End:**
 - Cash in Bank Account Debit
 - Lease Equalisation (Current Asset/Liability in Balance Sheet) Account Debit/Credit (Balancing Figure)
 - To Lease Rent Income (Profit and Loss) Account
 - AS 19 suggests to book lease rent on a **Straight Line Method (SLM) Basis** unless any other basis is more appropriate.
 - Depreciation Account Debit (Profit and Loss)
 - To Property, Plant, and Equipment Account (Depreciation is always charged by the lessor over the useful life of the asset).
 - **Special Case in Operating Lease (Lease Rent in Proportion of Output)**
 - When the lease rent is expected to be derived in the ratio of output from the leased asset, the total lease rent for the lease term is allocated to each year in the **ratio of output** for that year. This calculated amount is the Lease Rent Expense/Income to be booked in the Profit and Loss Account each year.
-

8. Sale and Lease Back

- This involves a Sale transaction followed by a Lease Back transaction (either Operating or Finance Lease).
- The treatment of Profit or Loss on the sale transaction is discussed in AS 19.

A. Sale Done & Lease Back results in Finance Lease

- Profit/Loss on Sale is to be **amortised over the lease term** in the proportion of Depreciation.

B. Sale Done & Lease Back results in Operating Lease

- **Case 1: Sale Price (SP) = Fair Value (FV)**
 - Profit/Loss on sale (Calculated as Sale Price minus Book Value/Written Down Value) can be **recognised immediately**.
- **Case 2: Sale Price (SP) is Less than Fair Value (FV) (SP < FV)**
 - Profit/Loss on sale (Calculated as Sale Price minus Book Value/Written Down Value) can be **recognised immediately**.
 - **However**, if there is a loss and such loss is compensated by future lease payments at a **Below Market Rate**, then such loss should be **deferred and booked in proportion of future lease payments** (amortised over the lease term).
- **Case 3: Sale Price (SP) is More than Fair Value (FV) (SP > FV) (Cheating)**
 - Profit/Loss **up to Fair Value** (Calculated as Fair Value minus Book Value/Written Down Value) can be **booked immediately**.
 - The **Excess selling Price over Fair Value** (Selling Price minus Fair Value) should be **deferred and booked** over the period for which the asset is expected to be used (amortised over the lease term).

9. Other Miscellaneous Points

- **Contingent Rent:**
 - If lease rent is based on future sales, future profits, etc., such rentals will be **booked in the Profit and Loss Account as and when received / paid**.
- **Initial Direct Cost:**
 - Cost which is incurred for entering into the lease. Generally, they are incurred by the lessor in most cases.
 - **Accounting Treatment if incurred by lessor:**
 - **Finance Lease:** Capitalise to the cost of the Asset.
 - **Operating Lease / All other cases:** Generally transferred to Profit and Loss Account.
 - **Accounting Treatment if incurred by lessee:**
 - Generally transferred to Profit and Loss Account.
- **Lease Rent at the Beginning of the Year:**
 - Normally, lease rentals are paid at the end of the year.
 - If rentals are paid at the **beginning of the year**, the Discount Factor for Present Value calculation will be adjusted accordingly (e.g., Year 1 beginning rent uses a discount factor of 1).

AS 20 - Earnings per Share (EPS)

I. Basic Earnings per Share

1. Formula

Basic EPS = Earnings available for equity shareholders divided by weighted average number of equity shares.

Note A: Earnings Available for Equity Share Holders (EAFESH)

Particulars	Calculation
Revenue (Total Income)	XXX
Less: Total expenses (Interest on Debentures)	(X)
Profit Before Tax (PBT)	XX
Less: Tax	(XX)
Profit After Tax (PAT)	XX
Less: Preference Dividend	
Cumulative Preference Share Dividend: Deduct whether or not it is declared. (Tax benefit is NOT available).	(XX)
Non-cumulative Preference Share Dividend: Deduct only when it is declared. (Tax benefit is NOT available).	(XXX)
Earnings Available for Equity Share Holders (EAFESH)	XXX

Note: Do not deduct equity dividend.

Note on Interest paid on Debentures: Tax Benefit is available on interest paid on debentures.

Note on Cumulative Preference Shares: If the dividend is 10% on cumulative preference shares, the liability to pay the dividend in arrears remains, so it is deducted.

Note on Non-Cumulative Preference Shares: If the dividend is 10% on non-cumulative preference shares, the dividend is deducted only if declared, because there is no obligation to pay the dividend if not declared.

Note B: Weighted Average No. of equity shares (WANES)

General Rule: The number of shares is weighted by the time outstanding.

Example: Year end is December.

Opening balance at the beginning of the year = 1800 shares
600 new shares issued on 31 May X1
300 shares bought back on 1 November X1

$WANES = (1800 \times 12 \div 12)$

$(600 \times 7 \text{ months} \div 12 \text{ months})$

$(-300 \times 2 \text{ months} \div 12 \text{ months}) = 2100 \text{ shares.}$

2. Partly Paid-up Shares

- Partly paid-up shares are treated as a **fraction of fully paid-up equivalent shares**.
- The conversion is based on the ratio of the paid-up value to the face value.
- *Formula to calculate equivalent fully paid-up shares:*

$$\text{Number of shares} \times (\text{Paid-up value} \div \text{Face value}).$$

3. Shares with Different Nominal Values

- When an enterprise has equity shares with different nominal values, the number of equity shares is calculated by **converting all such equity shares into equivalent number of shares of the same nominal value**.
- *Formula for conversion (Similar to partly paid-up):*

$$\text{Number of shares} \times (\text{Face value of shares} \div \text{Face value of target equivalent shares}).$$

4. Bonus Shares / Share Split / Share Consolidation

- Bonus shares are issued to existing shareholders outstanding for **no additional consideration**.
- The number of shares is increased without any increase in cash resources.
- Therefore, in the case of a Bonus, the **date of issue of Bonus shares is irrelevant**.
- Bonus shares are assumed to be outstanding from the **earliest reporting period** (i.e., we take the effect of Bonus in the current year and the previous year both).
- Just like Bonus shares, the **same treatment is also applicable to share split or share consolidation**.
- When Bonus shares are issued, three EPS figures must be reported (for 2 years):
 1. Previous Year (P.Y.) Original
 2. Previous Year (P.Y.) Restated (including Bonus effect)
 3. Current Year (C.Y.) Original (or sometimes C.Y. Restated is also mentioned in notes)

Formula for Restated EPS of Previous Year (P.Y.):

Basic EPS of previous year (restated) = EAFESH divided by WANES (including bonus)

5. Time of Inclusion in Calculation of Weighted Average No. of Shares

When shares are issued	When to include in denominator
1. Shares issued for cash (e.g., New shares issue)	When cash is receivable
2. Issued for conversion of debentures	Date of conversion
3. Shares given against interest or principal repayment of loan	Date when interest or principal ceases to accrue
4. Shares given for settlement of a liability	Date of settlement
5. Shares given for acquisition of asset	Date when acquired asset is recognised
6. Shares to be issued for services rendered	Date when services are rendered

6. Right Shares

- Existing shareholders are given shares at a lower price.
- Right shares are generally issued at **less than fair value**. It means that there is a **Bonus element** in right shares also.

Steps to solve Right Shares problems:

- Step 1: Calculate Theoretical Ex-Right Price (TERP)
$$\text{TERP} = (\text{Fair value of shares outstanding before right issue} + \text{Amount received through right shares}) \div \text{Total number of shares after right issue}$$

Step 2: Split the right issue shares into Bonus element and Shares issued for consideration

Bonus Shares (no time weight): Bonus shares = Total shares issued in right issue – Shares issued for consideration

Shares issued for consideration (time weight applies): Shares issued for consideration = Funds raised through right issue ÷ Theoretical Ex-Right Price

Step 3: Calculate EPS If 2 years are given then 3 EPS will be calculated: • Current Year Original • Previous Year Original • Previous Year Restated

Formula for Adjustment Factor (ICAI Method) Adjustment factor = Cum-Right Price ÷ Ex-Right Price

This adjustment factor is applied to the weighted average number of equity shares (WANES) before the right issue date while computing current year WANES.

II. Diluted Earnings per Share

1. Potential Equity Shares (PES)

- Potential Equity Shares are instruments which entitles the holder the right to acquire equity shares in the future. (Future mein equity share banega).
- **Examples:** Convertible Debentures, Convertible Preference Shares, Employee Stock Option Plans (ESOPs), Share Warrants.
- **Share Warrants:** It is an instrument that gives the holder the right to purchase the shares of a company at a pre-determined lower price which is set on Day 1.
-

2. Formula for Diluted EPS

Formula for Diluted EPS

Diluted EPS = (EAFESH + Effect of Potential Equity Shares on numerator) ÷ (WANES + Effect of Potential Equity Shares on denominator)

Note on Reporting:

- If Diluted EPS comes out to be **less than Basic EPS**, then it is **Dilutive** (Reported).
- If Diluted EPS comes out to be **more than Basic EPS**, then it is **Anti-Dilutive** (Not Reported).

Effect of PES on Numerator (Savings in Interest or Dividend, net of tax):

- **For Convertible Debentures:** Interest saved on debentures (multiplied by one minus tax rate).
- **For Convertible Preference Shares:** Dividend saved on preference shares (Preference dividend has no tax impact, so no tax adjustment is needed).
- **For Share Warrants / Options:** Effect on numerator is **NIL**. *Effect of PES on Denominator (Increase in Shares):*
- **For Convertible Debentures / Preference Shares:** The number of shares resulting from conversion (time weighted if issued during the year).
- **For Share Warrants / Options:** The number of shares issued at no consideration (free component) is considered as the effect on the denominator. Formula for Free Component Shares (ESOP Dilution)

Free component shares = Total shares under option – (Total shares under option × Exercise Price ÷ Market Price)

3. EPS in Case of Negative Earnings

Basic EPS (EAFESH)	Potential EPS (Incremental EPS)	Conclusion
Positive (e.g., 10)	Positive (e.g., 7)	Dilutive (10 → 7)
Negative (e.g., -10)	Positive (e.g., 3)	Anti-Dilutive (-10 → -7)
Negative (e.g., -10)	Negative (e.g., -2)	Dilutive (-10 → -12)

Rule: If the basic EPS is negative (a loss), PES are considered anti-dilutive if they reduce the loss (move towards zero or a positive number), and dilutive if they increase the loss (move further away from zero).

4. EPS in Case of Continued and Discontinued Operations

- Where profit/loss for continued and discontinued operations both are given, the decision of whether Potential Equity Shares (PES) are dilutive or not would be calculated **only on profit/loss from Continuing operations**.
- However, both Basic EPS and Diluted EPS must be reported for both continuing and combined (continuing + discontinued) operations, even if the combined EPS is anti-dilutive.

5. Multiple Potential Equity Shares (Kattappa Logic)

- When there are more than one class of Potential Equity Shares (PES), we will have to evaluate each class separately.

Steps for Calculation of Diluted EPS with Multiple PES:

1. Step 1: Calculate Incremental EPS for each PES

Incremental EPS = Incremental effect on numerator ÷ Incremental effect on denominator 2. **Step 2: Rank the PES from lowest to highest Incremental EPS.** 3. **Step 3: Conclusion (Dilutive/Anti-dilutive) - Apply the "Kattappa Rule".** * Start with Basic EPS. * Include the PES with the **lowest** Incremental EPS (Rank I) and calculate the new EPS. * If the new EPS is **less than the previous EPS** (i.e., dilutive), keep it and proceed to the next rank. * If the new EPS is **more than the previous EPS** (i.e., anti-dilutive), **stop (plato)** and do not consider this PES or any subsequent PES in the final Diluted EPS calculation.

Final Reported Diluted EPS: Consider only the PES that are found to be dilutive in the ranking process.

AS 21 - Consolidated Financial Statements

Consolidation (Overview of Related Standards)

Standard	Topic	Relationship
AS 21	Consolidated Financial Statements (CFS)	with Subsidiary
AS 23	Consolidated Financial Statements (CFS)	with Associate
AS 27	Consolidated Financial Statements (CFS)	Joint Ventures

I. Important Definitions

1. Parent Company (Holding Company):

- It is an entity which has **CONTROL** over one or more subsidiaries.

2. Control:

- It exists when the Parent has either:
 - **More than 50% voting power** (e.g., by acquiring more than 50% equity shares).
 - **OR** Power to control the **composition of the Board of Directors (BOD)**.
- *Example: Parent/Holding Company (AK Ltd acquired 75% equity Shares of Reliance Ltd) → Subsidiary. Example: Soft Bank → WeWork (agreement that director of WeWork will be appointed by Soft Bank).*

3. Minority Interest (MI):

- Net Assets / Percentage of ownership of a subsidiary **not owned** by parent.
- *Example: AK Ltd 75% → Reliance Ltd. AK 75% is Parent. Remaining 25% of Reliance (Ltd) is with Minority Interest (e.g., Mali 5%, Aadit 5%, Unnati 10%, Ram 5%).*

II. Financial Statements to be Prepared by Parent

1. Separate Financial Statements (SFS):

- Only Assets / Liabilities / Income / Expenses of Parent.
- For stake acquired in Subsidiary, the Journal Entry is: Investment in Equity Shares TO Cash In Bank (CIB).

2. Consolidated Financial Statements (CFS):

- Combine Financial Statements of Parent & Subsidiary using line by line consolidation (full Consolidation) method.

Consolidated Financial Statements (Components):

- Consolidated Balance Sheet (Consolidated B/S)
- Consolidated Profit and Loss (Consolidated P/L)
- Consolidated Cash Flow (Not in syllabus)
- Consolidated Notes to Accounts (Cons. Notes to A/c's)

III. Consolidated Balance Sheet - Procedure for Consolidation

- **Method:** Line by line consolidation / full consolidation.
- In CFS, Parent records **100% of Net Assets** of Subsidiary (even if stake is 75%).
- *Example: Investment in Reliance (Subsidiary) 75% eliminated → Net Assets in Reliance (100%) [Refer Page 3 Example]*

Procedure for consolidation (in CFS):

1. **De-Recognition of Investment** made by parent Co.
2. **Recognition of 100% Value of Net Assets** of Subsidiary.
3. **Recognition of Minority Interest** as per proportionate share in Net Assets.
4. **Recognition of Goodwill (GW) / Capital Reserve (CR)** (Cost of Control - COC) [Just like Amalgamation].
5. **Elimination of Intra Group Balances & Unrealised Profit.**

Consolidation Journal Entry (Conceptual Format):

- Assets of Subsidiary Account Debit (100%)
- Goodwill (Balancing Figure) Debit
- To Investment in Equity shares of Sub
- To Liabilities of Subsidiary Account (100%)
- To Minority Interest Account
- To Capital Reserve Account (Balancing Figure)

IV. Detailed Working Notes and Calculations

1. Analysis of Profit (AOP) / Net Assets of Subsidiary

Category	Definition	Allocation
Capital Profit (Pre-Acquisition)	Profit/Reserves accumulated up to the Date of Acquisition (DOA).	To Cost of Control (GW/CR) and Minority Interest (MI).
Revenue Profit (Post-Acquisition)	Profit/Reserves earned after the Date of Acquisition.	To Consolidated Reserves (Parent's Share) and Minority Interest (MI).

- **Net Assets of Subsidiary on DOA** can be calculated as: Assets on DOA of Subs - Liabilities on DOA of Sub OR Equity share Capital of Sub (on DOA) + Reserves of Sub (on DOA).

2. Minority Interest (MI) Calculation (Working Note 3)

- MI is calculated as the **Prop of Net Assets (MI Share)** = (Equity Share Capital + Pre-Acquisition Reserves + Post-Acquisition Reserves) × MI Percentage.
- **Components:** Calculation of Minority Interest (MI) Share

Equity Share Capital Share of MI × MI Percentage

Pre-Acquisition Share of MI (Capital Profit) × MI Percentage

Post-Acquisition Share of MI (Revenue Profit) × MI Percentage

Less: Unrealised Profit (URP) Share of MI (only if the subsidiary is the selling company – Upstream transaction) × MI Percentage

- **Note:** Minority Interest is shown under the Equity & Liabilities section of the Consolidated Balance Sheet.

3. Cost of Control (COC) (Goodwill / Capital Reserve) Calculation (Working Note 4)

- **Formula:** Calculation of Goodwill and Capital Reserve

Cost of Investment (Parent's Share)

Less: Net Assets of Subsidiary at Date of Acquisition (Parent's Share × (Equity Share Capital + Pre-Acquisition Reserves))

Goodwill (GW): If Cost of Investment > Net Assets Share (positive), then Goodwill is recorded as Non-Current Asset (NCA)

Capital Reserve (CR): If Cost of Investment < Net Assets Share (negative), then Capital Reserve is recorded in Reserves (RES)

4. Consolidated Reserves and Surplus Calculation (Working Note 5)

- **Formula:** Calculation of Parent's Reserves and Surplus

Parent's Reserves and Surplus (from SFS)

Add: Post-Acquisition Share of Subsidiary's Profit (Revenue Profit) × Parent's Percentage

Add: Capital Reserve from Cost of Control (if any)

Less: Unrealised Profit (URP) Share of Parent (Downstream or Upstream transaction) × Parent's Percentage

Less: Rectification for Pre-Acquisition Dividend incorrectly credited to Parent's Reserves / Profit and Loss Account (Parent's Share)

5. Time Adjustment (When Date of Acquisition is in the middle of the year)

- **Assumption:** Profits have accrued **evenly throughout the year** (unless otherwise stated).
- The profit for the period (Opening Reserves to Closing Reserves difference) is split into Pre-Acquisition and Post-Acquisition based on the number of months.

6. Abnormal Gain / Loss Adjustment (When Date of Acquisition is in the middle of the year)

- **Logic:** Time Adjustment is performed on **normal profit** (which is assumed to be evenly accrued). When there is abnormal gain / loss, time adjustment cannot be performed directly.
- **Steps:**
 1. Reverse the effect of Abnormal Gain / Loss from **Post-Acquisition profit (Always)**.
 2. Then perform **Time Adjustment** on the remaining normal profit.
 3. Then take effect of Abnormal Gain / Loss in **Pre/Post** depending on the **date of gain/loss**.

7. Inter Company Balances

- Inter Company Balances between Parent & Subsidiary like Trade receivables & Trade payables, Bills receivable & Bills payables, loan given & loan taken, etc., will get **eliminated in CFS**.

8. Unrealised Profit (Stock Reserve)

- Profit element on unsold stock (Inventory) between Parent and Subsidiary will be **eliminated in CFS** (Provided the goods are outstanding at year end).
- **Downstream Transaction (Parent sold goods to Subsidiary):** Profit was earned by Parent.
 - **Journal Entry in CFS:**
Consolidated Reserves Account Debit (XX)
To Inventory Account (XX)
- **Upstream Transaction (Subsidiary sold goods to Parent):** Profit was earned by Subsidiary. Subsidiary's profit was recorded by Parent & Minority Interest.
 - **Journal Entry in CFS:**
Consolidated Reserves Account Debit (Parent's Share) (XX)
Minority Interest Account Debit (MI's Share) (XX)
To Inventory Account (XXX)

9. Revaluation Gain / Loss on Net Assets (Fair Value Adjustments)

- We need Net Assets of Subsidiary @ **Fair Value on Date of Acquisition (DOA)**.
- **Procedure for AOP:** Take Fair Value of Asset / Liability Adjustment (FV Adj) in **Pre column** after Time Adjustment.
 - *Reason for Pre column:* As fair value adjustments are done on DOA & effects of DOA are taken in Pre column.
- **Depreciation Adjustment:** Excess Depreciation (due to increase in FV of Asset) → Charge in **Post-Acquisition** column. Savings in Depreciation (due to decrease in FV of Asset) → Add in **Post-Acquisition** column.

10. Dividend Paid by Subsidiary to Parent

- **Final Dividend (for previous year, paid in current year):**
 - *CFS Adjustment for Subsidiary (Payer):*
 1. Add Back Dividend to the Profit/Reserve balance.
 2. Perform Time Adjustment.
 3. Deduct the dividend from the **Pre-Acquisition** column (assuming dividend paid in current year was paid for profit which falls in pre-acquisition period).
- **Interim Dividend (paid out of current year profits):**
 - *CFS Adjustment for Subsidiary (Payer):*
 1. Add Back Dividend in the Post column.
 2. Perform Time Adjustment.
 3. Deduct from **Pre OR Post** (Depending on months falling in Pre/Post for dividend).
- **Adjustment for Parent (Receiver):**
 - **Pre-Acquisition Dividend:** Treated as **Recovery of Investment** (Reduces the Cost of Investment).
 - *Rectification if wrongly credited to Income/Reserves:* Reserves or Profit and Loss Account Debit To Investment.
 - **Post-Acquisition Dividend:** Transferred to **Income** (Profit and Loss Account).

11. Time of Incorporation (for new Subsidiary)

- If the subsidiary is newly incorporated (date of incorporation is the DOA):
 - **Reserves of Subsidiary (Anushka)** on the date of incorporation must have been **zero**.
 - The entire profit earned from the date of incorporation to the year end is treated as **Post-Acquisition Profit**.

AS 22 - Accounting for Taxes on Income

Summary of Tax Expense in Profit and Loss (P/L) Account (Draft Format)

Particulars	Amount
Current Tax	XXX
Deferred Tax	(XX)
Tax Expense	XXX

Formula for Tax Expense: Formula for Tax Expense

Tax Expense = Current Tax Expense (Profit and Loss) + Deferred Tax Liability – Deferred Tax Asset

1. Definitions

- **Deferred Tax:** It is the tax effect of **timing difference** between Accounting profit and Taxable profit.
 - **Deferred Tax Asset (DTA):**
 - DTA means paid **more tax in current year** but will pay **less tax in future**.
 - It arises when accounting profit is less than taxable profit due to timing differences (Expense in Accounting is recognized earlier than in Tax Books, or Income in Accounting is recognized later than in Tax Books).
 - **Deferred Tax Liability (DTL):**
 - DTL means paid **less tax in current year** but will pay **more tax in future**.
 - It arises when accounting profit is more than taxable profit due to timing differences (Income in Accounting is recognized earlier than in Tax Books, or Expense in Accounting is recognized later than in Tax Books).
 - **Current Tax:** It is the amount of tax determined to be payable in respect of taxable income.
-

2. Timing Difference and Permanent Difference

- **Timing Difference:**
 - These are differences between Accounting income and Taxable income that **originate in one period** and are **capable of reversal** in one or more subsequent periods.
 - *Examples:* Depreciation, preliminary expenditure, expense allowed on cash basis (e.g., Interest paid to NBFCs is allowed only on payment basis in tax, but on accrual basis in accounting).
 - Deferred Tax is created on **all timing differences**.
 - **Permanent Difference:**
 - These are differences between Accounting income and Taxable income that originate in one period and **Do Not Reverse subsequently**.
 - *Examples:* Fines and penalties, donation to political party/trust, etc. These are permanently disallowed in tax.
 - **No Deferred Tax is created on permanent differences.**
-

3. Deferred Tax on Carry Forward Losses and Unabsorbed Depreciation

- Deferred Tax Asset (DTA) Recognition

Carry forward losses result in less tax in future → Create Deferred Tax Asset (DTA)

4. Recognition of Deferred Tax Asset (DTA) and Deferred Tax Liability (DTL)

- **Deferred Tax Liability (DTL):**
 - There are **no pre-conditions** to recognise DTL. DTL is recognized without any conditions.
 - **Deferred Tax Asset (DTA):**
 - **DTA arising due to normal timing differences (any other reason):**
 - DTA are recognised only to the extent there is **reasonable certainty** of their realisation (i.e., sufficient **future expected profit**).
 - **DTA arising due to unabsorbed depreciation or carry forward losses:**
 - DTA should be recognised only when there is **virtual certainty** supported by **convincing evidence** that sufficient future taxable profit will be available against which such DTA can be realised.
 - *Examples of convincing evidence:* Future export orders, projection of future profits made by the enterprise, etc.
-

5. Review of Unrecognized DTA

- At each balance sheet date, the Company should **reassess unrecognized DTA**.
 - If future taxable profit is now **reasonably certain** (or virtually certain, as applicable), then the company can record **previous years' unrecognized DTA**.
-

6. Tax Rates for Current Tax and Deferred Tax

- **For Current Tax:** Use the Tax Rate that is applicable to the **current period**.
 - **For Deferred Tax:** Use the **future tax rate** if announced/proposed by the government. If the future tax rate is not available, then use the current year rate.
 - *Example:* If in the current year 2024-25, the tax rate is 30%, but the government proposed a 35% rate for future years:
 - Current Tax will be calculated @ 30%.
 - Deferred Tax will be calculated @ 35%.
-

7. Implication in Tax Holiday Period

- DTA or DTL in respect of timing differences which **reverse during the tax holiday period** should **not be recognised**.
 - The timing difference which originates first should be considered to **reverse first**.
-

Note on Current Tax Calculation (If Minimum Alternate Tax - MAT is Applicable):

- Current Tax is calculated as **Higher of:**
 - Taxable profit × Tax Rate
 - Book profit × MAT Rate (if applicable)

AS 23 - Accounting for Investments in Associates in Consolidated Financial Statements

1. Definitions

- **Associate:** An associate is an entity in which the investor has **significant influence** and which is neither a subsidiary nor a joint venture of the investor.
- **Significant Influence:** It is the **power to participate** in the financial or operating decisions of the entity.
 - **How Significant Influence can be obtained:**
 1. Voting power (20% to 50%).
 2. Representation on the Board of Directors.

Relationship Summary (Contextual Note):

Investor	Ownership Percentage	Relationship	Applicable Standard
Parent	75%	Subsidiary	AS 21
Investor	30% (20% to 50%)	Associate	AS 23

2. Accounting for Investments in Associates

- **In Separate Financial Statements (SFS):**
 - Investment in Associate is accounted for as per **AS 13 (Accounting for Investments)**.
 - The investment is recorded at **Cost** of Investment less: Pre-Acquisition dividend.
- **In Consolidated Financial Statements (CFS):**
 - Investment in Associate is accounted for using the **Equity Method (AS 23)**.

3. Equity Method (for Consolidated Financial Statements)

- The Equity Method is a valuation method used to calculate the value of Investment in Associate in the Consolidated Financial Statements.

A. Calculation of Goodwill / Capital Reserve (at Date of Acquisition - DOA)

Particulars	Amount
Cost of Investment (Investor's Stake Percentage)	XXX
Less: Pre-Acquisition dividend (If any, related to period before acquisition)	(X)
Adjusted Cost of Investment	XX
Less: Net Assets of Associate (Investor's Stake Percentage)	(XXX)
Goodwill (If Adjusted Cost of Investment $\geq$ Share of Net Assets)	XXX
Capital Reserve (If Adjusted Cost of Investment $<$ Share of Net Assets)	(XXX)

- **Note on Net Assets (NA) of Associate at Date of Acquisition:** Net Assets are calculated as:
Assets @ Fair Value - Liabilities @ Fair Value
OR
Equity Share Capital on DOA + Pre-Acquisition Reserves

B. Presentation of Investment in Associate in Consolidated Balance Sheet (Day 1)

Particulars (CFS Balance Sheet - Extract)	Amount
Investment in Associate	
Share of Net Assets at DOA	XX
(+) Goodwill	XXX
Total Value of Investment (Day 1)	XXX

- *Note:* The Total Value of Investment (Day 1) will be equal to the Adjusted Cost of Investment.

C. Calculation of Value of Investment on Subsequent Dates (e.g., Year End - as per Equity Method)

- The Carrying Amount (Value) of the Investment in Associate is adjusted each year to reflect the investor's share of the associate's post-acquisition profit or loss.

Particulars	Amount
Carrying Amount of Investment (Share of NA + Goodwill/Capital Reserve) at the beginning of the period	XXX
(+) Post Acquisition Share of Profit (Associate Profit × Investor's Stake)	XX
Less: Post Acquisition Dividend (Associate Dividend × Investor's Stake) (Treated as recovery of invested amount)	(X)
Less: Unrealised Profit (Unrealised Profit × Investor's Stake)	(X)
Less: Excess Depreciation due to revaluation of Associate's Assets (Excess Depreciation Amount × Investor's Stake)	(X)
Value of Investment at Year End (as per Equity Method)	XXX

D. Dividend Consideration based on Period:

- **Pre-Acquisition Dividend:** Reduces the Cost of Investment.
- **Post-Acquisition Dividend:** Reduces the Carrying Amount of Investment (Treated as recovery of invested amount).

E. Proposed Dividend:

- Dividend declared after the year-end (Proposed Dividend) will **NOT** be taken into consideration while computing the value of the Investment for the year ended.

F. Potential Equity Shares:

- Potential equity shares (e.g., Convertible Debentures, Convertible Preference Shares) held by the investor **should not be taken into consideration** for determining voting power or significant influence, because voting power is not available today.

G. Carrying Amount (Value) of Investment in Consolidated Financial Statements Cannot be Negative:

- Adjustment of Post Acquisition loss/expense is made only **up to the value of the Investment**.
- If the cumulative post-acquisition losses/expenses exceed the Carrying Amount of Investment, the Investment value is reduced to **NIL**. Any further losses are not adjusted, and the investment will be shown as **NIL** in the Consolidated Balance Sheet.

4. Cases where Equity Method is NOT to be Followed (Discontinuation)

- The investor is **NOT** required to follow the Equity Method (even if significant influence exists) if:

1. The investment is intended to be **temporary**.
2. There are **severe or long-term restrictions** which significantly restrict the transfer of funds to the investor.

- The investor is required to **discontinue** the Equity Method if:
 1. It **ceases to have significant influence** due to the sale of the investment (either wholly or partially).
 2. Before there were no restrictions, but now there are **severe long-term restrictions** which significantly restrict the transfer of funds to the investor.
 - *Note: If the Equity Method is discontinued, the investor will revert to accounting for the investment using AS 13 (Cost or Market Value, whichever is lower).*

AS 24 - Discontinuing Operations

1. Definition of Discontinuing Operation

A component of an entity is considered a discontinuing operation if it satisfies all three conditions:

1. It is a component of an entity that the enterprise has decided to **dispose pursuant to a single plan** (in a single transaction, by demerger, by spin-off, or piecemeal by selling off components of assets and settling liabilities individually, or by terminating through abandonment).
2. It represents a **separate major line of business or geographical area** of operation.
3. It can be **distinguished operationally and for financial reporting purposes**.

2. Activities That May NOT be Considered as Discontinued Operations

The following activities may **NOT** be considered as discontinued operations:

- Gradual phasing out of a product line or class of service.
- Discontinuing several products within an ongoing line of business (e.g., closing only one product and not a line of business).
- Shifting of some production or marketing activities for a particular line of business from one location to another (e.g., production plant shift from Bengal to Gujarat).
- Closing of a facility to achieve productivity improvements or other cost savings (e.g., outsourcing production instead of closing the business line).
- Changing the scope of operation or the manner in which business is conducted is not abandonment or discontinued operation, as although changed, business is still continuing (e.g., offline teaching shifting to online teaching).
- Selling a subsidiary whose activities are **similar to the Parent** is **NOT** a discontinued operation (e.g., Parent is in teaching business and sells a subsidiary also in teaching business; the teaching business is still running).
- **Note:** If the Parent disposes of a subsidiary in a different line of business (e.g., Parent in Teaching, Subsidiary in Manufacturing), then it **WILL BE** a discontinued operation as the manufacturing business will shut down.

3. Initial Disclosure Event (IDE) (When to Start Disclosing)

The initial disclosure event occurs on the **earlier of**:

- The enterprise has entered into a **binding sale agreement** for substantially all of the assets attributable to the discontinuing operation.
- The **Board of Directors have approved a detailed formal plan AND** an **announcement** of the plan has been made.

4. Presentation and Disclosure

4.1. Initial Disclosure (Beginning with the financial statements for the period in which the initial disclosure event occurs)

An enterprise should include the following information relating to a discontinuing operation in its notes to the financial statements:

- A description of the discontinuing operation(s).
- The business or geographical segment(s) in which it is reported as per AS 17.
- The date and nature of the initial disclosure event.
- The date or period in which the discontinuance is expected to be completed, if known or determinable.

- The carrying amounts, as of the balance sheet date, of the **total assets to be disposed of** and the **total liabilities to be settled**.
- The amounts of revenue and expenses in respect of the ordinary activities attributable to the discontinuing operation during the current financial reporting period.
- The amounts of net cash flows attributable to the operating, investing, and financing activities of the discontinuing operation during the current financial reporting period.

4.2. Disclosures on the Face of the Statement of Profit and Loss

The following amounts should be shown on the face of the statement of profit and loss:

- The amount of **pre-tax profit or loss from ordinary activities** attributable to the discontinuing operation during the current financial reporting period, and the **income tax expense** related thereto.

4.3. Disclosures Other Than Initial Disclosures

When an enterprise disposes of assets or settles liabilities attributable to a discontinuing operation or enters into binding agreements for the sale or settlement of such, it should include, in its financial statements, the following information when the events occur:

- For any gain or loss that is recognised on the disposal of assets or settlement of liabilities attributable to the discontinuing operation:
 - The amount of the **pre-tax gain or loss**.
 - **Income tax expense** relating to the gain or loss.
- The **net selling price or range of prices** (which is after deducting expected disposal costs) of those net assets for which the enterprise has entered into one or more binding sale agreements, the **expected timing of receipt of those cash flows**, and the **carrying amount of those net assets on the balance sheet date**.

5. Updating the Disclosures

- In addition to these disclosures, an enterprise should include, in its financial statements, for periods subsequent to the one in which the initial disclosure event occurs, a description of any significant changes in the amount or timing of cash flows relating to the assets to be disposed or liabilities to be settled and the events causing those changes.
- The disclosures should continue in financial statements for periods up to and including the period in which the discontinuance is completed.
- Discontinuance is completed when the plan is **substantially completed or abandoned**, though full payments from the buyer(s) may not yet have been received.

6. Abandonment or Withdrawal from a Plan

- If an enterprise **abandons or withdraws** from a plan that was previously reported as a discontinuing operation, that **fact**, **reasons** therefore, and its **effect** should be disclosed.

7. Separate Disclosure for Each Discontinuing Operation

- Any disclosures required by AS 24 should be presented **separately for each discontinuing operation**.

8. Final Presentation of Disclosures

The disclosures required are presented in the notes to the financial statements except for the following, which should be shown on the face of the statement of profit and loss:

- The amount of **pre-tax profit or loss from ordinary activities** attributable to the discontinuing operation during the current financial reporting period, and the **income tax expense** related thereto.
- The amount of the **pre-tax gain or loss recognised on the disposal of assets or settlement of liabilities** attributable to the discontinuing operation.

9. Restatement of Prior Periods

- Comparative information for prior periods that is presented in financial statements prepared after the initial disclosure event should be **restated** to segregate assets, liabilities, revenue, expenses, and cash flows of **continuing and discontinuing operations** in a manner similar to the required disclosures.

10. Disclosure in Interim Financial Reports

Disclosures in an interim financial report in respect of a discontinuing operation should be made in accordance with AS 25, 'Interim Financial Reporting', including:

- Any **significant activities or events** since the end of the most recent annual reporting period relating to a discontinuing operation.
- Any **significant changes in the amount or timing of cash flows** relating to the assets to be disposed or liabilities to be settled.

AS 25 - Interim Financial Reporting

1. Definition of Interim Period

- Interim period is a financial reporting period which is **shorter than a full financial year** (e.g., one month, three months, six months, nine months).

2. Content of an Interim Financial Report

- An interim financial report can be presented in two options:
 - **Option 1: Condensed Financial Statements (Summary):**
 - It includes at minimum each of the **headings and subheadings** of the Balance Sheet and Profit and Loss items.
 - It also includes **only relevant explanatory notes**.
 - Here, the face of the Balance Sheet, Profit and Loss, and Cash Flow are given.
 - **Option 2: Complete set of Financial Statements:**
 - Here, the company gives **full details** like Annual Financial Statements.

3. Periods for which Interim Financial Statements are Required to be Prepared (Comparatives of Interim Financial Statements)

- The periods for which statements are required are structured as follows:

Statement	Current Period	Comparative Period
Balance Sheet	End of current interim period.	End of immediately preceding financial year.
Profit and Loss	i) Current interim period AND ii) Cumulative for Year to date.	i) Comparable interim period of Previous Year AND ii) Comparable Year to date of Previous Year.
Cash Flow	Cumulative for Year to date.	Comparable Year to date of Previous Year.

- *Example (Interim period is 3 months, ending 31/12/26):*
 - **Balance Sheet:** As on 31/12/26 compared to As on 31/03/26.
 - **Profit and Loss:**
 - i) 01/10/26 to 31/12/26 compared to 01/10/25 to 31/12/25.
 - ii) 01/04/26 to 31/12/26 compared to 01/04/25 to 31/12/25.
 - **Cash Flow:** 01/04/26 to 31/12/26 compared to 01/04/25 to 31/12/25.
- *Example (Interim period is 6 months, ending 30/09/28):*
 - **Balance Sheet:** As on 30/09/28 compared to As on 31/03/28.
 - **Profit and Loss:**
 - i) 01/04/28 to 30/09/28 compared to 01/04/27 to 30/09/27.
 - **Note:** Since the interim period (6 months) is the same as the year to date (6 months), the cumulative year to date is the same as the current interim period and is not required to be shown separately.
 - **Cash Flow (Year to date):** 01/04/28 to 30/09/28 compared to 01/04/27 to 30/09/27.

4. Revenue received seasonally or occasionally

- Such revenue should be **booked during the interim period in which it is earned** and it should **not be deferred** to any other interim period.

5. Expense / Cost incurred unevenly during the financial year

- Such cost should be **booked during the interim period in which it is accrued and incurred**.

6. Income Tax Expense

- Income Tax is recognised in each interim period based on the **best estimate of weighted average Annual effective Income Tax Rate** expected for the **full financial year**.
- **Formula for Weighted Average Annual Tax Rate:** Formula for Weighted Average Annual Tax Rate

Weighted Average Annual Tax Rate = (Tax Expense for full year ÷ Total profit of full year) × 100

6.1. When different class of income is earned by company (e.g., Business Income and Capital Gains), in such cases different Tax Rates will be applied to different class of income.

6.2. When Accounting Year and Tax Year end is different, in such cases a different Average Annual Tax Rate is computed for quarters falling in different Tax Years.

- **Note on Zero Average Annual Tax Rate (Loss Scenario):** When Average Rate is 0%, do not write tax expense as 0 in all quarters. Instead, calculate **tax expense on profit** and **tax savings on loss** as per the rate given in the question.

7. Other Special Cases

- 1) Whether quarterly results prepared under clause 41 of Listing agreement entered between stock exchange and listed enterprise meets the definition of Interim financial report as per AS 25 and whether provisions of AS 25 should be applied on the same?
 - Those quarterly results **do not meet the definition** of AS 25.
 - However, **recognition and measurement principles** given in AS 25 of items contained in such interim results **should be applied** for recognition and measurement.
- 2) Impairment loss of Property, Plant, and Equipment / write-down of Inventories to Net Realisable Value (NAV)
 - Impairment loss/write-down in one interim period can be **reversed** in another interim period if **favourable conditions exist** or the condition due to which loss was booked is **not existing any more**.
- 3) On what Basis Provision for Gratuity, Pension, etc., should be Calculated?
 - Determined on a **Year to date Basis**.
 - *Example (Provision for Gratuity):*
 - Quarter 1 (Year to date is 3 months): Provision for Gratuity is 10,000. (Profit and Loss Debit 10,000 To Provision 10,000)
 - Quarter 2 (Year to date is 6 months): Provision for Gratuity is 15,000. The incremental expense is 5,000. (Profit and Loss Debit 5,000 To Provision 5,000, bringing the total provision to 15,000).

AS 26 - Intangible Assets

1. Definitions

- **Intangible Assets:**
 - Non-Monetary Asset
 - Without Physical Substance
 - Held for use in the business.
 - **Identifiable:** Must meet any one of the following two conditions:
 1. It can be separately sold from other assets or
 2. It arises from a separate legal contract.
- **Non-Monetary Asset (As per AS 11):**
 - It is not realisable in a fixed or determinable amount.
 - *Note:* The monetary/non-monetary concept is only for Balance Sheet items.

Distinction for Assets:

Asset Type	Purpose	Applicable Standard
Intangible Asset	Held for use in the business	AS 26
Intangible Asset	Held for sale in the ordinary course of business	AS 2 - Inventory

Guidance on Assets that incorporate Both Tangible and Intangible elements:

- The entity should assess which element is more significant.
- *Example:* Software purchased in a CD → AS 26.
- *Example:* Computer machine purchased incorporating software → AS 10 - Property, Plant, and Equipment (PPE).

2. Recognition criteria

- **Future Economic Benefits (FEB's):** The asset is expected to generate future economic benefits.
- **Cost Measurement:** The cost can be measured reliably.

3. Measurement

- **Initial Measurement:** Measured at Cost.
- **Subsequent Measurement:** Measured at Cost less: Accumulated Amortization.

Initial Measurement (Cost)

Acquisition Method	Treatment
i) Purchased	Purchase Price (Less: Trade discount and Rebates) + Non-Refundable taxes and duties (Refundable taxes are not considered in cost) + Directly Attributable Expenses. Exclusion from cost is the same as AS 10.
ii) Exchange	Same as AS 10 (Recorded at the Fair Value of the asset received or the Fair Value of the asset given up, whichever is more clearly evident).
iii) Amalgamation	Any intangible asset taken over by the purchasing Company in Amalgamation will be recorded at Fair Value . Any excess Purchase Consideration paid over and above the Fair Value of Net Assets acquired will be recorded as Goodwill .

Acquisition Method	Treatment
iv) Internally Generated Assets (Other than Goodwill)	The cost incurred in the Development Phase will be Capitalised if all six conditions are met. Research Phase expenditure must be charged to the Profit and Loss Account.
v) Government Grant	Accounting as per AS 12 - Accounting for Government Grants.

Internally Generated Intangible Assets (Other than Goodwill)

- **Internally generated Goodwill:**
 - Not recognised as Intangible Asset because:
 1. It is **Not Identifiable**.
 2. Cost cannot be measured reliably.
- **Research Phase:**
 - The entity cannot demonstrate that an Intangible Asset exists.
 - All Research Phase Expenses must be transferred to the **Profit and Loss Account**.
- **Development Phase:**
 - This is the phase that converts the results of Research into a marketable product.
 - **Capitalise** all directly attributable expenses of the development phase.
 - **Development phase Begins only when All six conditions are met:**
 1. Technical feasibility of completion.
 2. Intention to complete.
 3. Ability to use or sell the Intangible Asset.
 4. Availability of adequate resources like technical, financial, etc.
 5. How it will generate Future Economic Benefits (FEB's).
 6. Cost can be measured reliably.
 - **Intangible Assets that cannot be recorded if internally generated:**
 1. Brand
 2. Customer Database
 3. Publishing Titles and Mastheads
 - **Hint for Development Phase conditions:** Two conditions related to completion, two related to availability ('A's - Ability, Availability of resources), and two related to Recognition criteria (FEB's, Cost measurement).

4. Subsequent Cost Incurred

- **Subsequent Measurement:** Cost of Intangible Asset less: Accumulated Amortization (Only Cost Model is allowed).
- If such subsequent expenditure will generate **future economic benefit**, then it can be **added to the cost of the intangible asset**.
- If **No future economic benefits (FEB's)**, then transfer the expenditure to the **Profit and Loss Account**.
 - *Example:* Software repair fees (no increase in validity) → Profit and Loss.
 - *Example:* Renewal fees (software validity increases by 5 years) → Capitalise.

5. Expenditure incurred, But No Intangible Asset

- The following expenditures should always be recognised as an **Expense** (Always Profit and Loss Account):
 - Training Expense
 - Advertising Expense / Promotional Expense
 - Startup Expense
 - Expense of relocation or reorganising activities
 - Research Phase Expense

6. Amortization

- **A. Methods:**
 - Straight Line Method (SLM)
 - Written Down Value (WDV) Method
 - Units of Production
 - (Same as AS 10 - Property, Plant, and Equipment)
 - **B. Amortization Period:**
 - **Start Date (Commencement):** When the asset is **Available for use**.
 - **End Date (Cessation):** When the life is over OR the asset is disposed (sold).
 - **Note:** When the Carrying Amount (CA) reaches the Residual Value, no further amortization is to be done.
 - **Useful life of Intangible Asset:**
 - As per AS 26, the **Maximum life** of an Intangible Asset is **10 years** (Presumption by AS 26).
 - Life can be **more than 10 years** only when the company has **evidence**.
 - As per AS 14 (Amalgamation), Goodwill should be amortised over **5 years** (This is a note from AS 14 context).
-

7. Residual Value

- Since an Intangible Asset has **no physical substance**, its scrap / Residual Value is assumed to be **zero**.
 - **Exception:** If there is a **commitment by a third party** to purchase the intangible asset at the end of its useful life, then that price can be assumed to be the Residual Value.
-

8. Changes in Estimate

- Changes in Estimate of Amortization method, useful life, or Residual Value are **changes in Accounting Estimates** (As per AS 5).
 - Hence, do **Prospective Accounting**.
-

9. De-Recognition (Removal from Books)

- De-recognise the asset when:
 1. It is sold OR
 2. The life of the asset is over.
 - If it is sold, then the **gain or loss on sale** will be transferred to the **Profit and Loss Account**.
-

10. Impairment (AS 28)

- **Impairment Test:** Compare the **Carrying Amount (CA) of the Asset** with the **Recoverable Amount (RA) of the Asset**.
 - **Recoverable Amount (RA):** It is the **Higher of:**
 1. Value in Use (Present Value of future cash flows)
 2. Net Selling Price (Sale Price less: Cost of Disposal)
 - **Impairment Loss** = Carrying Amount - Recoverable Amount (If CA > RA).
 - *Journal Entry:* Impairment Loss Account Debit to Asset Account.
 - **Impairment Gain:** There is **no concept of Impairment Gain**. If the Recoverable Amount is higher than the Carrying Amount, the asset will stay at the Carrying Amount.
-

11. Other Miscellaneous Points

- **Intangible Asset purchased in exchange of shares:**
 - The asset is recorded at the **Fair Value of the asset acquired** OR the **Fair Value of the shares given up**, whichever is **more clearly evident**.

- **Accounting for Previous Years' Mistakes (Prior Period Items - PPI):**
 - As per AS 5, mistakes of previous years are to be treated as **Prior Period Items** and its effect will be considered in the **Current Profit and Loss Account** as a Prior Period Item.
 - *Example:* If amortization was not done in previous years, the missed amount is recorded as "Prior Period Item (Profit and Loss) Account Debit" in the current year.
- **Annual Fees (Percentage of Revenue):**
 - Annual fees based on Net Revenue will be charged to the **Profit and Loss Account as an expense when it is incurred.**
- **Amortization Policy:**
 - If the company follows a policy of charging **full year amortization in the year of purchase/acquisition**, this must be mentioned in the question.

AS 27: Financial Reporting of Interests in Joint Ventures

1. Definition

A) Joint Venture (JV)

- A Joint Venture is a contractual agreement whereby two or more parties undertake an economic activity which is subject to joint control.

B) Venturers

- Parties to the Joint Venture.

2. Types of Joint Venture

Type	Full Form	Meaning / Features	Accounting
JCO	Jointly Controlled Operations	* Contractual agreement is there but they have not formed a separate legal entity. * Each venturer has its own separate business. * No separate legal entity for Joint Venture. * All venturers use their own assets, incur expenses, meet the liabilities for Joint Venture. * Any revenue generated is shared by the venturers as per the contract.	* Under JCO, each venturer should recognise its own share of asset, liability, income, expense. * We will also prepare a Consolidated Profit and Loss Account of JCO (it is like rough extract).
JCA	Jointly Controlled Assets	* Venturers come together to construct a common asset for their own use. * There is common control over the joint asset.	* Under JCA, each venturer will record their share of asset/expense/liability/Income.
JCE	Jointly Controlled Entities	* Venturers create a separate legal entity for their business. * Joint Venture in case of JCE will maintain its own accounting records.	Accounting by Venturers: * We will record Investment in Joint Venture (As per AS 13). * Proportionate consolidation method (AS 27). * Here venturers record asset, liability, income, expense of JCE in Consolidated Financial Statements (CFS) only to the extent of own share. * Procedure is same as AS 21 (Except there is no Minority Interest).

3. Cases where AS 27 does not allow use of Proportionate Consolidation

- Where Investment is intended to be temporary.
- There are severe long-term restrictions which significantly restrict the transfer of funds to the venturer.

4. Discontinuance of Proportionate Consolidation Method

The method is discontinued when:

- Venturers cease to have joint control in the Joint Venture. OR
- The Joint Venture has started operating in severe long-term restrictions.

After discontinuance of proportionate consolidation method:

- If stake is more than 50% → Apply AS 21.
- If stake is 20% to 50% → Apply AS 23.
- If stake is less than 20% → Apply AS 13.

5. Transactions Between a Venturer & Joint Venture

- When a venturer sells any asset to the Joint Venture or purchases from the Joint Venture, in that case the venturer in its books should record the transaction only to the extent of other parties' share.

When both venturers contribute an asset to Joint Venture (JCE - Separate Entity, e.g., J Ltd., 50:50):

- **Rule:**
 - Asset given up will be de-recognised at Carrying Amount (CA) to the extent of other parties' share.
 - Asset received via Joint Venture will be recorded at Fair Value (FV) to the extent of own share.
 - **Journal Entry (J.E.) in the Books of A Ltd. (Consolidated Financial Statements - CFS):**
 - Asset Received Account Debit ($FV \times 50\%$)
 - Profit and Loss Account Debit (Calculated as: Asset given up @ $CA \times 50\%$ - Asset received @ $FV \times 50\%$)
 - To Asset Given Up ($CA \times 50\%$)
 - **Journal Entry (J.E.) in the Books of B Ltd. (Consolidated Financial Statements - CFS):**
 - Asset Received Account Debit ($FV \times 50\%$)
 - To Asset Given Up ($CA \times 50\%$)
 - To Profit and Loss Account (Calculated as: Asset Received @ $FV \times 50\%$ - Asset given up @ $CA \times 50\%$)
-

AS 28 - Impairment of Assets

1. Scope

- Accounting Standard 28 (AS 28) deals with the impairment of assets, which is a decline in the value of assets.
 - This standard is applicable to all assets, except:
 - Inventories (Accounting Standard 2).
 - Assets arising under construction contracts (Accounting Standard 7).
 - Financial assets including investments covered under (Accounting Standard 13).
 - Deferred Tax Asset (Accounting Standard 22).
 - This standard is applicable to:
 - Property, Plant, and Equipment (Accounting Standard 10).
 - Intangible Assets (Accounting Standard 26).
-

2. When is an Asset Impaired?

- An asset is impaired when the **Carrying Amount** is more than the **Recoverable Amount**.
-

3. Recoverable Amount

- Recoverable Amount is the **Higher of**:
 1. **Value in Use** (Present Value of future cash flows from using the asset).
 2. **Net Selling Price**.
 - **Value in Use**:
 - It is the present value of future cash flows expected to be generated from using the asset.
 - To calculate Value in Use, we need two things:
 - **Expected future cash flows**:
 - Cash inflows from using the asset.
 - Less: Cash outflows (if any) which are incurred to generate inflows.
 - Add: Residual value of the asset at the end of its useful life (Add in the last year's cash flow).
 - **Discount Rate**: Use **Pre-tax discount rate**.
 - (Note: Post-tax discount rate is not used.)
 - **Net Selling Price**: Selling Price – Cost of disposal / Selling cost / Cost to sell
-

4. Treatment of Impairment Loss

- **If the asset is at Cost Model**:
 - Transfer Impairment loss to the **Profit and Loss Account**.
 - Journal Entry: Impairment Loss (Profit and Loss) Account Debit to Property, Plant, and Equipment / Intangible Asset Account.
- **If the asset is at Revaluation Model**:
 - First, adjust the Impairment loss from the **Balance of Revaluation Reserve** (if any).
 - Remaining Impairment loss will be transferred to the **Profit and Loss Account**.

- *Journal Entry Example (When Impairment Loss Exceeds Revaluation Reserve)

Impairment Loss (Revaluation Reserve) Account Debit Impairment Loss (Profit and Loss) Account Debit To Property, Plant, and Equipment Account

- **Effect of Impairment on Depreciation:** Once an asset is impaired, the depreciation changes **prospectively** (i.e., it is calculated on the **Revised Carrying Amount** after impairment, over the remaining useful life).

5. Can Recoverable Amount be Negative?

- Recoverable Amount can be zero.
- If the Net Selling Price is negative (Selling Price is zero and Cost of Disposal is a positive number), the Recoverable Amount will be zero (since Recoverable Amount is the Higher of Value in Use and Net Selling Price, and Value in Use cannot be negative).
- If Carrying Amount (CA) is 100 and Recoverable Amount (RA) is zero, the Impairment loss will be the full 100.
- *Note:* Sometimes a negative Net Selling Price must be booked as a write-off under some other accounting standard (e.g., Accounting Standard 29).

6. When to Conduct Impairment Test?

- Conduct Impairment Test whenever there is an **indication of impairment**.
- Indication does not mean impairment has already occurred; it means the test must be conducted.

External Sources of Indication	Internal Sources of Indication
1. Asset market value has declined.	1. Physical Damage to the asset.
2. Significant changes in Technology or Market conditions which has an Adverse (negative) effect on the entity.	2. Asset has become idle or there is a plan to dispose of the asset.
3. Market Interest rates have increased, which might reduce the Present Value (PV) of Value in Use.	3. Performance of the asset is worse than expected.

7. Cash Generating Unit (CGU)

- To conduct an impairment test of an individual asset, it is necessary to calculate the Value in Use of that asset.
- Sometimes, individual assets do not have individual Value in Use (e.g., a laptop in a whole teaching setup).
- In such cases, an individual asset impairment test might not be possible.
- In such cases, we will conduct an impairment test as a **Cash Generating Unit (CGU)**.
- **CGU** is a **group of assets** that generates cash flow together.
- A single company can have multiple CGUs.

Impairment Testing of a CGU (When loss exists):

- When Impairment loss is calculated for a CGU (Carrying Amount of CGU minus Recoverable Amount of CGU), the loss must be allocated between **All Assets** in the CGU in the **ratio of their Carrying Amounts**.

8. Impairment Testing with Goodwill (GW)

- Individual Impairment Test for Goodwill is **Not possible**.
- Therefore, Goodwill must be allocated to CGUs for the purpose of the impairment test.

A. Goodwill is Allocable to CGUs (Bottom-up Approach)

- If Goodwill is allocable to individual CGUs, the impairment test is conducted for each CGU (CGU Carrying Amount including allocated Goodwill, compared to CGU Recoverable Amount).
- The Impairment loss is first allocated to **Goodwill** associated with that CGU, and the **balance loss (if any)** is allocated to other assets in the CGU in the **ratio of their Carrying Amounts**.

B. Goodwill is Unallocable to CGUs (Two-Step Testing)

- If Goodwill provides benefit to multiple CGUs but is unallocable in any ratio, we follow the **Bottom-up Approach + Top-down Approach**.
- **First Test (Bottom-up):** Test individual CGUs **without** unallocable Goodwill.
 - Impairment loss is calculated and allocated among the assets of the CGU (if the CGU is impaired).
- **Second Test (Top-down):** Combine the revised Carrying Amounts of all CGUs (after the first test) **plus** the unallocable Goodwill.
 - Impairment loss is calculated for the combined unit and allocated **only to the unallocable Goodwill**.

9. Impairment Testing with Corporate Assets (e.g., Headquarter Building)

- Individual Impairment Test of a Corporate Asset is **Not possible** (as it does not generate separate cash flows).
- Corporate Assets must be allocated to CGUs for the impairment test.

A. Corporate Asset is Allocable to CGUs (Bottom-up Approach)

- If the Corporate Asset is allocable, the impairment test is conducted for the CGU (CGU Carrying Amount including allocated Corporate Asset, compared to CGU Recoverable Amount).
- The Impairment loss is allocated among all assets in the CGU (including the allocated Corporate Asset) in the **ratio of their Carrying Amounts**.

B. Corporate Asset is Unallocable to CGUs (Two-Step Testing)

- If the Corporate Asset provides benefit to multiple CGUs but is unallocable in any ratio, we follow the **Bottom-up Approach + Top-down Approach**.
- **First Test (Bottom-up):** Test individual CGUs **without** the unallocable Corporate Asset.
- **Second Test (Top-down):** Combine the revised Carrying Amounts of all CGUs (after the first test) **plus** the unallocable Corporate Asset.
 - Impairment loss is calculated for the combined unit and allocated to the assets of the CGUs and the Corporate Asset in the **ratio of their Carrying Amounts**.

10. Reversal of Impairment Loss

- An impairment loss which was previously booked on an asset can be **reversed in the future**.
- **Journal Entry for Reversal:** Property, Plant, and Equipment Account Debit to Reversal of Impairment Loss (Profit and Loss/Revaluation Reserve).
- If the impairment loss was previously adjusted from the **Profit and Loss Account**, the reversal should also be done through the **Profit and Loss Account**.
- If the impairment loss was previously adjusted from the **Revaluation Reserve**, the reversal should also be done through the **Revaluation Reserve** (up to the balance previously adjusted).
- **Maximum Reversal:**

- The actual reversal of impairment loss is the difference between the **Recoverable Amount** and the **Carrying Amount** (after Impairment and subsequent Depreciation).
- The **Maximum Reversal** that can be booked is the amount by which the asset's **Carrying Amount (if no impairment had been recorded)** exceeds the **Carrying Amount (after impairment and subsequent Depreciation)**.
- *Formula for Maximum Reversal:*
Formula for Maximum Reversal of Impairment

Maximum Reversal = Carrying Amount (if no impairment) – Carrying Amount (after impairment)

- **Reversal of Impairment Loss on Goodwill:**
 - An impairment loss which is booked on Goodwill **can be reversed**, but subject to certain conditions.
 - **Note:** If 5 years of Goodwill's life have lapsed (as per AS 14 for Amalgamation), then the impairment loss of Goodwill **cannot be reversed**.

11. Extra Concepts

- **Individual Asset Impairment within a CGU:** If an individual asset is transferred to a CGU for impairment testing, the individual asset is impaired **only if the CGU is impaired**. If the CGU is **Not Impaired**, then the individual asset is **also not impaired**.
- **Cash Generating Unit Determination (Example Scenario):**
 - If Plant A produces a component that is assembled in either Plant B or Plant C, and products are sold world-wide from B or C, the CGU depends on the market for the component:
 - **Case 1: Active market for Plant A's products:** Plant A generates independent cash flows, so Plant A is one CGU, and Plants B and C together form another CGU.
 - **Case 2: No active market for Plant A's products:** Plants A, B, and C generate cash flow together, forming a **single CGU**.

AS 29 - Provisions, Contingent Liabilities & Contingent Assets

I. Definitions

- **Liability:**
 - It is a **Present Obligation**
 - Arising out of **Past Events**.
 - Settlement of which is expected to result in **outflow of Resources**.
- **Obligation / Obligating Event:**
 - It is an event that results in an enterprise having **no realistic alternative** to settling the obligation.
 - *Obligation means if we have to settle this, otherwise, there is no other way.*

Obligation / Likelihood of Outflow:

- **Present Obligation:**
 - Means the outflow of resources is **More likely than NOT** (More than 50% chance of paying it).
- **Possible Obligation:**
 - Means the outflow of resources is **Less likely than NOT** (Less than or equal to 50% chance of paying it).
- For an obligation to arise there should be a **past event**.
 - *Example: Loan taken → Past Event is taking loan from a Bank.*
 - *Example: Penalty on government dues or penalty on contamination → Past Event is not paying the government dues or contaminating the river.*

II. Provisions

- **Definition of Provision:**
 - It is a **liability** with **uncertain timing or amount**.
- **Recognition of Provision:**
 - A provision should be recognised when:
 1. An entity has a **present obligation**.
 2. As a result of a **past event**.
 3. It is **probable** that an outflow of resources will be required.
 4. A **reliable estimate** of the amount can be made.
- **Measurement of Provision:**
 - The entity shall apply its **best estimate** to measure the amount of provision.
 - The amount of provision should **NOT be discounted to its Present Value**.
 - **Exception:** In case of Decommissioning / Dismantling / Site Restoration, it is recorded at **Present Value** (As discussed in AS 10).
- **Changes in Provisions:**
 - Provision should be **reviewed at each Balance Sheet date** to reflect the best estimate.
 - If a provision is **no longer required**, then **reverse the provision**.
- **Use of Provision:**
 - Only expenditure that relate to the **original provision** are adjusted against it.

- *Example of Reversing Provision

If Provision for warranty was 15,000 but the actual expense was 12,000, then the remaining 3,000 is reversed:

Provision for Warranty Account Debit 3,000 To Profit and Loss (Reversal) 3,000

III. Special Points related to Provision

1. Virtually Certain Implementation of Law:

- If any law is announced by the government, due to which an obligation to make the payment might arise on the company, then create provision **only when the law is virtually certain to be implemented**.
- *Example: If a law for penalty on river contamination is announced in parliament, formal signing is pending, the law is virtually certain to be implemented, and a provision for the penalty should be created (YES).*

2. Requirement of Inspection / Major Overhaul:

- Only those provisions are recognised for which the entity has **no realistic alternative** rather than settling it.
- If the entity can **avoid such expenditure by its future actions** (e.g., by selling the asset before the inspection is due), then **No provision is recognised**.
- *Note: Provision can be made after 5 years of use of the asset, when the inspection cost becomes due.*

3. Future Operating Losses:

- **No Provision** is to be recognised as it **does not meet the definition of Provision** (It does not arise from a **Past Event**).

4. Onerous Contract (Loss making contract):

- It is a contract where the **unavoidable cost** of meeting the obligation **Exceeds** the **Benefits to be received** from it.
- *Rule: Create Provision for the lower of: unavoidable loss or cancellation penalty.*

5. Restructuring:

- **Restructuring** is a program that materially changes the **Scope of Business OR the Manner in which Business is conducted**.
 - A provision for restructuring cost is recognised **only when recognition criteria of Provision are met**.
 - *Example: Restructuring plan ready, announced restructuring, steps started for restructuring → Recognise Provision.*
 - *Example: Restructuring Karne ka soch rahe hai, no steps undertaken → No Provision.*
 - **Restructuring Provision Amount:**
 - **Includes:** Only the **direct expenditure** arising from restructuring which are **BOTH**:
 1. Necessarily entailed by the restructuring, **AND**
 2. Not associated with ongoing activities of the entity.
 - *Example of Included:* 10 employees lay off - 2 month salary, 2 Years rent payable (agreement was non-cancellable), Other relevant expense for closing the business.
 - **Excludes:** Expenses related to the **future conduct of business**, such as:
 - Retaining cost of continuing staff.
 - Relocation cost of continuing staff.
 - Marketing of online teaching.
 - Investment in new systems (Mic, Projector, camera, iPad, etc.).
 - *(No Provision is created for these as this relates to future conduct of Business).*
-

IV. Reimbursements

- In this case, some or all of the expenditure required to settle a provision is **expected to be reimbursed by another party**.
- **Reimbursement is recognised only when it is virtually certain that such reimbursement will be received.**
- The amount of reimbursement shall **NOT Exceed the amount of provision**.
- **Presentation in Financial Statements:**
 - **Profit and Loss Account:** Expense and Reimbursement Income are shown **net off** (Net Expense).
 - **Balance Sheet:** Provision (Liability) and Reimbursement Asset (Asset) are **NOT net off** (No net off allowed).

V. Contingent Liability

- **Definition (Any 1 condition to be met):**
 1. It is a **Possible Obligation** arising out of a **Past Event**, the existence of which will be confirmed by the occurrence/non-occurrence of one or more future uncertain events.
 2. It is a **Present Obligation** arising out of a **Past Event** where the outflow is **NOT probable** (less than 50% chance), but the amount can be estimated reliably.
 3. It is a **Present Obligation** arising out of a **Past Event** where the outflow is **probable** (more than 50% chance), but the **amount cannot be estimated reliably**.
- **Recognition of Contingent Liability:**
 - Contingent liability should **NOT be recognised** in the financial statements but should be **disclosed in Notes to Accounts**.
 - **Exception:** If the probability of contingent liability is **very Remote** (e.g., chance of losing the case is 5% or less), there is **No need to disclose** such contingent liability.

VI. Contingent Asset

- **Definition:**
 - It is a **possible Asset** arising out of **Past Events**, the existence of which will be confirmed **only by the occurrence or non-occurrence** of one or more uncertain future events.
- **Recognition of Contingent Asset:**
 - Contingent Asset is **Neither recognised NOR disclosed in the Financial Statements**.
 - If the company wants to disclose it, it can disclose it in the **Report of Approving Authority (Director's Report)**.
 - **Exception:** If inflow is **virtually certain**, then it is **no more a contingent asset**. It becomes a **normal asset**, and therefore, it is **Recognised in the Financial Statements**.

Summary of Accounting Treatment (Implicit from Definitions and Rules)

Item	Outflow Probability	Reliable Estimate of Amount	Recognition	Disclosure
Provision	Probable (>50%)	Yes	Yes	Yes
Contingent Liability	Not Probable ($\leq 50\%$)	Yes / No	No	Yes*
Contingent Asset	Probable / Possible	Yes / No	No	No**

Notes:

- *Contingent Liability is disclosed unless the probability is very remote (5% or less).*

- *Contingent Asset is neither recognised nor disclosed in Financial Statements (but can be disclosed in the Directors' Report).*

Accounting for Branches

1. Classification of Branches

Branches can be classified into:

- 1. **Domestic Branch**
 - Dependent Branch
 - Independent Branch
- 2. **Foreign Branch**
 - Only Independent Branch

2. Dependent Branch

A dependent branch is one that is dependent on the Head Office for its accounting.

- This means there are **no books of account maintained at the Branch level**.
- Only the Head Office will maintain branch records in its own books.

2.1 Accounting Methods for Dependent Branch

Method Name	Suitable for	Purpose / Key Feature
Debtors Method	Small sized branches	A separate Branch Account is prepared for each Branch to compute the profit or loss made by each branch.
Stock and Debtors Method		
Final Accounts Method		
Wholesale Price Method		

2.2 Debtors Method (Branch Account Proforma)

- **Hint:** In the Branch Account, **transactions between the Branch and the Head Office are recorded**.

Debit Side (To)	Credit Side (By)
Opening Balance of Assets (Stock, Debtors, Petty Cash, etc.)	Opening Balance of Liabilities (Creditors, etc.)
Goods Sent to Branch (GSB)	Cash/Bank (Money sent from Debtors remitted to Head Office)
Cash/Bank (Cash paid by Head Office to Branch for expenses like Salary, Rent, Sundry expenses, etc.)	Goods Sent to Branch (Returns from Branch to Head Office)
Closing Balance of Liabilities (Creditors)	Cash/Bank (Remittance to Head Office)
Net Profit (Balancing Figure)	Cash/Bank (Cash Sales remitted to Head Office)
	Closing Balance of Assets (Stock, Debtors, Petty Cash, etc.)

2.3 Recording Transactions in Head Office Books (Branch Account)

1. **Goods sent to Branch by Head Office:**
 - Branch Account Debit
 - To Goods Sent to Branch (GSB) Account
2. **Returns from Branch to Head Office:**
 - Goods Sent to Branch (Returns) Account Debit
 - To Branch Account
3. **Cash paid by Head Office to Branch** (to meet expenses like salary, rent, sundry expenses, etc.):
 - Branch Account Debit
 - To Cash/Bank (CIB)
4. **Cash remittance by Branch to Head Office:**
 - Cash/Bank Account Debit
 - To Branch Account
5. **Cash sales made by Branch to outside parties:**
 - This is **not a transaction between Branch and Head Office** directly.
 - However, because it is a cash sale, the Branch will receive the money on sale, and the Branch will have to immediately remit this money to the Head Office.
 - Such remittance becomes a **transaction between Branch and Head Office** and thus will be recorded.
 - Journal Entry (J.E.): Cash/Bank (Cash Sales) Debit To Branch Account
6. **Credit Sales by Branch to outside third party:**
 - In the Branch Account, there is **No entry directly**.
 - But when we show the opening debtors and closing debtors, the credit sale impact will indirectly appear.

2.4 Memorandum Accounts

- The Branch will maintain a few rough records to find the opening and closing balances of Assets and Liabilities. Such rough accounts are known as **Memorandum Accounts**.
- **Transactions between the Branch and outsiders will be shown in Memorandum Accounts.**
- Transactions such as Bad debts, Discount allowed to Debtors, and returns from Debtors are shown in the Memorandum Debtors Account first (1st effect).
- By default, the 2nd effect is: Branch remits the cash to Head Office (J.E.: Cash/Bank To Branch Account).

Crux (Summary of Transactions):
Transaction between Branch and Head Office → will appear directly in the Branch Account.
Transaction between Branch and outsider (but Cash/Bank (CIB) involved) → Appear directly in the Branch Account. (e.g., Cash sales, cash expenses paid by Branch, which are then indirectly adjusted/remitted to Head Office).
Transaction between Branch and outsider (NO Cash/Bank (CIB) involved) → Appear in Memorandum Accounts . (e.g., credit sales, credit purchases, bad debts, discount, depreciation, etc.).

2.5 Final Accounts Method (Trading and Profit and Loss Account)

- Here, the Head Office prepares the Branch Trading and Profit and Loss Account.
- In this method, Trading and Profit and Loss Accounts are prepared considering each branch as a **separate entity**.
- The main advantage of this method is that it is **easy to prepare and understand**.
- It also gives **complete information of all transactions** which are ignored in other methods.
- **Please note** that the Branch Trading and Profit and Loss Account is merely a **Memorandum Account**, and entries made there **do not have any double entry effect** in the Head Office main books.

2.6 Goods Sent to Branch at Invoice Price / Selling Price

- Sometimes the Head Office does not want to reveal the cost of goods to the branch and therefore invoices goods at a price which is **higher than the cost price**. Such a price is known as **Invoice Price (IP)**.
- The difference between cost price and invoice price is called **“loading”**.

- **Crux (Rule for Loading Reversal):** Reverse loading only on the following items:
 1. Goods Sent to Branch (GSB)
 2. GSB Returns
 3. Opening Stock (Opn Stk)
 4. Closing Stock (Cls Stk)
- **Note:** The Branch's cash/credit sales price should **not** have loading reversed.

2.7 Commission to Manager

- **Commission to Manager (After charging such commission):** Formula for Commission

Commission = Net Profit (before commission) $\times 10 \div 110$

Commission to Manager (Before charging such commission): Commission = Net Profit (before commission) $\times 10 \div 100$

3. Stock and Debtors Method

- **Concept:** In the Debtors Method, memorandum accounts were prepared in the working notes. In the Stock and Debtors Method, **all memorandum accounts become part of your main solution, and no single Branch Account is prepared.**
- **Purpose:** The Stock and Debtors Method is followed if the Head Office wants to exercise **more detailed control** over the working of a branch.
- **Accounts maintained by Head Office:**

Account Name	Balancing Figure (Bal fig) Represents
1. Branch Stock Account	Surplus/Shortage or Goods Sold/Transferred to Customers
2. Branch Adjustment Account	Gross Profit
3. Branch Debtors Account	Closing Balance / Collection from Debtors
4. Branch Cash Account	Cash Closing Balance / Remittance to Head Office / Branch Collection Expenses
5. Branch Fixed Asset Account	Closing Balance
6. Branch Expense Account	Total Expense transferred to Profit and Loss Account
7. Branch Profit and Loss Account	Net Profit of Branch
8. Goods Sent to Branch Account	Net Cost of goods sent to Branch

3.1 Adjustments in Stock and Debtors Method

Loss Type	Where Adjusted (IP/Cost)	Where Adjusted (Account)	Note
Normal Loss	Stock @ Invoice Price (IP)	Branch Stock Account (Credit side)	Loading to be adjusted from Gross Profit: Debit Branch Adjustment Account.
Abnormal Loss (Lost by fire, pilferage, theft)	Loading part is adjusted from Gross Profit (Branch Adjustment Account). Cost part is adjusted from Net Profit (Branch Profit and Loss Account).	Branch Adjustment Account (for loading) and Branch Profit and Loss Account (for cost).	Goods are sent by Head Office to Branch @ Cost + 25%.

4. Wholesale Price Method

- **Concept:** Under this method, the Head Office supplies goods to the branch at **Cost plus Wholesale Profit**, which is equal to the **Wholesale Price (WP)**.
- The branches sell these goods to customers at the **Retail Price (RP)**.
- In such a case, the Head Office is interested in knowing the **additional profit** which has been earned by the branch.
- The **additional profit** is the difference between the Retail Price and the Wholesale Price.

Price Component	Formula
Cost	100%
(+) Wholesale Profit	
= Wholesale Price (WP)	
(+) Retail Profit	
= List Price / Retail Price (RP)	

- **Branch Trading Account (Draft under Wholesale Price Method):**
 - The **Gross Profit (G.P.)** calculated in the Branch Trading Account will represent the additional profit (Retail Profit).
- **Valuation of Closing Stock:** The real cost of the branch is the **Wholesale Price**, so closing stock at the branch has to be valued at the **Wholesale Price**.
- **Stock Reserve:** In the books of the Head Office, it is necessary to create a **Stock Reserve** on the opening stock and closing stock.
 - The amount of the Stock Reserve will be equal to the difference between the **Wholesale Price and the Cost to Head Office**.
 - Stock Reserve will be transferred in the Head Office Profit and Loss Account.

5. Independent Branch

A branch is considered **Independent** if it **maintains its own set of books of accounts**.

5.1 Inter-Office Accounting Entries

Transaction	Head Office Books	Branch Books
1. Goods sent by Head Office to Branch	Branch Account Debit To Goods Sent to Branch (GSB)	Goods Received from Head Office Account Debit To Head Office Account
2. Goods returned by Branch to Head Office	GSB Returns Account Debit To Branch	Head Office Account Debit To Goods Received (Returned)
3. Branch Expense incurred and paid by Branch	No entry	Expense Account Debit To Cash/Bank Account
4. Branch Expense paid by Head Office	Branch Account Debit To Cash/Bank (CIB)	Expense Account Debit To Head Office Account
5. Purchase made from party other than Head Office, by Branch directly	No entry	Purchases Account Debit To Cash/Creditors Account
6. Sales made by Branch to outside customers	No entry	Cash/Debtors Account Debit To Sales
7. Collection from Debtors directly received by Head Office	Cash/Bank Account Debit To Branch	Head Office Account Debit To Debtors

Transaction	Head Office Books	Branch Books
8. Purchases made by Branch and payment done by Head Office	Branch Account Debit To Cash/Bank (CIB)	Purchases Account Debit To Head Office Account
9. Purchase of Asset by Branch and paid by Branch	No entry	Asset Account Debit To Cash/Bank
10. Asset account maintained at Head Office but purchased by Branch & paid by Branch	Branch Asset Account Debit To Branch	Head Office Account Debit To Cash/Bank
11. Depreciation when asset account is maintained at Head Office for Branch Asset	Branch Account Debit To Branch Asset Account	Depreciation Account Debit To Head Office Account
12. Remittance of funds by Head Office to Branch	Branch Account Debit To Cash/Bank	Cash/Bank Account Debit To Head Office Account
13. Remittance of funds by Branch to Head Office	Cash/Bank Account Debit To Branch	Head Office Account Debit To Cash/Bank
14. Goods dispatched by Head Office but not received by Branch (Goods in Transit)	No entry	Goods in Transit Account Debit To Head Office Account
15. Cash remitted by Branch to Head Office, but not received by Head Office (Cash in Transit)	Cash in Transit Account Debit To Branch Account	No entry
16. Cash remitted by Head Office to Branch, but not received by Branch	No entry	Cash in Transit Account Debit To Head Office Account
17. Inter-Branch Transactions (e.g., Kolkata Branch incurred expenditure of ₹1000 for Delhi Branch)	Hint: Inter-Branch Transactions are usually adjusted as if they were entered into with the Head Office .	<i>HO Books:</i> Delhi Branch Account Debit To Kolkata Branch Account
		<i>Delhi Branch:</i> Advertisement Expense Account Debit To Head Office Account
18. Head Office Expenses allocated to some extent to Branch	Branch Account Debit To Expense (Expense Reverse)	Expense Account Debit To Head Office Account

Note on Commission to Manager (Rule for Inter-Office Transactions):

- If Head Office receives cash from Debtors, the Branch debits Head Office Account and credits Debtors Account. The Head Office debits Cash/Bank and credits Branch Account.
- If an Inter-Branch transaction occurs (e.g., Br. A pays expense for Br. B), the Head Office records it by debiting Br. B and crediting Br. A. Br. A debits HO and credits Cash. Br. B debits Expense and credits HO.

Buy Back of Equity Shares (Section 68)

1. Meaning of Buy Back

- The term **Buy Back of shares** implies the act of purchasing its own shares by the company.
- When shares are bought back by a company, they have to be **cancelled** by the company.
- Thus, shares buy-back results in a **decrease in share capital** of the company.
- A company **cannot** buy its own shares for the purpose of investment.

2. Objectives/Advantages of Buy Back of Shares

The following may be the objectives/advantages of Buy-back of shares:

- To increase **earnings per share (EPS)** if there is no dilution in the company's earnings, as the buy-back of shares reduces the outstanding number of shares.
- To increase **promoters' holding** as the shares which are bought back are cancelled.
- To discourage others to make a **hostile bid** to take over the company, as the buy-back will increase the promoters' holding.
- To support the **share price** on the stock exchanges when the share price, in the opinion of company management, is less than its worth, especially in a depressed market.
- To pay **surplus cash** to shareholders when the company does not need it for business.

3. Sources of Buy Back (Section 68 (1))

The Companies Act, 2013 under Section 68 (1) permits companies to buy-back their own shares and other specified securities out of:

- Its **free reserves**; or
- The **Securities Premium Account**; or
- The **proceeds of the issue of any shares or other specified securities**.

Note on Fresh Issue Proceeds:

- No buy-back of any kind of shares or other specified securities shall be made out of the proceeds of an earlier issue of the **same kind of shares or same kind of other specified securities**.
- *For example:* If equity shares are to be bought-back, then, preference shares may be used for the purpose.

4. Transfer of Reserves to Capital Redemption Reserve (CRR)

A. Rule (Section 69 (1))

- Where a company purchases its own shares out of the **free reserves** or **Securities Premium Account**, a sum equal to the **nominal value (face value)** of shares so purchased shall be **transferred to the Capital Redemption Reserve Account (CRR)**.

B. Purpose of Transfer to CRR

- The transfer to CRR is a mechanism to **lock funds** (or reserve funds).
- CRR is a **non-free reserve**.

C. Restriction on Use of CRR

- CRR **can only be used for issuing Bonus shares**.
- Journal Entry (J.E.):
 - Capital Redemption Reserve Account Debit
 - To Bonus Shares Account
 - Bonus Shares Account Debit

- To Equity Share Capital Account
- As Bonus shares are given, there is **no impact** on free reserves.
- Only CRR reduces and Equity Share Capital increases.

D. Exception to CRR Creation

- Transfer of face value of shares will **not** be done from Free Reserve to CRR when the company issued **new share** (equity or preference) for the purpose of Buy Back.
- No need to lock funds in CRR if the buy-back is funded by a fresh issue of shares.

5. Treatment of Securities Premium

- Securities Premium is **not** a free reserve, but for the purpose of **Buy Back**, it will be treated as a Free Reserve.
- Securities Premium (Free Reserve) can be used for **writing off Premium on Buy Back**.
- Securities Premium is **not to be used** for transfer to CRR (as per the note in the table: *Securities Premium for writing off Premium on BB can be used, for transfer to CRR Not to be used.*)

6. Journal Entries for Buy Back (Conceptual Flow)

- **@ Cancellation of Shares Bought Back:**
 - Equity Share Capital Account Debit (Face Value)
 - Premium on Buy Back Account Debit (Premium Paid)
 - To Equity Share Holders Account / To Equity Shares Bought Back Account
- **@ Payment of Amount Due:**
 - Equity Share Holders Account / Equity Shares Bought Back Account Debit
 - To Cash in Bank Account
- **@ Write off Premium on Buy Back:**
 - Security Premium Account Debit
 - Free Reserves Account Debit (e.g., General Reserve, Profit and Loss, Revenue Reserve, etc.)
 - To Premium on Buy Back Account
- **@ Transfer of Reserves to CRR:** (To the extent of face value of shares bought back)
 - Free Reserves Account Debit
 - To Capital Redemption Reserve Account

7. Provisions and Conditions for Buy Back (Section 68 (2))

No company shall purchase its own shares or other specified securities unless:

- The buy-back is authorised by its **articles of association**.
- A **special resolution** has been passed in a general meeting of the company authorising the buy-back.
 - **Exception:** The special resolution provision does **not** apply where the buy-back is **ten percent or less** of the paid-up equity capital plus free reserves and is authorized by a **Board Resolution** passed at a duly convened meeting of the directors.
- The buy-back must be **equal to or less than twenty-five per cent** of the total paid-up capital and free reserves of the company. (**Resource Test**)
- The buy-back of shares in any financial year must **not exceed 25% of its total paid-up capital and free reserves**. (**Share Outstanding Test**) (*Note: This seems like a repetition or confusion with the 25% of the total number of outstanding shares test, as explained below.*)
- The **ratio of the debt owed** by the company (both secured and unsecured) after such buy-back is **not more than twice** the total of its paid-up capital and its free reserves. (**Debt-Equity Ratio Test**)
 - **Debt** here should include both long-term debt as well as short-term debt.
 - The Central Government may prescribe a higher ratio of the debt than that specified under this clause for a class or classes of companies.
- All the shares or other specified securities for buy-back are **fully paid-up**.
- The buy-back of the shares or other specified securities listed on any recognised stock exchange is in accordance with the regulations made by the Securities and Exchange Board of India (SEBI) in this behalf.
- The buy-back in respect of shares or other specified securities other than those specified in clause (f) is in accordance with the guidelines as may be prescribed.

8. Calculation of Maximum Number of Shares to be Bought Back

The maximum number of shares that can be bought back is the **LEAST** of the number of shares determined by the three tests:

A. Shares Outstanding Test

- Formula: Total No. of equity shares outstanding $\times$ 25%.

B. Resource Test

- Formula: (25% of Paid up Capital + Free Reserves) $\div$ Buy Back Price

C. Debt / Equity Ratio Test (2:1)

- The Debt / Equity ratio post Buy Back should not exceed the ratio of **2:1**.
- **Steps for calculation:**
 1. Compute Total Debt (Secured + Unsecured + Long term + Short term).
 2. Minimum Equity to be maintained Post Buy Back = Total Debt $\div$ 2.
 3. Present Equity = Present Equity Share Capital + Free Reserves.
 4. Maximum Amount Available for Buy Back (By simultaneous equation).
 5. No. of shares that can be bought back = (Maximum Amount Available for Buy Back) $\div$ Buy Back Price.
- **Logic (Debt / Equity Ratio Test):**
 - Equity means Paid up Capital plus Free Reserves.
 - Post Buy Back equity should not fall below the Minimum Equity calculated in step 2.

9. Other Important Provisions

- **Time Restriction:** No offer of the buy-back shall be made within a period of **one year** reckoned from the date of closure of a previous offer of buy-back, if any. This means that there cannot be more than one buy-back in one year.
- **Time Limit for Completion:** Every buy-back shall be completed within **twelve months** from the date of passing the special resolution, or the resolution passed by the board of directors.
- **Methods of Buy Back:** The buy-back may be—
 - From the existing security holders on a **proportionate basis**; or
 - From the **open market**; or
 - By purchasing the securities issued to employees of the company pursuant to a scheme of **stock option or sweat equity**.
- **Declaration of Solvency (Section 68(5)):** Before making such buy-back (after passing the special resolution), the company shall file with the Registrar and the SEBI a **declaration of solvency** in the prescribed form and verified by an affidavit.
 - The declaration must state that the Board of Directors has formed an opinion that the company is capable of meeting its liabilities and will not be rendered insolvent within a period of **one year** of the date of declaration.
 - It must be signed by at least two directors, one of whom shall be the managing director, if any.
 - **Note:** No declaration of solvency shall be filed with the SEBI by a company whose shares are **not listed** on any recognised stock exchange.
- **Extinguishment of Securities (Section 68(6)):** Where a company buys-back its own securities, it shall **extinguish and physically destroy** the securities so bought-back within **seven days** of the last date of completion of buy-back.
- **Restriction on Further Issue (Section 68(7)):** After completion of the buy-back, the company shall not make a further issue of the **same kind of shares** or other specified securities within a period of **six months**, except by way of:
 - Bonus issue.
 - Discharge of subsisting obligations (such as conversion of warrants, stock option scheme, sweat equity, or conversion of preference shares or debentures into equity shares).

- **Maintenance of Register (Section 68(8)):** The company shall maintain a register of the securities so bought, the consideration paid, the date of cancellation, the date of extinguishing and physically destroying of securities, and such other particulars as may be prescribed.
- **Filing of Return (Section 68(9)):** After the completion of the buy-back, the company shall file a return containing particulars relating to the buy-back within **thirty days** of such completion with the Registrar and the SEBI.
 - **Note:** No return shall be filed with the SEBI by a company whose shares are **not listed** on any recognised stock exchange.
- **Penalty (Section 68(10)):** If a company makes default in complying with the provisions of Section 68 or any SEBI regulations, the company may be punishable with a fine of not less than ₹1 Lakh but which may extend to ₹3 Lakh. Every officer in default shall be punishable with imprisonment for up to 3 years or with a fine of not less than ₹1 Lakh but which may extend to ₹3 Lakh or with both.

10. ESOP (Employee Stock Option Plan)

- **Concept:** A company promises to give employees shares for free or at a lower price, if the employee stays with the company for certain years.
- **Journal Entry (Conceptual):**
 - Bank Account Debit (Shares subscribed × Exercise price)
 - ESOP Liability Account Debit (Shares subscribed × (Market Price - Exercise Price)) → *This is the implied entry based on the note, often representing the expense/compensation.*
 - To Equity Share Capital Account (Shares subscribed × Face Value)
 - To Securities Premium Account (Shares subscribed × (Exercise Price - Face Value))

11. Cancellation of Investment in Own Debentures

- **Journal Entry (Conceptual):**
 - Debentures (Liability) Account Debit (Face Value)
 - To Investment in Own Debentures Account (Cost)
 - To Profit on Cancellation (Capital Reserve) (Difference/Profit)

12. Note on Total Debt for Debt/Equity Ratio Test

- While calculating Total Debt for the purpose of the Debt/Equity ratio, one can consider other current or other non-current Liabilities in Debt.
- **Please Note:** If trade payables are given separately, ideally they should not form part of total Debt. Alternative assumptions are also permitted by the ICAI.

Internal Reconstruction (Section 66 of the Companies Act, 2013)1. Introduction

- **Meaning of the term Reconstruction:** The term "Reconstruction" means to rebuild or rearrange.
- **Types of Reconstruction:**
 - **Internal Reconstruction:** Re-organisation within the same entity (Covered in this chapter).
 - **External Reconstruction:** Covered by Accounting Standard 14 (AS 14).
- **Internal Reconstruction:** Internal Reconstruction means restructuring the Balance Sheet position of the company without liquidating the company.
- **Implementing the Scheme:** In order to implement the scheme, a special account is created called the **Capital Reduction Account** or **Reconstruction Account**.
- **Nature of Capital Reduction Account:** This account is a **nominal account** which is created to transfer the:
 - Sacrifice made by shareholders or outside parties.
 - Losses from the reduction of assets.

2. Journal Entries (J.E.)

The Capital Reduction Account is the central account for recording all sacrifices and writing off all accumulated losses and overvalued assets.

2.1 For Increase / Decrease in Value of Assets

Action	Journal Entry (J.E.)
a) For Increase in Asset	Asset Account Debit → To Capital Reduction Account
b) For Decrease in Asset	Capital Reduction Account Debit → To Asset Account

2.2 For Claims Waived off by Creditors / Debenture holders / Outside Parties

- **Journal Entry (J.E.):** Creditor / Debenture / Liability Account Debit → To Capital Reduction Account

2.3 For Contingent Liabilities Cancelled

- **Rule: No entry.**
- **Reason:** Because in the Balance Sheet (B/S), such a liability was **NOT** recorded. Therefore, there is **No entry** on the waiver of this liability.
- **Examples of Contingent Liabilities:**
 1. Arrears of Preference Dividend (Pref. Div).
 2. Capital Expenditure commitment.
 3. Any other contingent liability specified in the question.

2.4 Contingent Liability Paid Off

- **Option 1 (Liability Recognized and Paid):**
 - Capital Reduction Account Debit (for the liability amount) → To Liability Account (for recognizing the liability)
 - Liability Account Debit (for the liability amount) → To Cash in Bank Account (for payment)
- **Option 2 (Paid Directly from Reconstruction Fund):**
 - Capital Reduction Account Debit (for the payment amount) → To Cash in Bank Account

2.5 For Reconstruction Expenses

- **Journal Entry (J.E.):** Capital Reduction Account Debit → To Cash in Bank Account

2.6 For Intangible Assets Appearing in the Balance Sheet

- **a) In case of Goodwill (GW):**
 - **Rule:** Write off, if nothing is mentioned.
 - **Journal Entry (J.E.):** Capital Reduction Account Debit → To Goodwill Account
- **b) For other Intangibles** (Patents, Copyrights, etc.): Do as per the information given in the question.

2.7 For Reduction of Share Capital

- **a) When Face Value of shares is reduced:**
 - **Journal Entry (J.E.):** Equity Share Capital Account Debit (Old Face Value) → To Equity Share Capital Account (New Face Value) → To Capital Reduction Account (Difference/Sacrifice)
- **b) When only Paid Up Value is reduced (Face Value remains the same):**
 - **Journal Entry (J.E.):** Equity Share Capital Account Debit (Reduction amount per share) → To Capital Reduction Account (Total reduction amount)
 - **Reason:** The net entry is passed because the face value of shares is still the original amount (e.g., ₹10).
- **Important Note:** If in the question, no specific information is given as to whether the paid-up value is reduced or the face value is reduced, it is **assumed that the face value is reduced**, and the entry should be passed as per the rule for 2.7(a).

2.8 Write off Debit Balance of Profit and Loss Account (P&L) or Miscellaneous Expenditure or Accumulated Losses

- **Rule:** This is to be done **ALWAYS** whether mentioned or not in the question.
- **Journal Entry (J.E.):** Capital Reduction Account Debit → To Profit and Loss / Miscellaneous Expenditure / Accumulated Losses

2.9 For Any Credit Balance left in Capital Reduction Account (if any)

- **Journal Entry (J.E.):** Capital Reduction Account Debit → To Capital Reserve

3. Other Provisions

3.1 Words "AND REDUCED"

- **Note:** When the Balance Sheet (B/S) is prepared after the Internal Reconstruction scheme, the words **"AND REDUCED"** should be added with the name of the company.

3.2 Subdivision and Consolidation of Shares

- **a) Subdivision of Shares (e.g., ₹10 share divided into 2 shares of ₹5 each):**
 - **Journal Entry (J.E.):** Equity Share Capital Account Debit (Old Face Value) → To Equity Share Capital Account (New Face Value)
- **b) Consolidation of Shares (e.g., 2 shares of ₹10 each consolidated into 1 share of ₹20 each):**
 - **Journal Entry (J.E.):** Equity Share Capital Account Debit (Old Face Value) → To Equity Share Capital Account (New Face Value)
- **Note:** In the case of sub-division/consolidation of shares, the Equity Share Capital **Amount remains the same**, only the number of shares and face value change. Therefore, there is **No Capital Reduction** involved.
- **c) Conversion of Equity Shares to Equity Stock:** This is similar to the consolidation of shares.
 - **Journal Entry (J.E.):** Equity Share Capital Account Debit (Share Capital) → To Equity Stock (Stock Value)

4. Surrender of Shares

- **Concept:** Under this scheme, the shareholders are expected to return a part of their holdings back to the company. The company can either **cancel** or **reissue** these surrendered shares to the creditors / debenture holders to settle their dues.
- **Note:** The amount of sacrifice by shareholders is temporarily held in the Share Surrender Account and is transferred to Capital Reduction only when cancelled or if the balance remains unutilized.

4.1 Journal Entries for Surrender of Shares

- **1) Entry for Surrender of Shares:**
 - Equity Share Capital Account Debit → To Share Surrender Account
- **2) Entry for Reissue:**
 - **a) For Reissue of shares surrendered to creditors or debenture holders:**
 - Shares Surrendered Account Debit → To Equity Share Capital Account
 - **b) Entry for cancellation of liability so settled (The amount of liability settled is the sacrifice):**

- Creditor / Debenture Account Debit → To Capital Reduction Account
- **3) Balance in the Shares Surrendered Account NOT utilized (i.e., shares to be cancelled):**
 - Shares Surrendered Account Debit → To Capital Reduction Account