CA INTER
ADVANCED ACCCOUNTS

SUPER 35 - CONCEPTS
(By CA. Jai Chawla)

BRANCH ACCOUNTS

ACCOUNTING FOR DEPENDENT BRANCHES

Concept 1: Final Account System (Cost Basis)

1. Head Office shall prepare Branch Trading at its own Cost Price.
2. All items Such as Opening Stock of Branch, Branch Purchases (Goods Sent From Head Office), Branch Shortage, Branch Closing Stock shall be recorded at Cost Price (Cost to HO)
3. Branch sales shall be recorded at Actual SP
4. GP amount means Difference of SP & Cost Price
5. If any Item is given in Question at Invoice Price, we shall convert it into Cost First & then record in Trading A/c
6. HO Shall prepare Branch Trading as a working. Therefore, in solution we always use the word:
   "Memorandum Branch Trading A/c"

Dr. Branch Memorandum Trading and Profit & Loss A/c Cr.

Particulars	Amount	Particulars	Amount
To Opening Stock A/c	Cost	By Sales A/c	Sales Value
To Goods sent to Branch A/c	Cost	Less Sales Return	
Less goods returned to HO		By Loss of Stock	Cost
To Direct Purchases A/c	Cost	By Closing Stock	Cost
To Direct Expenses A/c			
To Gross Profit			

Concept 2: Final Account System (Wholesale Price or Invoice Price Method)

Under this system, the profit/loss made by branch is calculated by preparing the Trading and Profit & Loss account on **Wholesale Price basis**. This account is not made as a part of main accounting system and is prepared on Memorandum basis. Since the account is made on **Wholesale price basis**, following points are needed to be note as under:

1) Head Office shall prepare Branch Trading @IP Value
2) Means all items (Except Sales) shall be recorded at IP
3) Sales shall be recorded @ actual figure given
4) While Calculating Closing Stock & Shortage, COGS shall be determined at IP also.
5) Head Office Shall Calculate Stock Reserve (Unrealised Profit) on Opening Stock of Branch, Closing Stock of Branch & Shortage @Branch.

6) Why we are Calculating SR?

(i) On Closing Stock / Shortage

Since Goods are not Sold till year end by Branch & Such Goods are shown at IP Value, it means Head Office has already booked Profit on such Closing Stock & Shortage. Therefore, Head Office shall reverse the profit element included in Closing stock & Shortage.

Head office Books

P&L A/c Dr.

To SR A/c

(ii) On Opening Stock:

Last year this Opening Stock was closing stock & Profit portion was eliminated, in CY assuming it is actually sold by Branch. Therefore, Profit Portion is recognised.

SR A/c Dr.

To P&L A/c

Concept 3: Stock And Debtor System

Under this system, the HO maintains for every branch, Branch stock account, Branch debtor account, other Branch assets/liabilities accounts (individually), Branch expenses accounts (individually), Branch adjustment account and Branch profit & loss account.

1. **Branch Stock Account:** This account records the physical flow of goods between HO and branch at INVOICE PRICE. However, sales are recorded at selling price. The invoice price is the amount at which goods are transferred from HO to branch. The goods can also be transferred by HO to branch at cost to the HO. The basic relationship between the various components is as follows:

   Cost to HO + Mark-up (Loading) = Invoice Price (Cost to branch)

   Or Invoice Price - Mark-up (Loading) = Cost.

2. **Branch Adjustment Account:** This account is a nominal account and calculates the gross profit/loss by branch but is made in a different manner from the trading account. It basically records loading (i.e. difference of invoice price and cost) on opening stock, goods supplied, goods returned, closing stock etc.

3. **Branch Profit & Loss Account:** This account is a nominal account and calculates the net profit/loss earned by branch and is made in the same manner as usual profit and loss account.

4. **Branch Assets/Liabilities Account:** These accounts are made in the usual manner according to the double entry system.

The various journal entries made under this system are as follows:

(1) For goods supplied to branch by the HO.

Branch Stock A/c Dr.
To Goods sent to branch A/c (with invoice price of goods sent)

(2) For goods returned by branch to HO.

Goods sent to branch A/c Dr.
To Branch stock A/c

(3) For goods returned by debtors to branch.

Branch stock A/c Dr.
To Branch debtors A/c

(4) For goods returned by credit customers (debtors) or cash customers direct to HO

Goods sent to branch A/c Dr.
To Branch debtors A/c/Cash A/c

(5) For cash sales made by branch.

Branch Cash/Bank A/c Dr. (With selling price)
To Branch stock A/c

(6) For credit sales made by branch.

Branch debtors A/c Dr. (With selling price)
To Branch stock A/c

To determine gross profit, the excess of invoice price of goods over cost of goods sent to branch is recorded at the time of goods sent. If goods remain unsold at the end of the year stock reserve is created. At the time of sale, the difference of sales price and invoice price of goods sold is recorded. Following six entries are passed for these purposes:

(7) For mark-up (or loading) on opening stock

Stock reserve A/c Dr.
To Branch adjustment A/c

(8) For mark-up (or loading) on closing stock.

Branch adjustment A/c Dr.
To Stock reserve A/c

(9) For mark up on goods sent to branch

Goods sent to branch A/c Dr.
To Branch Adjustment A/c

(10) For mark up on goods received back (returned) by HO

Branch Adjustment A/c Dr.
To Goods sent to Branch A/c

(11) For goods sold at a price higher than Invoice Price
Branch Stock A/c Dr. (with excess of SP over IP)
To Branch Adjustment A/c

(12) For goods sold at a price lower than Invoice Price
Branch Adjustment A/c Dr. (with excess of IP over SP)
To Branch Stock A/c

(13) For Cash/Bank received from branch debtors by branch
Brach Cash/Bank A/c Dr.
To Branch Debtors A/c

(14) For remittance from HO to branch
Branch Cash/Bank A/c Dr.
To Cash/Bank A/c

(15) For remittance from branch to HO
Cash/Bank A/c Dr.
To Branch Cash/Bank A/c

(16) For shortage in branch stock which is considered normal
Branch Adjustment A/c Dr.
To Branch Stock A/c

(17) For shortage in branch stock which is considered abnormal
Branch Adjustment A/c Dr. (with loading on abnormal loss)
Branch P&L A/c Dr. (with cost of abnormal loss)
To Branch Stock A/c

(18) For closing goods sent to branch account
Goods sent to branch A/c Dr.
To Trading/Purchase A/c

Golden Rules under Stock and Debtors Method:

1) **Goods sent to branch accounts** – shall always be shown at cost price.
If it is not at cost (but any amount is at Invoice Price/Cost Price), then in the opposite side show the margin/markup which is over and above cost to make it at cost price. Such margin is known as "**Branch Adjustment Account**".
2) **Branch stock account:** shall always be shown at Invoice Price. If it is not at Invoice price (i.e., shown at other than Invoice Price) then on opposite side show the margin/markup to make it at Invoice price.

3) Under **Branch Stock account,** if closing stock is already recorded then while closing this account, if balancing figure appears on credit side then such balancing figure will be treated as shortage.

Following Journal Entry is passed:

Branch Profit & Loss A/c	Dr.	Cost	
Branch Adjustment A/c	Dr.	Margin	
To Branch Stock A/c			Invoice Price

4) **Opening stock and closing stock under branch stock account** are shown at Invoice Price, therefore stock reserve (margin) shall be calculated shown under Branch Adjustment A/c

5) Under **Branch Stock Account,** if balancing figure appears on the debit side then it is to be treated as surplus (i.e., Goods sold to customer at above Issue Price) hence fully transferred to branch adjustment account.

Concept 4: Debtors Method

- Branch account is nominal account which calculates the profit/loss made by the branch.
- Under this system, entries are recorded assuming the Branch is the Debtor of HO.
- Here, only the transactions between HO and Branch are to be recorded (except one special transaction), i.e. any transaction between branch and outside party is to be ignored while preparing branch account.
- While preparing Branch A/c under this method, balances of various accounts such as stock a/c, debtor's a/c, cash a/c etc. may be missing and it is not possible to complete the Branch A/c without knowing such required missing figures.
- Such missing figures/balances can be found out with the help of 'Stock and Debtors' method and hence Stock and Debtors method is also prepared to complete the Branch A/c under Memorandum basis and only account prepared under double entry basis is the 'Branch A/c'.

The various journal entries made under this system are as follows:

(1) For goods supplied to branch from HO

Branch A/c	Dr.	
To Goods sent to branch A/c		(with invoice price, if any)

(2) For goods returned by branch to HO

Goods sent to branch A/c	Dr.	
To Branch A/c		(with invoice price, if any)

(3) For goods returned direct to HO (Special Transaction)

Credit Customers (Debtors):

Goods sent to branch A/c	Dr.	
To Branch A/c		

Cash Customers:

Goods sent to branch A/c	Dr.	and	Branch A/c	Dr.
To Branch A/c			To Cash A/c	

(4) For remittance from HO to branch for expenses or for any purpose

Branch A/c	Dr.
To Cash/Bank A/c	

(5) For cash received by HO from branch

Cash/Bank A/c	Dr.
To Branch A/c	

(6) To remove loading on opening stock and closing stock

Opening Stock:

Stock Reserve A/c	Dr.
To Branch A/c	

Closing Stock:

Branch A/c	Dr.
To Stock Reserve A/c	

(7) Following Transactions Shall not be recorded in Branch A/c: -

(i) Sale made by Branch
(ii) Expenses Incurred by Branch
(iii) Shortage of Goods @Branch
(iv) Cash collection from Debtors by Branch
(v) Sales return to Branch

(8) Apart from above transaction which are to be recorded in Branch A/c, HO Shall maintain Opening & Closing Balances of Branch Assets & Branch Liabilities to prepare Consolidated Balance Sheet of Business

(a) To Maintain Closing Branch Assets: -

Branch Stock A/c	Dr.
Branch Cash A/c	Dr.
Branch Debtors A/c	Dr.
Branch Other Assets A/c	Dr.
To Branch A/c	

(b) To Maintain Closing Branch Liabilities: -

Branch A/c	Dr.
To Branch Liabilities A/c	

(c) To eliminate Branch Assets & Branch Liabilities in the next year (i.e. Opening Branch Assets & Opening branch Liabilities): -

(i)	Branch A/c	Dr.

To Branch Stock A/c
To Branch Debtors A/c
To Branch Cash A/c
To Branch Other Asset A/c

(ii) Branch Liabilities A/c Dr.
To Brach A/c

(9) Under this Method, if goods are recorded at IP Value, then on Opposite side of Branch A/c, Loading shall be recorded. So that the Ultimate effect can be Shown at Cost Only.

(10) Cash remittance is Very Important Figure to prepare Branch A/c. If it is missing in question, then it is to be found out by preparing Branch Cash A/c in working Note.

(11) If any Opening/Closing Balances are missing Like Stock / Debtors / Cash / Other Assets we shall prepare working note of that A/c

Question 1: (Master Problem)

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

Cash sales at IP

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

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

SOLUTION

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

Memorandum Branch Trading and P&L A/c

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

CONSOLIDATION (AS 21)

Concept 5: Dividend Paid or Declared by Subsidiary (Treatment in AOP)	**Case 1: Dividend is Paid during the year, assume this dividend belongs to PY (hence entry must have been passed)** **Step 1:** Add back in Post Acquisition column of AOP **Step 2:** Apply Time Adjustment of Post Acquisition Column **Step 3:** Deduct in Pre-acquisition Column or Post Column depending on the period of Dividend and DOA **Case 2: Dividend is declared at the end of Current year, assume it belongs to Current Year Only (hence entry is not yet passed)** Directly Deduct after Time Adjustment in Pre/Post Column depending upon the DOA. Other Important Points for Dividend Paid by Subsidiary: ➢ There are two types of dividends, Interim dividend and Final dividend. ➢ Interim dividend always belongs to Current Year ➢ Treatment of Both types of dividend in AOP is same.
Concept 6: Dividend Received by Holding Company from Subsidiary Co.	If the dividend belongs to Pre-acquisition period, it is Pre-acquisition dividend. If dividend belongs to Post acquisition period, it is Post acquisition dividend 1) **Pre-acquisition Dividend Received by Holding** ➢ It must be deducted from the cost of investment of holding co. ➢ If it is wrongly credited to Profit and Loss of Holding Co. then it should be deducted from Consolidated P&L working and deducted to Cost of Investment under Cost of Control working. ➢ Always assume that, Pre-acquisition dividend received by parent is wrongly credited to its P&L A/c

	2) **Post Acquisition Dividend received:** It is already credited to Profit and Loss of Holding co. which is correctly done hence no further treatment required.
Concept 7: Revaluation of Assets of Subsidiary	➢ As per AS 21, Net Assets of subsidiary to be recognised at Fair Value in consolidated financial statement. ➢ Revaluation of Assets of subsidiary shall be done on Date of Acquisition only. Apply following steps after Time Adjustment: **Step 1: Calculate Revaluation Gain/loss on Assets as under** Book Value of Asset on the date of Acquisition Less: Market Value of Assets on the date of Acquisition **Step 2: Revaluation Gain/loss is treated as Pre-acquisition gain/loss** Hence it should be added or deducted in Pre column **Step 3: Calculate Depreciation effect on Asset due to Revaluation for post-acquisition period** Depreciation that should be charged on MV of asset from DOA to BS date Less: Depreciation actually charged by Subsidiary in SFS from DOA to BS date **Step 4: Treatment of Depreciation effect calculated as above** If Additional Depreciation: Deduct in Post-acquisition column in AOP If Reversal of Depreciation: Add in Post acquisition column in AOP
Concept 8: Unrealized Profit on Unsold Stock in Inter Co. Transaction	Inter company transaction means transactions between holding and subsidiary for purchase/sale of Goods. **Example:** Suppose Holding co. has sold goods costing 10,000 to subsidiary at 15,000. Out of which, 50% goods are sold by subsidiary to its customers. Now subsidiary co. shows remaining 50% stock (i.e. 7,500) in its Balance Sheet.

	Holding co. while preparing consolidated financial statements shall consolidate the stock of subsidiary at 7,500 and eliminate 2,500 profit earned by holding and included in the stock. **In case of Downstream Transaction (Goods Sold by H to S):** Consolidated Profit and Loss A/c Dr. To Stock A/c **In case of Upstream Transaction (Goods Sold by S to H):** AOP (Post Acquisition Column) A/c Dr. To Stock A/c **Note:** in case of loss, above entries will be reversed.
Concept 9: Analysis of Profit and Time Adjustment	➢ For Cost of Control, we need Net Assets (ESC + R&S Balance) as on DOA ➢ On DOA, Equity Share Capital must be given, But Balance of Reserves & Surplus on DOA may be missing. ➢ The difference between balances of R&S as on Beginning of year and End of Year is the Profit for the Year and it will be shown under Post Acquisition Column of AOP. ➢ Time Adjustment for Post Acquisition Profit Column is required so that Reserves & Surplus Balance as on DOA must be determined. ➢ For making Time Adjustment **we will always assume that profit of each month is same**. Following points should also be taken care of while doing time adjustment of Revenue Profit: ✓ Take Normal profit always for Time Adjustment (Normal profit means Profit After Tax excluding the effect of Abnormal Gains/Losses) ✓ Normal Profit should be after Tax. ✓ But Before Dividend ✓ Before Revaluation Gain/Loss ✓ Before Un-realised Gain/Loss ✓ Before Bonus Issue

Concept 10:
CONSOLIDATED PROFIT AND LOSS STATMENT

1) All Incomes and expenses of Holding and Subsidiary are merged in Consolidated Profit and loss statements.
2) In the year of acquisition, Incomes and Expenses of Subsidiary co. shall be considered from the date of acquisition (i.e. for Post acquisition period). Hence, the proportionate amount of Income and Expenses of subsidiary shall be taken.
3) Final Net Profit of Group is allocated between Share of Minority Interest and Share of Owners of Parent.
4) Share of Minority Interest in the Net Profit of the group can be calculated with the Help of AOP. It is share in Post Acquisition Profit of Subsidiary co.

Question 2: (Consolidated Profit and Loss A/c)

Statement of profit & Loss year ending 31/3/24

Particular	H Ltd.	S Ltd.
Revenue form Operation	50,00,000	30,00,000
Other income	4,50,000	2,00,000
	54,50,000	**32,00,000**
Cost of Material consumed	18,00,000	9,00,000
Changes in Inventories	(3,00,000)	(1,80,000)
Employee Benefit Expenses	6,00,000	5,00,000
Finance cost	5,50,000	3,80,000
Other expenses	11,00,000	8,00,000
	37,50,000	**24,00,000**
Profits before Taxes	17,00,000	8,00,000
(-) Tax expenses	(5,00,000)	(2,00,000)
Profit After Taxes	12,00,000	6,00,000
Less: Dividend paid	(2,50,000)	(1,00,000)
Retained Earnings	9,50,000	5,00,000

(1) Date of Acquisition is 1/7/23
(2) Acquired 75% of equity
(3) During the year: -
  (a) Goods Sold by H to S for Rs.4,00,000
  (b) Interest paid by S to H Rs. 50,000
(4) Opening inventory on 1/7 of S is 5,00,000 & Closing Inventory as on 31/3 of S is 6,20,000

SOLUTION:

Consolidated statement of Profit & Loss of group for the year ended 31/3/24

Particular	H	S	Contra	Total
Revenue from Operation	5,00,000	22,50,000	(4,00,000)	68,50,000
Other Income	4,50,000	1,50,000	(50,000)	5,50,000
Total (A)	**54,50,000**	**24,00,000**	**(4,50,000)**	**74,00,000**
Cost of material consume	18,00,000	6,75,000	(4,00,000)	20,75,000

Changes in Inventory	(3,00,000)	(1,20,000)	-	(4,20,000)
Employment Benefit Expenses	6,00,000	3,75,000	-	9,75,000
Finance cost	5,50,000	28,5000	(50,000)	78,5000
Other Expenses	11,00,000	6,00,000	-	17,00,000
Total (B)	**37,50,000**	**18,15,000**	**(4,50,000)**	**51,15,000**
Profit Before tax (A.B)	17,00,000	5,85,000		22,85,000
(-) Tax expenses	5,00,000	1,50,000	-	(6,50,000)
Profit after Tax	12,00,000	4,35,000	-	16,35,000
(-) Dividend declared	(2,50,000)	(1,00,000)	75,000	(2,75,000)
Retained earnings	9,50,000	3,35,000	75,000	13,60,000
Retained earnings attributable to owners of Parent (B/F)				12,76,250
R/E attributable to M/I (3,35,000 X 25%)				83,750

AMALGAMATION (AS 14)

Concept 11:

CALCULATION OF PURCHASE CONSIDERATION

Purchase Consideration can be calculated in different ways. However, the most common methods are as under:

(a) Exchange Ratio Method

(b) Net Assets Method

Exchange Ratio Method:

Here we need Exchange Ratio (Swap Ratio) for calculation of PC. Exchange ratio is a ratio for exchange of No. of Shares. It can be given in the question.

If it is missing in question, then we shall use Deemed Exchange Ratio as under:

Fair Value of Share of Transferor ÷ Fair Value of Share of Transferee

The above Fair values can be Intrinsic Values, Market Values or any other values given in the question.

In absence of any Information, we will use Intrinsic Values.

Purchase consideration based on Net Assets Value:

- If Some Asset/Liabilities are not taken over then we shall not consider such Asset or Liabilities while calculating Purchase consideration **(Refer Example 6)**
- If there are any unrecorded Asset/Liabilities they may also be taken over & to be considered in calculation of Purchase Consideration. **(Refer Example 6)**
  If Goodwill value is given in the Question, then Goodwill shall also be taken for the purpose of calculation of Purchase Consideration. **(Refer Example 8)**
- Sometimes Question asks to calculate Purchase consideration based on Intrinsic Values, If so then we shall assume that all Asset & all liabilities are being taken over.
- **How to Calculate Intrinsic Value:**
  Market Value of All Assets
  (+) Goodwill if Any
  (-) All Liabilities
  (-) PC to PSH
  = Net Assets for Equity Shareholders ÷ No of Equity Shares

Concept 12:

PAYMENT TO DEBENTURE HOLDERS (Settlement of Liability)

- Purchase Consideration is payable to Equity Shareholders & Preference Shareholders only.
- Anything payable to Debenture holders or any other party is not Purchase Consideration.

Question 3: (Discharge of Purchased Consideration)

B/S (extract) of Transferor

Equity Share Capital (10/-) 2,00,000 no.	20,00,000
9% Preference Share Capital (100/-) 2,500 no.	2,50,000
11% Debenture (100/-)	15,00,000

Transferee shall discharge following:

(1) Cash ₹ 3,00,000 to Equity Share Holders
(2) 3 Equity Share against every 10 equity share of Transferor. Market Value Per share of Transferee = 18/-
(3) New 12% Debenture to given to Equity shareholders of Transferor of 5,00,000/-
(4) Preference share of Transferor will get equal no of preference share in Transferee to be issued at 10% premium (Face Value 100/-)
(5) 11% Debenture of Transferor will get new 12% Debenture of Transferee at a value at which same Interest Amount should be received.

Calculate Purchased Consideration

SOLUTION:

Calculation Purchased Consideration

	Payment to	Payment In	Working	Amount
(a)	Equity Shareholders	(i) Cash	given	3,00,000
		(ii) Equity Shares	2,00,000/10 x 3	10,80,0000
		(iii) 12% Debenture	given	
(b)	Preference Shareholders	Preference Share	2,500 x 110	2,75,000
	Total			**21,55,000**

Payment to Debenture holders: (Not a part of PC)

Issue of new 12% Debenture = Old Interest amount/New Rate = 1,65,000÷12% = 13,75,000

Question 4:

Transferor has an outstanding 7% Debenture of Rs. 12,00,000. Transferee will settle these Debenture at 20% Premium by Issue of New 8% Debenture at 25% premium.

SOLUTION:

Settlement Value to Debenture holders of Trasferor = 12,00,000 + 20% = 14,40,000 (Payable Value)

No. of New 8% Debenture to be issue against settlement = 14,40,000/125 = 11,520 no.

2nd Entry		
Asset A/c	Dr.	
To Debenture Holders		14,40,000
(Payable value always)		
4th Entry (Settlement)		
Debenture Holders	Dr.	14,40,000
To 8% Debenture		11,52,000
To Securities Premium		2,88,000

Question 5:

9% Debenture of 10,00,000 to be settled at 20% premium, by issue of new 10% Debenture to be issued at 25% Discount.

SOLUTION:

Payable value = 10,00,000 + 20% = 12,00,000

New 10% Debenture no. against settlement = 12,00,000 ÷ 75 = 16,000 no.

Debenture holders A/c	Dr.	12,00,000	
Discount A/c	Dr.	4,00,000	
To 10% Debentures			16,00,000

Question 6:

6% Debenture of ₹ 7,20,000 to be discharged at 10% Discount by issue of equity share @ 12/- per share. Face Value = 10/-

SOLUTION:

Payable Value to Debenture holders = 72,00,00 – 10% = 6,48,000

New Equity No. to be settled = 6,48,000/12 = 54,000

Debenture Holder	Dr.	6,48,000	
To Equity Share Capital			5,40,000
To Securities Premium			1,08,000

BUYBACK OF EQUITY SHARES

Concept 13:

HOW TO CALCULATE MAXIMUM PERMISSIBLE BUYBACK

Here we need to conduct three important Tests for calculating Maximum permissible Buyback in accordance with Companies Act, 2013. These Tests are:

1. **Share Outstanding Test:** Maximum no. of buyback should not excess 25% of total Outstanding Equity Shares immediately before buyback.
2. **Resource Test:** Maximum Amount of Buyback should not excess 25% of Total Equity Paid up capital plus Free Reserves including Securities premium.
3. **Debt Equity Test:** After the Buyback of Equity, Debt-Equity Ratio should not exceed 2:1. (Here equity means ESC + PSC + Free Reserves)

Note: Debt means All Borrowings (Long term + Short Term) including Debentrues and Bank Loans but does not include any other current liabilities such as Creditors/BP.

Question 7: (on Maximum Permissible Buyback):

The Buyback Price is Rs. 25/-

Outstanding Equity Share Capital (10/- each)	35,00,000
General Reserve	25,00,000
Profit & Loss Balance	11,50,000
Securities Premium	17,50,000
Debentures	60,00,000
Bank Loan (Non-Current Liability)	70,00,000
Current Maturity of Bank Loan	15,00,000
Sundry Creditors	25,00,000
Investment allowance Reserve	10,00,000

SOLUTION:

(1) Shares outstanding Test: -

Total Outstanding No. of Equity Shares x 25%

3,50,000 x 25% = **87,500 No.**

(2) Resources Test: -

(Total Paid-up Capital + Free Reserve) x 25% = Maximum Amount of Buyback

89,00,000 x 25% = 22,25,000/-

Therefore, Maximum No. of Buyback = 22,25,000/25 = **89,000 no.**

(3) Debt Equity Test: -

Debt Equity Ratio should not exceed 2:1 after Buyback

Debt (after buyback) = 1,45,00,000

Equity after Buyback Should be = 1,45,00,000 / 2 = 72,50,000

Current Equity – Buyback effect = Equity after Buyback

Assume No. of shares to be bought back is X

Therefore, Buyback Effect = Face Value (10X) + Premium on BB (15x) + CRR to be Created equal to FV out of FR (10X) = 35X

89,00,000 – 35x = 72,50,000

X = **47,142 No.**

Note: for the purpose of this chapter, equity means Share Capital + Free reserves + Securities Premium

(Capital Redemption Reserve will not be a part of Equity)

Conclusion: Hence Final No. of Shares to be bought back should not be more than 47142 No. (whichever is lower in above three tests)

AS 2 – VALUAITON OF INVENTORIES

Concept 14:

CALCULATION OF COST OF RM CONSUMED AND COST OF FINISHED GOODS PRODUCED

Cost Per Unit of RM Consumed	Total Purchase Value (Outflow in Rs.) Total Units Purchased – Normal wastage
Bifurcation of Units Purchased	Total Units Purchased (-) Normal Wastage **(=) Remaining Units (including Abnormal loss)** Out of above Remaining units, following working is required: 1. Cost of Good Units (Consumed or Sold): No. of Units Consumed/Sold **X** Cost per Unit as above 2. Cost of Closing Stock of RM/SIT: No. of Units **X** Cost per Unit as above 3. Abnormal Loss: No. of Units **X** Cost per Unit as above
Cost of FG Produced	**Particulars** — **Working** Cost of RM Consumed — Opng. RM (No.) (+) Purchased (No.) (-) Closing (No.) Consumed (No.) **X** Cost Per Unit Wages/Labour Cost — Given in Question Fixed Production O/H Cost — F O/H Cost per Unit **(X)** Units Consumed/Produced Fixed O/H cost per unit: - Total Fixed O/H ÷ Higher of Actual Capacity or Normal Capacity Variable O/H Cost — Var. O/H Cost Per Unit **(X)** Units Consumed/Produced

	Total Cost of FG Produced **÷** **Finished Goods Produced (No.)** **Note:** if nothing is specified in the question always assume that for every 1 unit of Raw Material – 1 unit of FG is produced

Question 8:

Particulars		**Kg.**	**Rs**
Opening Inventory:	Finished Goods	1,000	25,000
	Raw Materials	1,100	11,000
Purchases of Raw Material		10,000	1,00,000
Labour			76,500
Overheads (Fixed)			75,000
Sales		10,000	2,80,000
Closing Inventory:	Raw Materials	900	
	Finished Goods	1200	

The expected production for the year was 15,000 kg of the finished product. Due to fall in market demand the sales price for the finished goods was Rs. 20 per kg and the replacement cost for the raw material was Rs. 9.50 per kg on the closing day. You are required to calculate the closing inventory as on that date.

SOLUTION:

Calculation of cost for closing inventory

Particulars	**Rs**
Cost of Purchase (10,200 x 10)	1,02,000
Direct Labour	76,500
Fixed Overhead 75,000X10,200/15,000	51,000
Cost of Production	2,29,500
Cost of closing inventory per unit (2,29,500/10,200)	Rs 22.50
Net Realisable Value per unit	Rs 20.00

Since net realisable value is less than cost, closing inventory will be valued at Rs. 20.

As NRV of the finished goods is less than its cost, relevant raw materials will be valued at replacement cost i.e. Rs. 9.50.

Therefore, value of closing inventory: Finished Goods (1,200 x 20) Rs. 24,000
Raw Materials (900 x 9.50) =Rs. 8,550
Total =Rs. 32,550

AS 7 – CONSTRUCTION CONTRACTS

Concept 15:

How to Solve the Full Question Covering Maximum adjustments of AS 7?

Step 1	**Calculate % of Completion of Contract (PCM):** Cost Incurred till date (work certified + work uncertified) X 100 Total Estimated Cost of Project
Step 2	**Recognise Contract Revenue & Cost and Calculate Contract Profit/loss:** Contract Revenue = Total Price x PCM (%) = XXX (less) Revenue Recognised till last year Contract Cost = Work Certified + Uncertified = XXX **Contract Revenue (-) Contract Cost = Contract Profit/loss**
Step 3	**Recognise Provision of Foreseeable Loss:** (if total contract cost is expected to exceed contract revenue) Total Contract Revenue XXX (-) Total Contract Cost of Project XXX **Total Loss in a Contract XXX** (-) Loss already recognised XXX (+) Profit already recognised XXX **Provision for Foreseeable Loss XXX**
Step 4	**Calculation of "Amount due from Customer or due to Customer"** Contract Cost incurred till date XXX (+) Profit Recognised till date XXX (-) Loss Recognised Till date XXX (-) Progress Billings (XXX) **Amount Receivable or (Payable) from/to Customer XXX/(XXX)** Progress Billing = Payment Received + Payment Retained by Client

Question 9:

Sarita Construction Co. obtained a contract for construction of a dam. The following details are available in records of company for the year ended 31st March, 2018:

	Rs In Lakhs
Total Contract Price	12,000
Work Certified	6,250
Work not certified	1,250
Estimated further cost to completion	8,750
Progress payment received	5,500
Progress payment to be received	1,500

Applying the provisions of Accounting Standard 7 "Accounting for Construction Contracts" you are required to compute:

(i) Profit/Loss for the year ended 31st March, 2018.

(ii) Contract work in progress as at end of financial year 2017-18.

(iii) Revenue to be recognized out of the total contract value.

(iv) Amount due from/to customers as at the year end.

Solution:

(i)	**Loss for the year ended, 31st March, 2018**	**(Rs in lakhs)**
	Amount of foreseeable loss	
	Total cost of construction (6,250 + 1,250 + 8,750)	16,250
	Less: Total contract price	(12,000)
	Total foreseeable loss to be recognised as expense	4,250

According to AS 7, when it is probable that total contract costs will exceed total contract revenue, the expected loss should be recognised as an expense immediately. Loss for the year ended, 31st March, 2018 amounting Rs 4,250 will be recognized.

(ii)	**Contract work-in-progress as on 31.3.18**	**(Rs in lakhs)**
	Contract work-in-progress i.e., cost incurred to date are Rs 7,500 lakhs:	
	Work certified	6,250
	Work not certified	1,250
		7,500

(iii) **Proportion of total contract value recognised as revenue**

Cost incurred till 31.3.18 is 46.15% (7,500/16,250×100) of total costs of construction.

Proportion of total contract value recognised as revenue:

46.15% of Rs 12,000 lakhs = Rs 5,538 lakhs

(iv) **Amount due from/to customers at year end**

(Contract costs + Recognised profits – Recognised Losses) – (Progress payments received + Progress payments to be received)

= (7,500 + Nil – 4,250) – (5,500 + 1,500) Rs in lakhs

= [3,250 – 7,000] Rs in lakhs

Amount due to customers = Rs 3,750 lakh

AS 10 – PROPERTY PLANT AND EQUIPMENT

Concept 16:
CALCULATION OF COST OF PPE

Question 10:

On 1 April 20X1, Sun Ltd purchased some Land for Rs.10000 (including legal costs of Rs 1000) in order to construct a new factory. Construction work commenced on 1st May 20X1. Sun ltd incurred the following costs in relation with its construction:

- Preparation and levelling of the land – Rs. 300
- Purchase of materials for the construction – Rs. 6080 in total.
- Employment costs of the construction workers – Rs. 200 per month.
- Overhead costs incurred directly on the construction of the factory – Rs. 100 per month.
- Ongoing overhead costs allocated to the construction project using the company's normal overhead allocation model – Rs. 50 per month.
- Income received during the temporary use of the factory premises as a car park during the construction period – Rs. 50.
- Costs of relocating employees to work at the new factory – Rs. 300
- Costs of the opening ceremony on 31st January 20X1 – Rs. 150

The factory was completed on 30th November 20X1 and production began on 1 February 20X2. The overall useful life of the factory building was estimated at 40 years from the date of completion. However, it is estimated that the roof will need to be replaced 20 years after the date of completion and that the cost of replacing the roof at current prices would be 30% of the total cost of the building.

At the end of the 40-year period, Sun Ltd has a legally enforceable obligation to demolish the factory and restore the site to its original condition. The directors estimate that the cost of demolition in 40 years' time (based on prices prevailing at that time) will be Rs 20000. An annual risk adjusted discount rate which is appropriate to this project is 8%. The present value of Rs 1 payable in 40 years' time at an annual discount rate of 8% is Rs. 0.046

The construction of the factory was partly financed by a loan of Rs. 17500 taken out on 1 April 20X1. The loan was at an annual rate of interest of 6%. During the period 1 April 20X1 to 31 August 20X1 (when the loan proceeds had been fully utilised to finance the construction), Sun Ltd received an investment income of Rs 100 on the temporary investment of the proceeds.

Required:

Compute the carrying amount of the factory in the Balance Sheet of Sun Ltd on 31st March 20X2. You should explain your treatment of all the amounts referred to in this part in your answer.

SOLUTION:

Computation of the cost of the factory

Description	Included in P.P.E.	Explanation
Purchase of land	10,000	Both the purchase of the land and the associated legal costs are direct costs of constructing the factory.
Preparation and leveling	300	A direct cost of constructing the factory
Materials	6,080	A direct cost of constructing the factory
Employment costs of construction workers	1,400	A direct cost of constructing the factory for a seven-month period
Direct overhead costs	700	A direct cost of constructing the factory for a seven-month period
Allocated overhead costs	Nil	Not a direct cost of construction
Income from use as a car park	Nil	Not essential to the construction so recognised directly in profit or loss
Relocation costs	Nil	Not a direct cost of construction
Opening ceremony	Nil	Not a direct cost of construction
Finance costs	612.50	Capitalise the interest cost incurred in as even month period (purchase of land would not trigger off capitalisation since land is not a qualifying asset and it is separate from building. Construction started from 1st May)
Investment income on temporary investment of the loan proceeds	(100)	offset against the amount capitalized
Demolition cost recognised as a provision	920	Where an obligation must recognise as part of the initial cost at PV.
Total cost of Land & Building	**19,912.50**	
Computation of accumulated depreciation		
Total depreciable amount	9,912.50	All of the net finance cost of 512.50 (612.50 – 100) has been allocated to the depreciable amount. Also acceptable to reduce by allocating a portion to the non- depreciable land element principle

Depreciation must be in two parts: Depreciation of roof component Depreciation of remainder	49.56 57.82	9,912.50x 30% x 1/20 x 4/12 9,912.50x 70% x 1/40 x 4/12
Total depreciation	107.38	
Computation of carrying amount	**19,805.12**	**19,912.50 – 107.38**

Concept 17:
REPLACEMENT OF COMPONENT OF PPE

Question 11:

Bharat Infrastructure Ltd. acquired a heavy machinery at a cost of ₹ 1,000 lakhs, the breakdown of its components is not provided. The estimated useful life of the machinery is 10 years. At the end of Year 6, the turbine, which is a major component of the machinery, needed replacement, as further usage and maintenance was uneconomical. The remainder of the machine is in good condition and is expected to last for the remaining 4 years. The cost of the new turbine is ₹ 450 lakhs. Give the accounting treatment for the new turbine, assuming SLM Depreciation and a discount rate of 8%.

Solution:

As per AS 10, Property, Plant and Equipment, the derecognition of the carrying amount of components of an item of Property, Plant and Equipment occurs regardless of whether the cost of the previous part / inspection was identified in the transaction in which the item was acquired or constructed. If it is not practicable for an enterprise to determine the carrying amount of the replaced part/ inspection, it may use the cost of the replacement or the estimated cost of a future similar inspection as an indication of what the cost of the replaced part/ existing inspection component was when the item was acquired or constructed.

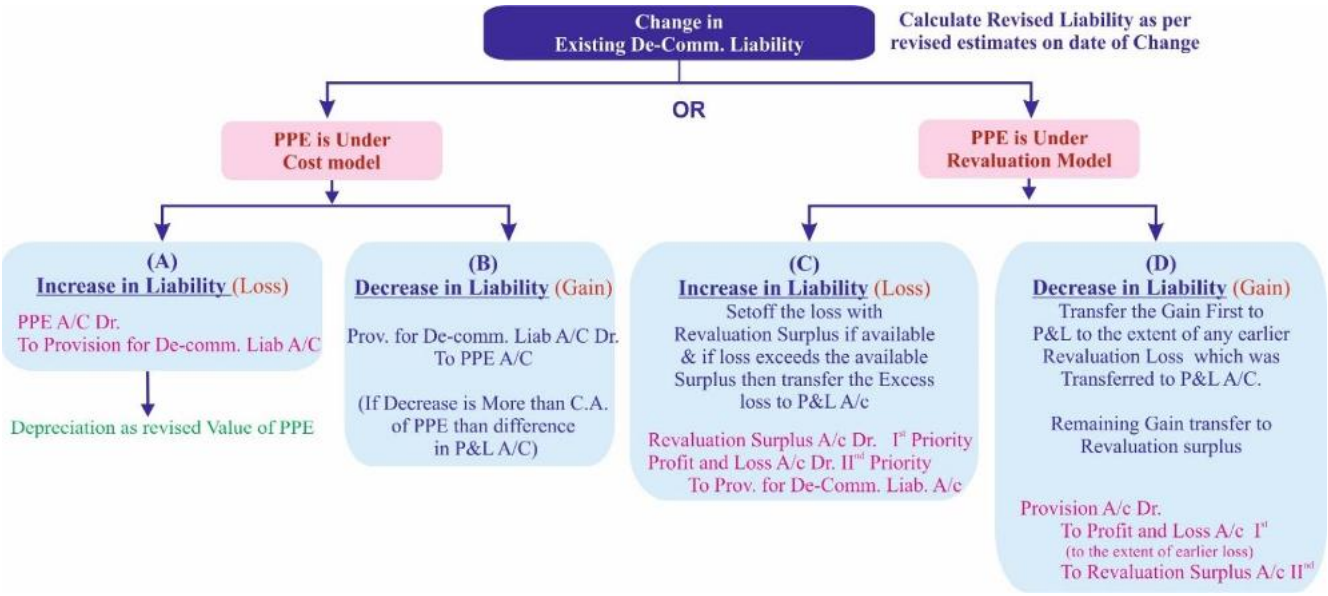
In the given case, the new turbine will produce economic benefits to Bharat Infrastructure Ltd. and the cost is measurable. Since the recognition criteria is fulfilled, the same should be recognised as a separate item of Property, Plant and Equipment. However, since the initial breakup of the components is not available, the cost of the replacement of ₹ 450 lakhs can be used as an indication based on the guidance given above, discounted at 8% for the 6-year period lapsed.

Thus, estimate of cost 6 years back = ₹ 450 lakhs ÷ 1.08^6 = ₹ 283.58 lakhs Current carrying amount of turbine (to be de-recognised) = Estimated cost ₹ 283.58 lakhs (–) SLM depreciation at 10% (useful life 10 years) for 6 years ₹ 170.15 lakhs= ₹ 113.43 lakhs. Hence revised carrying amount of the machinery will be as under:

Particulars	₹ in lakhs
Historical Cost [₹ 1,000 lakhs (–) SLM Depreciation at 10%	400.00

(10 year life) for 6 years]	
Add: Cost of new turbine	450.00
Less: Derecognition of current carrying amount of old turbine	(113.43)
New Carrying Amount of Machinery	**736.57**

Concept 18:
CHANGES IN EXISTING DECOMMISSIONING, RESTORATION AND OTHER LIABILITIES



AS 11 – THE EFFECTS OF CHANGES IN FOREIGN EXCHANGE RATES

Concept 19:

PARA 46 OF AS 11 ON LTFCMI

(a) Corporate/Non-Corporate entities can opt for the application of this Para & option is irrevocable.

(b) FCMI of Long Term in nature (whose realization/payment is beyond 12 months from the date of original transaction) will be converted using closing rate in subsequent recognition.

Exchange difference arising from above point will be recognized as follows:

- Transfer Exchange difference to value of **Depreciable Fixed Assets (PPE)** if long term monetary item was taken to finance such Depreciable F.A. (i.e., to be capitalized if debit difference and subtracted if credit difference) **(Refer Example No. 4)**
- Transfer Exchange difference to **Foreign Currency Monetary Items Translation Diff a/c** (FC MIT Diff a/c) if Long Term Monetary Item has no relation with Depreciable Fixed Assets. **(Refer Example No. 5)**
- **FC MIT Diff a/c** will be **amortised** over the balance period of such long-term assets or liability, by recognition as income or expense in each of such periods **(written off in periods equally till the life of LTFCMI.)**

The balance in FC MIT Diff a/c (debit or credit) should be shown on the "Equity and Liabilities" side of the balance sheet under the head "Reserves and Surplus" as a separate line item. (as decided by the council of ICAI)

Question 12:

Vsmart Ltd. took a Foreign Currency Loan of $1,00,000 to purchase machine of the same amount. On 1st April, 2022 Loan is of 5Years. To be repaid in lumpsum after 5 Years.
Depreciation Rate is 10%
Exchange rates are as follows:
On 1/4/22 - $1 = ₹ 78

On 31/3/23 - $1 = ₹ 82
On 31/3/24 - $1 = ₹ 80.5
Show A/c as per AS 11 in following cases:
(a) Without PARA 46
(b) With PARA 46

Solution:

1) Initial Recognition:

Foreign Currency should recognise at the rate prevailing on transaction Date (i.e. SPOT Rate) i.e. $1 = ₹ 78
Transaction Value = $1,00,000 x 78 = 78,00,000
1/4/22

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

(Note: assuming machine is measured at cost always)
(Note: Foreign Currency Loan is a LTFCMI)

2) Subsequent measurement:

Case 1: without PARA 46

Exchange Difference due to Subsequent measurement shall be transfer to Profit & Loss A/c
1st Year end: 31/3/23
Foreign Currency Loan Should be = $1,00,000 x 82 = 82,00,000
Exchange Difference (Loss) = 4,00,000
31/3/23

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

2nd Year end: 31/3/24
Foreign Currency Loan Should be = $1,00,000 x 80.5 = 80,50,000
Exchange Difference (Gain) = 82 – 80.5 = 1,50,000

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

Case 2: with PARA 46

Exchange Difference should be adjusted to the cost of machine
31/3/23
Exchange Difference (Loss) = 4,00,000

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

Depreciation @10& = 82,00,000 x 10% = 8,20,000

Remaining Balance of Machine = 73,80,000
31/3/24
Exchange Difference (Gain) = 1,50,000
Deduct From Machines Book Value

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

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

Question 13:

Vsmart Ltd. took a loan of $75,000 on 1/4/22 when $1 = ₹ 78. Loan is utilized for working capital requirement loan is of 6 Years. Principal repayment equally every year.

1st year end - $1 = ₹ 81.30
2nd year end - $1 = ₹ 82.15
3rd year end - $1 = ₹ 82
4th year end - $1 = ₹ 81.50
5th year end - $1 = ₹ 81.90
6th year end - $1 = ₹ 82

Apply PARA 46 of AS 11:

Solution:

1) Initial Recognition:

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

2) Subsequent Measurement:

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

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

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

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

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

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

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

Concept 20:

Accounting Treatment of Forward Exchange Contracts:

FEC have been classified into two types for the purpose of accounting treatment:

(1) Forward exchange contracts entered for managing risk (Hedging)

(2) Forward exchange contracts entered for trading or speculation.

Forward Exchange Contracts entered For Managing Risk (Hedging):

- Any forward premium/discount should be **amortized/recognized over the tenor** of contract in the profit and loss a/c.
- If the forward contract is cancelled or renewed, the profit or loss arising on cancellation or renewal is recognized in the profit & loss statement for the period.

Forward Exchange Contracts entered for Trading or Speculation:

- **Here forward premium/discount should be ignored.**
- At each balance sheet date the value of contract is marked to market, **any gain or loss on the contract is recognized immediately.**
- Upon sell of forward contract, any profit or loss to be recognized **immediately in the statement of profit & loss.**

AS 13 – ACCOUNTING FOR INVESTMENTS

Concept 21:

Conversion of Debenture Investment to Equity Share Investment:

When there is a Investment in convertible debentures or bonds and issuing company is converting the debentures into equity shares **then such change shall be recorded at the same carrying amount of investments.**

Question 14: (RTP May19) (MTP May22)

A Ltd. purchased on 1st April, 2018 8% convertible debenture in C Ltd. of face value of Rs. 2,00,000 @ Rs. 108. On 1st July, 2018 A Ltd. purchased another Rs. 1,00,000 debentures @ Rs. 112 cum interest.

On 1st October, 2018 Rs. 80,000 debenture was sold @ Rs. 108. On 1st December, 2018, C Ltd. give option for conversion of 8% convertible debentures into equity share of Rs. 10 each. A Ltd. receive 5,000 equity share in C Ltd. in conversion of 25% debenture held on that date. The market price of debenture and equity share in C Ltd. at the end of year 2018 is Rs. 110 and Rs. 15 respectively. Interest on debenture is payable each year on 31st March, and 30th September. The accounting year of A Ltd. is calendar year.

Prepare investment account in the books of A Ltd. on average cost basis.

SOLUTION:

Investment Account for the year ending on 31st December, 2018

Scrip: 8% Convertible Debentures in C Ltd.

[Interest Payable on 31st March and 30th September]

Date	Particulars	Nominal value (Rs)	Interest (Rs)	Cost (Rs)	Date	Particulars	Nominal Value (Rs)	interest (Rs)	Cost (Rs)
1.4.18	To bank A/c	2,00,000	-	2,16,000	30.09.18	By Bank A/c [Rs. 3,00,000 x 8% x (6/12)]		12,000	
1.7.18	To bank A/c (W.N.1)	1,00,000	2,000	1,10,000	1.10.18	By Bank A/c	80,000		86,400
31.12.18	To P & L A/c [Interest]	3,00,000	14,033	3,26,000	1.10.18	By P&L A/c (loss) (W.N.1)			533
					1.12.18	By Bank A/c (Accrued interest) (Rs. 55,000 x 0.08 x 2/12)		733	

					1.12.18	By Equity shares in C Ltd. (W.N. 3 and 4)	55,000		59,767
					1.12.18	By Balance c/d (W.N.5)	1,65,000	3,300	1,79,300
		3,00,000	**16,033**	**3,26,000**			**3,00,000**	**16,033**	**3,26,000**

SCRIP: Equity Shares in C LTD.

Date	Particulars	Cost (Rs)	Date	Particulars	Cost (Rs)
1.12.18	To 8 % debentures	59,767	31.12.18	By balance c/d	59,767

Working Notes:

(i) Cost of Debenture purchased on 1st July = Rs. 1,12,000 – Rs. 2,000 (Interest) = Rs. 1,10,000

(ii) Cost of Debentures sold on 1st Oct. = (Rs. 2,16,000 + Rs. 1,10,000) x 80,000/3,00,000 = Rs. 86,933

(iii) Loss on sale of Debentures = Rs. 86,933– Rs. 86,400 = Rs. 533

Nominal value of debentures converted into equity shares = Rs. 55,000

[(Rs. 3,00,000 – 80,000) x.25]

Interest received before the conversion of debentures:

Interest on 25% of total debentures = 55,000 x 8% x 2/12 = 733

(iv) Cost of Debentures converted = (Rs. 2,16,000 + Rs. 1,10,000) x 55,000/3,00,000

= Rs. 59,767

(v) Cost of closing balance of Debentures = (Rs. 2,16,000 + Rs. 1,10,000) x 1,65,000 / 3,00,000

= Rs. 1,79,300

(vii) Closing balance of Debentures has been valued at cost being lower than the market value i.e., Rs. 1,81,500 (Rs. 1,65,000 @ Rs. 110)

(viii) 5,000 equity Shares in C Ltd. will be valued at cost of Rs. 59,767 being lower than the market value Rs. 75,000 (Rs. 15 x5,000)

Note: It is assumed that interest on debentures, which are converted into cash, has been received at the time of conversion.

AS 15 – EMPLOYEE BENEFITS

"Post Employment Employee Benefits" & "Other Long-Term Benefits - Accounting"

1) Types of Post employment benefits:

a) **Defined Contribution Plans (DCP):** Fixed contribution by employer to the specific fund such as EPF.

b) **Defined Benefit Plans (DBP):** Fixed Benefit (final amount payable) is payable by employer directly to employee in form of contributing variable amount every year to the fund.

Concept 22: **RECOGNITION OF DEFINED BENEFIT OBLIGATIONS (LIABILITY)**	
Important Steps to calculate annual Defined Benefit Obligation	**Step 1:** Calculate Expected Benefits to be paid to employees Expected Final Salary **x** Benefit (%) **x** No. of Years of Service **Step 2:** Allocate the Benefits to each year of Service (Attributed Benefits) Step 1 ÷ No. of Years of Service **Step 3:** Calculate Current Service Cost (CSC) using discount rate. PV of Attributed Benefits (PV working in upward mode) Current Service Cost (CSC) A/c Dr. (P&L) To DBO Payable A/c **Step 4:** Calculate Interest Cost on Opening Balance of DBO Payable using same discount rate. Interest Cost A/c Dr. (P&L) To DBO Payable A/c
Actuarial Gains or Loss in DBO liability	Due to change in financial and demographic assumptions of actuary or due to change in final expected salary, no. of years of services, DBO liability shall be remeasured with new assumptions. Increase in DBO Liability = Actuarial Loss Actuarial Loss (P&L) A/c Dr. To DBO Payable A/c

	Decrease in DBO Liability = Actuarial Gain DBO Payable A/c Dr. To Actuarial Gain (P&L) A/c Dr.
Past Service Cost (PSC)	If there is a modification in Defined Benefits announced by employer which results in increase of benefits for employee (i.e. additional benefits) then DBO Liability shall be increased accordingly. **PSC is divided into two parts:** **(a)** Amortised Past service cost - which is to be **recognized immediately** to the extent benefits are **already vested.** **(b)** Unamortised Past Service cost (UPSC)– to be recognized on **straight line basis** over the remaining period until the benefits are vested. Past Service Cost (P&L) A/c Dr. Unamortised PSC A/c Dr. To DBO Payable A/c
Curtailment and Settlement	Curtailment means cancellation of Defined Benefits of employees. Settlement means providing compensation to employees against cancellation of benefits. Curtailment shall reduce the liability as under: DBO Payable A/c Dr. To Unamortise PSC A/c (proportionate reversal) To Bank A/c Dr. To Gain on Settlement A/c (P&L)
Payment of Benefits to Employee	Whenever the employee retires, he/she will be eligible for benefits. DBO Payable A/c Dr. To Bank A/c Dr.

Concept 23: **RECOGNITION OF PLAN ASSETS (INVESTMENT for DBO)**	
Meaning	Investment made by Employer for meeting DBO liability. It is always recognised at Fair Value.
Contribution to Plan Assets	Contribution to Plan Asset means making Investment as per actuarial assumption under: Plan Assets A/c Dr. To Bank A/c (contribution is paid in beginning of year or mid of year or end of year)
Benefits Paid out of Plan Assets	When Employee is paid benefits, plan assets are realised as under:

	Bank A/c Dr. To Plan Assets A/c (Plan assets are realised in beginning of year or mid of year or end of year)
Expected Return on Plan Assets Plan Asset A/c Dr. To Exp. Return (P&L)	Interest Rate (%) **X** Balance of Plan Asset = Expected Return (Take same discount rate of DBO if separate rate is not given) If contribution and benefit <u>is made at end of year</u> Opening Balance of Plan Asset **x** Interest Rate (%) If contribution and benefit <u>is made at beginning of year</u> (Opening Balance of Plan Asset + Contribution Made – Benefits Paid) **x** Interest Rate (%) If contribution and benefit <u>is made at mid of year</u> Expected Return 1 - Opening Plan Assets **x** Interest (%) <u>(+) Expected Return 2</u> - Net Contribution **x** Six Monthly Interest (%) (=) Total Return Six Monthly Rate of Expected Return as under: **[**$\sqrt{1 + annaul\ rate}$ **- 1] x 100** If nothing is specified in question always assume that contribution is made, and benefits are paid at end of the year.
Closing Balance of Plan Assets	Always at Fair Value provided in Question
Actuarial Gain/Loss on Plan Assets	Any Difference in Plan Asset A/c is treated as Actuarial Gain or Loss and transferred to Profit and Loss A/c Plan Asset A/c Dr. Actuarial Loss (P&L) Dr. To Actuarial Gain (P&L) To Plan Asset A/c

Calculation of DBO Payable and Plan Asset

DBO Payable		Plan Asset	
Opening Balance of DBO	XXX	Opening Balance of Plan Asset	XXX
(+) Current Service Cost (CSC)	XXX	(+) Expected Return	XXX
(+) Interest Cost	XXX	(+) Contribution to Plan Asset	XXX
(+) Past Service Cost	XXX	(-) Payment of Benefits	XXX
(-) Curtailment of Benefits	XXX	(+/-) Actuarial Gain/(loss)	XXX
(-) Payment of Benefits	XXX	Closing Balance of Plan Asset	XXX
(+/-) Actuarial Loss/(Gain)	XXX		
Closing Balance of DBO	XXX		

Presentation in Financial Statements

BALANCE SHEET		STATEMENT OF PROFIT AND LOSS
Closing Balance of DBO	XXX	**Items of P&L:**
(-) Closing Bal. of Plan Asset	XXX	Employee Benefit Expenses
(-) Unamortised PSC	XXX	• Current Service Cost under Employee Benefit Exp. • Past Service Cost • Gain on Curtailment • Actuarial Gain/Loss on DBO • Actuarial Gain/Loss on Plan Assets
Net Defined Liability/(Asset)	XXX	Finance Cost • Net Interest Cost under Employee Benefit Exp. (Net Interest Cost means Interest Cost on DBO less Expected Return on Plan Asset)

Other Important Points:

1. The discount rate shall be determined by reference to market yields at the end of reporting period on Government Bonds.

2. **Current/Non-Current Distinction:**
   This Standard does not specify whether an entity should distinguish current and non-current portions of assets and liabilities arising from post-employment benefits.

Question 15:

An employee Roshan has joined a company XYZ Ltd. in the year 20X1. The annual emoluments of Roshan as decided is ₹14,90,210. The company also has a policy of giving a lump sum payment of 25% of the last drawn annual salary of the employee for each completed year of service if the employee retires after completing minimum 5 years of service. The salary of the Roshan is expected to grow @ 10% per annum.

The company has inducted Roshan in the beginning of the year and it is expected that he will complete the minimum five year term before retiring. Thus he will get 5 yearly increment.

What is the amount the company should charge in its Profit and Loss account every year as cost for the Defined Benefit obligation? Also calculate the current service cost and the interest cost to be charged per year assuming a discount rate of 8%.

(P.V factor for 8% - 0.735, 0.794, 0.857, 0.926, 1)

Solution:

Calculation of Defined Benefit Obligation (DBO)

Expected last drawn salary	₹ 14,90,210 x 110% x 110% x 110% x 110% x 110%	**₹24,00,000**

Defined Benefit Obligation (DBO)	₹ 24,00,000 x 25% x 5	**₹30,00,000**

Amount of ₹ 6,00,000 will be charged to Profit and Loss Account of the company every year as cost for Defined Benefit Obligation.

Calculation of Current Service Cost

Year	**Equal apportioned amount of DBO [i.e. ₹ 30,00,000/5 years]**	**Discounting @ 8% PV factor**	**Current service cost (Present Value)**
a	**b**	**c**	**d = b× c**
1	6,00,000	0.735 (4 Years)	4,41,000
2	6,00,000	0.794 (3 Years)	4,76,400
3	6,00,000	0.857 (2 Years)	5,14,200
4	6,00,000	0.926 (1 Year)	5,55,600
5	6,00,000	1 (0 Year)	6,00,000

Calculation of Interest Cost to be charged per year

	Opening balance	**Interest cost**	**Current service cost**	**Closing balance**
a	b	C =b×8%	d	e = b + c + d
1	0	0	4,41,000	4,41,000
2	4,41,000	35,280	4,76,400	9,52,680,
3	9,52,680	76,214	5,14,200	15,43,094
4	15,43,094	1,23,447	5,55,600	22,22141
5	22,22,141	1,77,859*	6,00,000	30,00,000

*Due to approximations used in calculation, this figure is adjusted accordingly

Assume in this question, at Beginning of 3rd year. There is a change in Actuarial Assumptions & due to such Change the Revised Estimated DBO Liability at Beginning of 3rd year is Rs. 10,10,000/-

Solution:

Carrying Amt of DBO Payable at 2nd year. end/3rd Year Beginning		9,52,680
Revised Balance of DBO Payable		10,10,000
Increase in DBO Liability (Actuarial Loss)		57,320
Actuarial Loss (P&L) Dr	57,230	
To DBO Payable A/c	57,230	

Further Current Service Cost and Interest Cost from 3rd Year onwards will also be Revised based on New Revised Liability.

Question 16:

As on 1st April, 20X1 the fair value of plan assets was ₹1,00,000 in respect of a pension plan of Zeleous Ltd. On 30th September, 20X1 the plan paid out benefits of ₹19,000 and received inward contributions of ₹49,000. On 31st March, 20X2 the fair value of plan assets was ₹1,50,000 and present value of the defined benefit obligation was ₹1,47,920. Actuarial losses on the obligations for the year 20X1- 20X2 were ₹600.

On 1st April, 20X1, the company made the following estimates, based on its market studies, understanding and prevailing prices

	%
Interest & dividend income, after tax payable by the fund	9.25
Realised and unrealised gains on plan assets (after tax)	2.00
Fund administrative costs	(1.00)
Expected Rate of Return	**10.25**

You are required to find the expected and actual returns on plan assets.

Solution:

Computation of Expected and Actual Returns on Plan Assets

		₹
Return on ₹ 1,00,000 held for 12 months at 10.25%		10,250
Return on ₹ 30,000 (49,000-19,000) held for six months at 5% (equivalent to 10.25% annually, compounded every six months)		1,500
Expected return on plan assets for 20X1-20X2		**11,750**
Fair value of plan assets as on 31 March, 20X2		1,50,000
Less: Fair value of plan assets as on 1 April,20X1	1,00,000	
Contributions received	49,000	(1,49,000)
		1,000
Add: Benefits paid		19,000
Actual return on plan assets		**20,000**

Alternatively, the above question may be solved without giving compound effect to rate of return.

AS 16 – BORROWING COSTS

Concept 24:

Capitalisation of Borrowing Costs to the Cost of Qualifying Asset:

There can be two types of borrowings which are as follows: -

A. **Specific Borrowing:** Loan is taken for specific qualifying asset
B. **General Borrowing:** Loan is not for any specific qualifying asset. It can be used for any purpose or for multiple assets.

Specific Borrowing Cost	General Borrowing Cost
Entire borrowing cost shall be capitalized from the date of 1st expenditure on qualifying asset. (i.e. start capitalization of entire borrowing cost from the date of 1st expenditure irrespective of expenses on different dates)	Capitalization shall be done expenditure wise (i.e. from the date of each expenditure on qualifying asset). To capitalize the borrowing cost we have to calculate weighted average of the borrowing rate (WABR) as under: Total Borrowing Cost incurred during the year x 100 Total Borrowings O/s during the Year Expenditure on QA x WABR (%) x Time Weight
If expenditure on qualifying asset is incurred out of specific as well as general borrowed funds then we shall first use specific borrowings if such borrowing is available on the date of expenditure.	

EXPENDITURE TO WHICH CAPITALISATION RATE IS APPLIED:

Expenditure Already incurred on QA (including Borrowing cost capitalized till last year)	XXX
Add: Expenditure incurred in CY (in Cash or payable)	XXX
Less: Progress Payments or Grants received during the CY	(XXX)
Total Expenditure on which WABR shall be applied	XXX

IMPORTANT POINT:

If any enterprise has earned temporary income by investment of unused borrowed funds, then amount of temporary income should be deducted against total borrowing cost and only thereafter principals of recognition should be applied.

Question 17:

Zebra limited began construction of a new plant on 1st April, 2021 and obtained a special loan of Rs. 20,00,000 to finance the construction of the plant. The rate of interest on loan was 10%.

The expenditure that was incurred on the construction of plant was as follows:

	Rs.
1st April, 2021	10,00,000
1st August, 2021	24,00,000
1st January, 2022	4,00,000

The company's other outstanding non-specific loan was Rs. 46,00,000 at an interest rate of 12%

The construction of the plant completed on 31st March, 2022.

You are required to:

(a) Calculate the amount of interest to be capitalized as per the provision of AS 16 "Borrowing Cost".

(b) Pass a journal entry for capitalizing the cost and the borrowing cost in respect of the plant

SOLUTION:

Total expenses to be capitalized for borrowings as per AS 16 "Borrowing Costs":

	Rs.
Cost of Plant (10,00,000 + 24,00,000 + 4,00,000)	38,00,000
Add: Amount of interest to be capitalized (W.N.)	3,24,000
	41,24,000

Journal Entry

		Rs.	Rs.
31st March, 2022	Plant A/c Dr. To Bank A/c [Being amount of cost of plant and borrowing cost thereon capitalized]	41,24,000	41,24,000

Working Note:

Computation of interest to be capitalized:

	Expenditure			Rs.
1st April, 2021	10,00,000	On specific borrowing	Rs. 10,00,000 x 10%	1,00,000
1st Aug, 2021	24,00,000	On specific borrowing	Rs. 10,00,000 x 10%	1,00,000
1st Aug, 2021		On non-specific borrowings	Rs. 14,00,000 x 8/12 x 12%	1,12,000
1st Jan, 2022	4,00,000	On non-specific borrowings	Rs. 4,00,000 x 3/12 x 12%	12,000
				3,24,000

`

Alternatively, interest cost to be capitalized can be derived by computing average accumulated expenses in the following manner.

Computation of Average Accumulated Expenses:

1st April, 2021	10,00,000 x 12/12	10,00,000
1st August, 2021	10,00,000 x 12/12 14,00,000 x 8/12	10,00,000 9,33,333
1st January, 2022	4,00,000 x 3/12	1,00,000
		30,33,333

Computation of interest to be capitalized:

		Rs.
On specific borrowing	Rs. 20,00,000 x 10%	2,00,000
On non-specific borrowing	Rs. (30,33,333- 20,00,000) x 12%	1,24,000
		3,24,000

NOTE:

Since specific borrowings are earmarked for construction of a particular qualifying asset, it cannot be used for construction of any other qualifying asset except for temporary investment. Therefore, once the commencement of capitalization of borrowing cost criteria are met, actual borrowing cost incurred on specific borrowing shall be capitalized irrespective of the fact that amount had been utilized in parts.

AS 17 – SEGMENT REPORTING

Concept 25: Segment Report

PRIMARY SEGMENT REPORT (Assuming Business Segments)

Particulars	Segment 1 (Reportable)	Segment 2 (Reportable)	Inter Segment Eliminations	Total
1. **Segment Revenue & Results:**				
Segment Revenue (Gross)				
Domestic:	XXX	XXX		XXX
Exports:	XXX	XXX		XXX
Total External Sales:	XXX	XXX	-	XXX
Inter Segment Sales:	XXX	XXX	(XXX)	XXX
Total Revenue	XXX	XXX	(XXX)	XXX
(-) Segment Expenses	XXXX	XXXX		XXXX
Segment Results (Profits/Losses)	XXX	XXX		XXX
(+) Unallocated Incomes less Expenses	-	-		XX
Net Profit before Interest & Tax				XXX
(-) Interest & Other Finance Cost				XXX
Net Profit before Tax				XXX
(-) Tax Expenses (Current +/- Deferred)				XXX
Profit After Tax (Entire)				XXX
2. **Segment Assets & Liabilities**				
(i) Assets:				
Non – Current Assets:	XXXX	XXXX		XXXX
Current Assets	XXXX	XXXX		XXXX
Total Segment Assets	XXXX	XXXX		XXXX
Unallocated Assets	-	-		XXX
Total Assets (Entire)	-	-		XXXX
(ii) Equity and Liabilities:				
Segment Liabilities	XXX	XXX		XXXX
Unallocated Liabilities	-	-		XXX
Total Liabilities	XXXX	XXXX		XXXX
Share Capital				XXXX
Reserves & Surplus				XXXX
Total Equity and Liabilities (Entire)				XXXX
3. **Other Information:**				

Capital Expenditure During the Year	XXX	XXX		XXX
Depreciation & Amortisation	XXX	XXX		XXX
Other Non-Cash Expenses	XXX	XXX		XXX

SECONDARY SEGMENT INFORMATION

(Assuming Geographical Segment Wise)

Geographical Information:	**Domestic**	**Foreign Country 1**	**Foreign Country 2**	**Total**
Total Revenue	XXX	XXX	XXX	XXX
Total Assets	XXX	XXX	XXX	XXX
Total Capital Expenditure During the Year	XXX	XXX	XXX	XXX

Concept 26: Segment Elements

SEGMENT REVENUE	**Aggregate of –** (a) Revenue Directly attributable to Segment (b) Enterprise Re (c) venue which is allocated to Segment on reasonable basis (d) Inter Segment Revenue (Transactions with other Segments) **Does not include** • Extraordinary items (defined in AS 5) • Interest or Dividend Income (Except Operation of segment is primarily of financial nature such as Banks and Financial Institutions) • Gains on Sale of Investments or Extinguishment of Debts (Except Operation of segment is primarily of financial nature)
SEGMENT EXPENSE	**Aggregate of –** (a) Expense Directly attributable to Segment resulting from Operating activities of segment. (b) Enterprise Expense which is allocated to Segment on reasonable basis (c) Inter Segment Expenses (Transactions with other Segments) **Does not include** • Extraordinary items (defined in AS 5) • Interest Expenses (Except Operation of segment is primarily of financial nature) • Losses on Sale of Investments or Extinguishment of Debts (Except Operation of segment is primarily of financial nature) • Income Tax Expenses

	• General Adm. Expenses, Head Office Exp. and Other Exp. incurred at enterprise level and related to entity as whole. **Important Point-** In case interest is capitalized to the cost of inventories as per AS 16 and such inventories are considered part of segment assets of a particular segment, then the interest should be considered as a segment expense.
SEGMENT RESULT	**SERGENT REVENUE LESS SEGMENT EXPENSES**
SEGMENT ASSETS	Operating Assets employed by the Segments in its operating activities (Directly Attributable or Allocated) Investments, Advances Receivables, Loans or Other related Assets are also included only and only when Interest and Dividend Income are part of Segment Results. **Does not include-** Income Tax Assets (TDS, Advance Tax, Deferred Tax Asset) Assets used for Head Office or General Purpose
SEGMENT LIABILITIES	Operating Liabilities of the Segments (Directly Attributable or Allocated) Borrowings, Loans Payables are also included only and only when Interest Expenses on above are part of Segment Results. **Does not include-** Income Tax Liabilities (Deferred Tax Liability, Current Tax Liability) Loans and Liabilities used for Head Office or General Purpose **Example:** Working Capital Loan taken for Particular Segment shall be part of Segment Liabilities but Other Long-Term Loans may not be included if taken for whole company.
ACCOUNTING POLICIES	Segment information should be prepared in conformity with the accounting policies adopted for preparing and presenting the financial statements of the enterprise as a whole. However, AS 17 does not prohibit the disclosure of additional segment information that is prepared on a basis other than the accounting policies adopted for the enterprise financial statements.

AS 19 – ACCOUNTING FOR LEASES

Concept 27:
FINANCE LEASE (BOOKS OF LESSEE)

<table>
<tr><td>Initial Recognition of Lease Liability and Asset on Lease</td><td>Lower of:
Present Value (PV) of MLP or
Fair Value of Asset

Note: PV shall be calculated using following discounting rates:
(a) Interest Rate implicit in lease (1st Priority); or
(b) Lessee's incremental borrowing rate</td></tr>
<tr><td>Minimum Lease Payment (MLP)</td><td>Initial Down Payment
(+) Annual Lease Rents
(+) Residual Value Guaranteed by Lessee (GRV)</td></tr>
<tr><td>Initial Direct Cost (IDC) incurred by Lessee</td><td>IDC shall be capitalized to the cost of Asset</td></tr>
<tr><td>Accounting Entry of Initial Recognition</td><td>Asset on Lease A/c Dr. (Including IDC)
To Lease Liability A/c
To Bank A/c (IDC Payment)

Lease Liability A/c Dr. (Payment of DP)
To Bank A/c</td></tr>
<tr><td>Depreciation</td><td>Asset on Lease is subject to depreciation under AS 10 over the Lease Period or Life of Asset whichever is lower.</td></tr>
<tr><td>Finance Charges (Interest Cost) on Lease Liability</td><td>Interest shall be calculated using the same discounting rate which was used earlier to calculate PV of MLP.
Interest shall be calculated on Opening Balance of Lease Liability as under:

<table>
<tr><th>Year</th><th>Opening</th><th>Interest</th><th>Payment</th><th>Closing</th></tr>
<tr><td>(1)</td><td>(2)</td><td>(3) = (2) x Rate</td><td>(4)</td><td>(2+3-4)</td></tr>
<tr><td></td><td></td><td></td><td></td><td></td></tr>
</table>
</td></tr>
<tr><td>Other Journal Entries</td><td>a) <u>For Charging Depreciation:</u>
Depreciation A/c Dr.
To Asset on Lease

b) <u>For Charging Finance Cost (Interest):</u>
Finance Charges A/c Dr.
To Lease Liability A/c

c) <u>For Payment of Lease Rent:</u></td></tr>
</table>

	Lease Liability A/c Dr. To Bank A/c **d)** Transfer to Profit and Loss: Profit and Loss A/c Dr. To Depreciation A/c To Finance Charges A/c

Note:

Interest Rate Implicit in the Lease (i.e. IRR) (Consider always from Lessor's point of view)	It is the rate at which- PV of (LP + UGRV) = FV at Inception + IDC
Lessee's Incremental Borrowing Rate	It is the rate at which Lessee can **Borrow additional funds over a similar term**, security for the same amount of underlying asset.

Concept 28:
FINANCE LEASE (BOOKS OF LESSOR)

KEY CONCEPTS FOR UNDERSTANDING LESSORS ACCOUNTING

'Gross investment in the lease' (GIL) = Initial Down Payment + Annual Lease Payments + GRV + UGRV	
'Net investment in the lease' (NIL)	(PV of GIL) PV of (DP + Lease Payments + UGRV) – Initial Direct Cost
'Unguaranteed residual value'	Total Estimated Residual Value (-) GRV

Non-dealer Lessor	Dealer or Manufacturer Lessor
Initial Recognition: Lease Receivable A/c Dr. (Net Invst. in Lease) Bank A/c Dr. (Down Payment) To Asset (PPE) A/c (Carrying Amt.) Difference in above entry is transfer to P&L a/c **Initial Direct Cost (IDC):** IDC is part of Cash Flows and will be considered under Interest Rate Calculation and then it is deducted from lease receivable.	**Initial Recognition:** Dealer Lessor shall record Sale at commencement of Lease: Lease Receivable A/c Dr. (Net Invst. in Lease) COGS A/c Dr. (Balancing Fig.) To Sale A/c (Lower of FV or PV of MLP) To Inventory A/c (Carrying Amt.) **Sale (-) COGS = Profit on Outright Sale** **Initial Direct Cost (IDC):**

Year End: Lease Receivable A/c Dr. To Finance Income (P&L) A/c Bank A/c Dr. To Lease Receivable A/c (Collection of Lease Rent)	IDC is directly transferred to Profit and Loss account and not a part of Interest Rate Calculation. **Year End:** Same as Non-dealer Lessor's Accounting
Calculation of Unearned Finance Income: Disclose Unearned Finance Income every year: Gross Investment in Lease (-) Net Investment in Lease	
Subsequent Measurement at Balance Sheet Date: At every BS date, **Lease Receivable** shall be recognised at Current Net Investment in Lease (i.e. PV of Remaining Lease Payments + Re-estimated UGRV). **UGRV shall be reviewed atleast once** in a year and if there is **any reduction** in the estimated UGRV the reduced amount shall be considered, this will result in reduction of Finance Income of the lessor.	

Concept 29:
SALE & LEASE BACK

A **sale and leaseback transaction** involves the sale of an asset and the leasing the same asset back. In this situation, a seller becomes a lessee, and a buyer becomes a lessor.

SALES AND LEASE BACK involves two transactions-

1. Sale of Asset by Seller Lessee to Buyer Lessor.
2. Lease Transaction (Finance Lease or Operating Lease)

Note: Here we have to understand the treatment of gain or loss on sale of Asset in the books of lessee (seller):

(A) Sale and Leaseback with Finance Lease

If the resulting lease is a **finance lease**, then in fact, the transaction is a loan securitized by the leased asset and seller / lessee keeps recognizing the asset. Any excess of proceeds over the carrying amount of the leased asset is deferred and amortized over the lease term in proportion of depreciation to be charged. **(i.e. Gain/Loss is to be deferred and amortised)**

Transaction 1: Sale of Asset

Bank A/c	Dr.
To Asset A/c	
To Gain on Sale A/c*	

*This Gain Shall be Deferred & Amortised over the Lease term in proportion of Depreciation to be Charged by Seller Lessee

Transaction 2: Finance Lease

Lease Asset A/c	Dr.
To Lease Liability A/c	

Lower of (a) FV or (b) PV of MLP

(B) Sale and Leaseback with Operating Lease

If the resulting lease is an operating lease, then a seller/lessee **derecognizes the asset**, and a buyer/lessor recognizes the asset. Further accounting treatment is as follow:

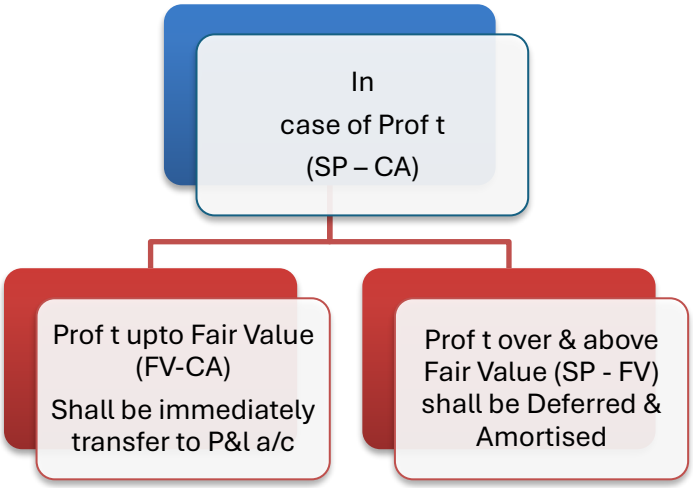
1. **Important Information: -**

SP means Actual Sale price of Asset (Agreed Contract Value)
CA Means Carrying Amt. (Book Value) of Asset
FV mean Fair Value of Asset (Market Value)

2. **Important Rules: -**

Rule – 1: If there is a Loss (CA – SP) then transfer it immediately to P&L.
Exceptions:- If Loss is to be Compensated with Future Lower Lease Rent. => then Loss is to be Deferred & Amortized over the Lease Term.

Rule – 2:



Rule – 3: Before Applying above 2 Rules, always Check if FV is lower than CA, if Yes then Impairment loss (CA – FV) shall be recognized First in P&L & then we can apply above Rule 1 & 2.

Question 18:

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

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

Answer:

1) No Profit/Loss

2) Gain 20000 => P & L immediately

3) Loss 20000
General Rule – Immediately transfer to P&L
Exception – If loss is compensated with future lease payments then Deferred &Amortised.

4) Gain = 20000 D&A

5) Gain = 40000 20K P & L
20K D&A

6) Rule-3 => Imp. Loss = 20000 P & L
Rule-2 => Profit = 20000 D&A

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

8) Loss = 10000 (same as 7)

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

10) Rule – 3 =>Imp. Loss 10000 P & L
Rule – 1 => Loss = 20000

AS 20 – EARNINGS PER SHARE

Concept 30:
DILUTED EARNINGS PER SHARE

1. Diluted EPS is calculated when there are outstanding potential equity shares.

2. Potential Equity Shares are those securities which can be converted into ordinary equity shares in future.
   E.g. Convertible Preference Shares, Convertible Debentures, share warrants, ESOPs, Call Options, partly paid-up shares if not eligible for dividend unless they become fully paid-up, Contingently issuable shares

3. Diluted EPS means reduction of Basis EPS if same earnings will continue with additional no. of shares when potential equity shares will be converted into ordinary shares.

4. Conversion into Ordinary shares may increase the Numerator and Denominator as under:

Numerator	Denominator
Saving of Interest after Tax due to conversion of Debentures. Saving of Preference Dividend due to conversion of Debentures.	Increase in No. of Shares due to conversion of Preference shares, Debentures, Warrants, ESOPs and Call Options.

5. Above Change in Numerator and Denominator may increase or decrease the existing Basic EPS.
   If there is a Decrease in EPS = It is Diluted EPS
   If there is a Increase in EPS = It is Anti Diluted EPS

6. Anti diluted EPS is not required to be reported. In that case, DEPS = BEPS

7. DEPS formulae:

Numerator	Denominator
Profit/loss attributable to ESH (+) Savings due to Conversion of Potential Equity Shares (after Tax if required)	Weighted Avg. O/s Ordinary Shares (+) Weighted Avg. O/s Potential Eq. Shares

Question 19:

EBIT	25,00,000
1st April	Ordinary Shares 80,000
1st June	Public Issue of Ordinary Shares – 25,000
1st July	Share Warrant issued 12,000 no. converted into ordinary shares on 1st Nov.
1st April	Opening Convertible debentures of 18,00,000/- @ 11% interest Converted on 1st Feb of Current year into 36,000 ordinary shares
1st December	Issued New ESOPs of 40,000 no. at Exercise price of 75/- each and Market Price was 120/- each
Calculate Basic and Diluted Earnings Per Share	

AS 22 – ACCOUNTING FOR TAXES ON INCOME

Concept 31:

Concept of Deferred Taxes

Accounting Income	PBT
Taxable Income	Income as per I T Act
Current Tax	Tax on Taxable Income
Difference of A/c Income and Taxable Income	Timing Difference and Permanent Difference
Permanent Difference	Arise in One Year but never reverse in Future periods **Examples:** Donations to Religious Trust Personal Expenses of Director Revaluation Reserve
Timing Difference	Arise in One Year and Capable of Reversal in Future Periods
Types of timing differences	a) Taxable Timing Difference – DTL b) Deductible Timing Difference - DTA
Taxable Timing Differences	**Examples:** Depreciation as per IT in CY is higher than Depreciation as per Books 100% Deduction of Scientific Research Expenditure is claimed as per IT in CY Any Income which would be taxable on cash basis in future.
Deductible Timing Differences	Provision for Doubtful Debts Expenses allowed as deduction on Cash Basis in Future Unamortised Preliminary Expenses as per Tax Records
DTL Journal Entry	Profit and Loss A/c Dr.

	To DTL DTL A/c Dr. To Profit and Loss A/c
Reversal of	DTA A/c Dr. To Profit and Loss A/c Profit and Loss A/c Dr. To DTA A/c
Total Tax Expense in Profit and Loss A/c	Current Tax Expense (Regular Tax) (+) Excess of MAT over Regular Tax (+) Deferred Tax Liability Created (-) Deferred Tax Asset Created (-) Deferred Tax Liability Reversed (+) Deferred Tax Asset Reversed

Question 20:

The following particulars are stated in the Balance Sheet of Deep Limited as on 31st March, 2020:

	(Rs. In Lakhs)
Deferred Tax Liability (Cr.)	28.00
Deferred Tax Assets (Dr.)	14.00

The following transactions were reported during the year 2020 -2021:

i. Depreciation as per books was Rs. 70 Lakhs whereas Depreciation for Tax purposes was Rs. 42 Lakhs. There were no additions to Fixed Assets during the year.
ii. Expenses disallowed in 2019-20 and allowed for tax purposes in 2020-21 were Rs. 14 Lakhs.
iii. Share issue expenses allowed under section 35(D) of the Income Tax Act, 1961 for the year 2020-21 (1/10th of Rs. 70.00 lakhs incurred in 2019-20).
iv. Repairs to Plant and Machinery were made during the year for Rs. 140.00 Lakhs and was spread over the period 2020-21 and 2021-22 equally in the books. However, the entire expenditure was allowed for income-tax purposes in the year 2020-21.

Tax Rate to be taken at 40%.

You are required to show the impact of above items on Deferred Tax Assets and Deferred Tax Liability as on 31st March, 2021.

Solution:

Impact of various items in terms of deferred tax liability/deferred tax asset on 31.3.21

Transactions	Analysis	Nature of difference	Effect	Amount (Rs.)
Difference in depreciation	Generally, written down value method of depreciation is adopted under IT Act which leads to higher depreciation in earlier years of	Responding timing difference	Reversal of DTL	28 lakhs × 40% = Rs. 11.20 lakhs

	useful life of the asset in comparison to later years.			
Disallowances, as per IT Act, of earlier years	Tax payable for the earlier year was higher on this account.	Responding timing difference	Reversal of DTA	14 lakhs × 40% = 5.6 lakhs
Share issue expenses	Due to disallowance of full expenditure under IT Act, tax payable in the earlier years was higher.	Responding timing difference	Reversal of DTA	7 lakhs × 40% = Rs. 2.8 lakhs
Repairs to plant and machinery	Due to allowance of full expenditure under IT Act, tax payable of the current year will be less.	Originating timing difference	Increase in DTL	70 lakhs × 40% = 28 lakhs

AS 23 – INVESTMENT IN ASSOCIATES

Concept 32:

EQUITY METHOD on Investment in Associates under Consolidated Financial Statements of Investor:

Value of Investment shall be increased or decreased by-	**Rs.**	**2nd effect to-**
Cost of Investments (Including Goodwill)	xxxx	
Add/Less: Post acquisition share in **P&L of** Associate Co. (EAESH)	xxx	CPL of investor
Less: Distributions received by way of dividend	xxx	CPL of Investor
Less: Additional depreciation on revaluation profit of PPE (if any)	xxx	CPL of Investor
Less: **Un-realised profit** on downstream transaction to the extent of Investor's share in gain/loss of Associate/JV	xxx	CPL of Investor
Value of Investments as per Equity Method	**XXXX**	

Note:

1. **Goodwill:**
   If cost of Investment is greater than investor's share of investees' net assets – it is not separately presented. It is included in the carrying amount of investment.
2. **Capital reserves:**
   If the cost of investment is less than investor's share of investee's net assets – it is recognised directly in Reserves & Surplus in the period in which investment is made.

Journal Entry as on acquisition date:

Investment A/c Dr.
To Capital Reserve A/c

Question 21:

On 1/7/24 B Ltd. acquired 20% Equity interest in A Ltd. at a cost of 2,40,000/-
On 1/4/24 Equity Share Capital of A Ltd was 8,00,000 and Reserves & Surplus of A Ltd. was 3,00,000
On 31/3/25 Reserves & Surplus of A Ltd. was 5,00,000
During 24-25, Dividend Paid by A Ltd. to its Share Holders 15% on 1st December.
On 1st July 2024, Market Value of PPE of A Ltd. was 12,00,000 but Book Value was 10,00,000 (Depreciation Rate was 10%)
What would be the value of Investment in SFS as per AS 13 and as per AS 23 under Consolidated Financial Statements both on DOA & Balance Sheet Date.

AS 25 – INTERIM FINANCIAL REPORTING

Concept 33:
Tax Expense for Interim Period

Profit/loss of each interim period may contain 2 parts:

(a) Normal Business Profit and;

(b) Special Income (e.g. capital gains) taxable at special rate

Tax Expense for Interim Period will be sum of:

(a) Normal Profit/loss (after deducting c/f losses) **X** WATR

(b) Special Income **X** Special Rate

Weighted Average Tax Rate (WATR):

$$\frac{\text{Estimated Annual Tax Amount}}{\text{Estimated Annual Income (before deducting c/f losses)}} \times 100$$

Note: Estimated Annual Tax will be calculated after w/off carried forward losses if given in the question.

Question 22:

Financial Year 24-25, C/f business losses (to be set off in CY) = Rs. 2,00,000

Income Quarter wise are as under:

Q1 (Actual)	3,00,000
Q2 (Expected)	2,00,000
Q3 (Expected)	4,00,000
Q4 (Expected)	6,00,000

Q1 income includes Special Income of 50,000 taxable at 12%

Tax Slab for Normal Income is:

Upto 2,50,000	Nil
2,50,000 – 5,00,000	10%
5 lacs to 8 Lacs	20%
Above 8 Lacs	30%

Calculate Tax Expense of Q1

AS 28 – IMPAIRMENT OF ASSETS

Concept 34:
Impairment Loss of a Cash-Generating Unit (CGU) Including Goodwill & Corporate Asset

A cash-generating unit is the smallest identifiable group of assets that generates cash inflows that are largely independent of the cash inflows from other assets or groups of assets.

- ☞ Always try to impair Individual Asset first for which indication ofimpairment exist and estimate the recoverable amount of that individual asset.
- ☞ If it is not possible to estimate the recoverable amount of the individual asset, then recoverable amount of the cash-generating unit to which the asset belongs should be determined and apply impairment testing of CGU.
- ☞ CGU may include current assets, goodwill, corporate assets and liabilities also.

Carrying Amount of CGU:	Carrying Amount of PPEs of CGU (+) Carrying Amount of Intangible Assets of CGU (+) Carrying Amount of Current Assets of CGU (+) Carrying Amount of Goodwill allocated to CGU (+) Carrying Amount of Corporate Assets allocated to CGU
Corporate Assets:	Assets other than goodwill that helps CGU under review and other CGUs to generate Independent Cash Flows. (For Ex. Head office buildings)
How to Impair Goodwill and Corporate Assets	Goodwill and Corporate Assets doesn't generate independent cash flows hence they can-not be tested for impairment individually. Goodwill & Corporate Assets are first allocated to different CGUs on a Reasonable basis and then they are tested for impairment.
How to allocate Goodwill and Corporate Assets?	Goodwill shall be allocated either in the ratio given in the question (or) in the ratio of Fair Values of CGUs at the time of business acquisition.

	Corporate Assets shall be allocated either in the ratio given in the question (or) in the ratio of following amounts of each CGU: Carrying Amt. x Useful life (if useful life is not given then only carrying amount of CGUs can be used to find out ratio)
Un-allocable Goodwill and Corporate Assets	Apply Bottom-up approach for Goodwill and Corporate Assets which are Allocable to CGUs. Apply Top-down approach for Goodwill and Corporate Assets which are not allocable to CGUs.
Important Note	Impairment Loss is never allocated to Current Assets or any other assets on which AS 28 is not applicable

Steps to Solve the Complete Question:

Approach	Particulars	CGU 1	CGU 2	CGU 3	Total
Bottom Up	Carrying Amt of CGUs	XXX	XXX	XXX	XXXX
	(+) Allocate Goodwill	XXX	XXX	XXX	XXXX
	(+) Allocate Corporate Assets	XXX	XXX	XXX	XXXX
	Total Carrying Amount of CGUs	XXX	XXX	XXX	XXXX
	Less:				
	Total Recoverable Amt. of CGUs	XXX	XXX	XXX	XXXX
Bottom up continued	Impairment Loss of CGUs	XXX	XXX	XXX	XXX
	(-) Allocable Goodwill (1st Priority)	XX	XX	XX	XX
	(-) Remaining Imp. Loss is allocated to all other Assets including Corporate Assets in the given ratio	XXX	XXX	XXX	XXX
Top-down	Revised Carrying Amt. of CGUs	XXX	XXX	XXX	XXX
	(+) Un-allocable Goodwill or Corporate Assets	-	-	-	XXX
	Total Carrying Amount of Entity as a whole				XXX
	(-) Recoverable Amt. of Entity as a whole				XXX
Top-	Additional Impairment Loss for Un-allocable Goodwill and Corporate				XXX

down	Assets only (Do not impair CGUs since they are already tested for impairment)				

Question 23:

A Ltd. gives following information

Asset	Carrying Amount	Cash generating unit
A	1,00,000	1
B	2,00,000	3
C	3,00,000	2
D	3,50,000	2
E	70,000	1
F	8,00,000	3
G	2,20,000	2
H	4,50,000	1
Goodwill X	90,000	Allocate in ratio 1:1:1
Goodwill Y	60,000	Unallocable
Corporate:		
Asset P	1,50,000	Allocate in ratio 3:2:1
Asset Q	2,00,000	Unallocable

Recoverable Amount of Cash generating Unit: 1 – 6,70,000; 2 – 8,40,000 and 3 – 10,30,000 Recoverable Amount of Entity: Case A – 25,50,000; Case B – 25,40,000. Calculate impairment loss.

Concept 35:
REVERSAL OF IMPAIRMENT LOSS

Goodwill:

An impairment loss recognised for goodwill shall not be reversed in a subsequent period.

Assets other than Goodwill:

If there is an Indication that shows Impairment Loss recognised earlier may no longer exists or may have decreased, then entity shall revers the impairment loss and accordingly recoverable amount is to be determined.

How to Calculate the Reversal of Impairment Loss:

Step 1: Identity Current Actual Carrying Amount of Asset – assume 1000/-

Step 2: Identity Current Recoverable Amount of Asset – assume 1200/-

Step 3: Calculate Current Carrying Amount of Asset if Asset were never impaired earlier

(assume 1150/-)

Step 4: Revised Carrying amount after reversal should be lower of Step 2 & Step 3

(Means 1150/-)

Step 5: Reversal of Impairment Loss = Step 4 – Step 1 (means 1150 – 1000 = 150)

Step 6: Calculate Revised Actual Carrying Amount = Current Carrying Amount before reversal (Step 1) + Reversal of I/L (Step 5)

Note: Depreciation shall be charged on Revised Carrying Amount

(Refer Examples)

Accounting treatment of Reversal of Impairment Loss:

Asset A/c Dr.

To Impairment Loss Reversal A/c

Impairment Loss Reversal A/c Dr.

To Revaluation Surplus A/c (if available & Asset is under Revaluation model)

To Profit and Loss A/c (Balancing Fig.)

Reversal of Impairment Loss of CGU:

A reversal of an impairment loss for a cash-generating unit shall be allocated to the assets of the unit, except for goodwill, in proportion of carrying amounts of those assets.

Question 24:

Himalaya Ltd. which is in the business of manufacturing and exporting its product. Sometimes, back at the end of 20X4, the Government put restrictions on export of goods exported by Himalaya Ltd. and due to that restriction Himalaya Ltd. impaired its assets. Himalaya Ltd. acquired identifiable assets worth Rs 5,500 lakhs for Rs 6,000 lakh at the end of the year 20X0. The difference is treated as goodwill. The useful life of identifiable assets is 15 years and depreciated on a straight-line basis. When the Government put the restriction at the end of 20X4, the company recognised the impairment loss by determining the recoverable amount of assets for Rs 3,120 lakh. In 20X6 Government lifted the restriction imposed on the export and due to this favourable change, Himalaya Ltd. re-estimate recoverable amount, which was estimated at Rs 3,420 lakh.

Required:

. Calculation and allocation of impairment loss in 20X4.

. Reversal of impairment loss and its allocation as per AS 28 in 20X6.

Solution

(Assuming goodwill is amortised over 5 years as per AS 14)

(i) Calculation and allocation of impairment loss in 20X4

(Amount in Rs.lakhs)

	Goodwill	Identifiable assets	Total
Historical cost	500	5,500	6,000
Accumulated depreciation/amortization (4 yrs.)	400	(1,467)	(1,467)
Carrying amount before impairment	100	4,033	4,133
Impairment loss*	(100)	(913)	(1013)
Carrying amount after impairment loss	**0**	**3,120**	**3,120**

***Notes:**

1. As per AS 28, an impairment loss should be allocated to reduce the carrying amount of the assets of the unit in the following order:
   - first, to goodwill allocated to the cash-generating unit (if any); and
   - then, to the other assets of the unit on a pro-rata basis based on the carrying amount of each asset in the unit.

Hence, first goodwill is impaired at full value and then identifiable assets are impaired to arrive at recoverable value.

(ii) Carrying amount of the assets at the end of 20X6 (Amount in Rs. lakhs)

End of 20X6	Goodwill	Identifiable assets	Total
Carrying amount in 20X6	0	2,553	2,553
Add: Reversal of impairment loss (W.N.2)	-	747	747
Carrying amount after reversal of impairment loss	**-**	**3,300**	**3,300**

Working Note:

1. **Calculation of depreciation after impairment till 20X6 and reversal of impairment loss in 20X6**

			(Amount in Rs lakhs)
	Goodwill	**Identifiable assets**	**Total**
A. Carrying amount after impairment loss in 20X4	0	3,120	3,120
B. Additional depreciation (i.e. (3,120/11) x 2)refer Note	-	(567)	(567)
C. Carrying amount	0	2,553	2,553
D. Recoverable amount			3,420
E. Excess of recoverable amount over carrying amount (D-C)			**867**

Note: It is assumed that the restriction by the Government has been lifted at the end of the year 20X6. Therefore, depreciation for 2 years is calculated (2005, 2006).

0. **Determination of the amount to be impaired by calculating depreciated historical cost of the identifiable assets without impairment at the end of 20X6**

(Amount in Rs lakhs)

End of 20X6	**Identifiable assets**
Historical cost	5,500
Accumulated depreciation	(366.67 x 6 years) = (2,200)
Depreciated historical cost	3,300
Carrying amount (in W.N. 1)	**2,553**
Amount of reversal of impairment loss	**747**

Notes:

As per AS 28, in allocating a reversal of an impairment loss for a cash-generating unit, the carrying amount of an asset should not be increased above the lower of:

. its recoverable amount (if determinable); and

. the carrying amount that would have been determined (net of amortization or depreciation) had no impairment loss been recognised for the asset in prior accounting periods.

Hence impairment loss reversal is restricted to Rs 747 lakhs only.

Note:

Impairment Loss on Goodwill shall not be reversed except certain conditions.