AS-7: SUMMARY CHART

Applicability : Contractors → YES
(construct asset owned by someone else)

SELF OWNED PROPERTY CONSTRUCTED – NO

Construction Contract :- Contract for :-

1) Construction of 1 asset or multiple assets.
2) Services directly related to construction activity.
3) Contracts for destruction, restoration of assets.
4) Contract for restoration of environment.

Segmenting v/s Combining :-

Segmenting	Combining
1. Separate proposal for each asset.	1. Negotiation as a single package.
2. Individual basis - accept / reject each proposal.	2. Asset constructed in a continuous sequence.
3. For each asset - cost / revenue can be individually identified.	3. Profit margin - overall basis
↓ legally 1 contract, but for accounting purpose separate / individual contract for each asset. ↓ Cost / Revenues of each asset will be separately recog.	↓ legally, multiple contracts, but for accounting purpose consider it as 1 contract. ↓ Overall cost / revenues will be calculated and recognised.

Construction of Additional Asset

↓

Cost / Revenue related to additional asset separately recognised if ;

1. Additional asset significantly differs in design, technology, function from original asset.

OR

2. Negotiation for additional asset done without regard to original asset.

TYPES OF CONSTRUCTION CONTRACTS

Fixed Price	Cost Plus	Hybrid
Contract gets a fixed price for work done.	Contracts gets his remuneration as a percentage of cost incurred.	Contracts gets his remuneration as a percentage of cost incurred subject to a maximum cap (limit)

CONTRACT REVENUE

Revenue Originally Agreed :-
& Includes

Claim	Variation Payment	Incentive Payment
Additional cost incurred by contractor for work not specified in the contract.	Change in scope of contract work.	Payment for meeting certain performance standards.
Recog. Criteria	Recog. Criteria	Recog. Criteria
→ Approved by customer → Measurement – certain	→ Approved by customer → Measurement – certain	→ Contract should reach sufficiently advanced stage that it is probable that incentive payment will be realised. → Measurement – certain

CONTRACT COSTS

→ Directly related costs.
→ Costs that can be allocated on a proportionate basis.
→ Costs specifically chargeable from a customer.
→ Cost of acquiring the contract.

REVENUE RECOGNITION

Whether outcome of the contract is reliably measurable.

YES	NO
1. Calculate stage of completion 2. Recognise revenue and cost in proportion to the stage of completion.	1. Recognise revenue only to the extent of cost incurred i.e. no profit can be recognised.

Stage of completion :-

$$= \frac{\text{Cost Incurred till date}}{\text{Total cost}}$$

Important Note :-

If at any stage it is probable that contracts costs will exceed contract revenue, total loss (full / entire) will be recognised immediately.

DISCLOSURES :-

Read from book.

LH7

STUDENT NOTES

QUESTION 9

Shera ~~Gym~~ Construction Ltd signed on 31st Dec, the Balance Sheet date, a contract where the total revenue is estimated at ₹15 Crores and the total cost is estimated at ₹20 Crores. No work began on the contract. Is the Contractor required to give any accounting effect for the year ended 31st December?

Answer:

Quote: *As per the provisions of AS-7: Revenue Recognition, "When it is probable that estimated total contract costs exceed the contract revenue, full loss will be recognized in the P&L irrespective of;*

- *Whether or not work has commenced on the contract.*
- *The stage of completion of contract activity.*
- *The amount of profits expected to arise on other contracts which are not treated as a single construction contract.*

Analysis: *There is an Expected Loss of ₹ 5 Crores (20 Crores - 15 Crores).*

Conclusion: *Such loss should be recognized in the Profit and Loss Statement as per AS-7, even though work has not commenced.*

QUESTION 10

✓ × 80% = 80

A Company took a Construction Contract for ₹100 Lakhs in January. It was found that 80% of the Contract was completed at a cost of ₹ 92 Lakhs on the closing date i.e. 31st March. The Company estimates a further expenditure of ₹23 Lakhs for completing the contract. The expected loss would be ₹15 Lakhs. Can the company recognize the loss in the Financial Statements prepared for the year ended 31st March?

TC = 92+23 = 115

Answer:

Quote: *As per the provisions of AS-7: Revenue Recognition, "When it is probable that estimated total contract costs exceed the contract revenue, full loss will be recognized in the P&L irrespective of;*

- *Whether or not work has commenced on the contract.*
- *The stage of completion of contract activity.*
- *The amount of profits expected to arise on other contracts which are not treated as a single construction contract.*

P&L

CC	92	CR	80
Prov for exp loss	3	TL	15

Analysis: *There is an Expected Loss of 15 Lakhs.*

Conclusion: *Such loss should be recognized in the Profit and Loss Statement as per AS-7, even though work has not commenced.*

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Work cert / work not cer → contract cost → not related.

payment recd.

L4T

TCC = 1050000
CI = 990000 } %

STUDENT NOTES

QUESTION 11 → Costs incurred till date

An amount of ₹9,90,000 was incurred on a contract work up to 31st March. Certificates have been received to date to the value of ₹12,00,000 against which ₹10,80,000 has been received in cash. The cost of work done but not certified amounted to ₹22,500. It is estimated that by spending an additional amount of ₹60,000 (including Provision for contingencies) the work can be completed in all respects in another two months. The agreed Contract Price of the work is ₹12,50,000. Compute a conservative estimate of the profit to be taken to the P&L A/C as per AS-7.

% com = 94.28%

Contract Rev = 1250000 × 94.28% = 1178500
Cost = 990000
188500

Answer:

	Particulars	₹
	Total Cost = Cost incurred till Date + Estimated Additional Cost = 9,90,000 + 60,000	10,50,000
	% of completion based on Cost = Cost incurred till date / Estimated Total Costs = (9,90,000/10,50,000) X 100	94.29%
	Contract Revenue to be recognized (12,50,000 x 94.29%)	11,78,625
Less:	Contract Cost incurred till date	9,90,000
	Contract Profit	1,88,625

QUESTION 12

A Company undertakes a number of Contracts. The following particulars are extracted in respect of certain loss-making contracts. Determine the amount of Expected Loss that should be recognized in the accounts for the year, (in ₹ Lakhs)

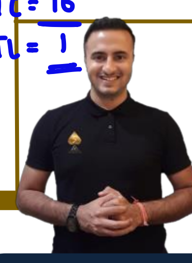
→ HW → HW

Contract	A	B	C	D
Contract Price	15.00	12.50	87.50	10.00
Cost Incurred till date	12.00	10.90	2.50	6.00
Costs expected to be incurred to complete the Contract	4.00	3.60	88.00	4.00

TR = 15
TC = 16
TL = 1

(A) = SOC = $\frac{12}{16}$ = 75%

CC 12 | CR 11.25
Loss T.D. 0.75 } A.P. for loss = 0.25
TL 1



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STUDENT NOTES

QUESTION 14

On 31st October 2017, Bihar Construction Co. Ltd. undertook a Contract to construct a flyover for ₹215 Crores. On 31st March 2018, the Company found that the Work is Certified for ₹100 Crores and Work to be Certified is for ₹35 Crores. Prudent estimates of additional Cost for Completion was ₹90 Crores. What amount should be charged to revenue in the Financial Accounts for the year ended 31st March 2018 as per AS-7?

135+90 = 225

SOC = $\frac{135}{225}$ = 60%

CR = 129
CC = 135
L = 6

Total loss = 215−225 = 10 Crores

Answer:

	Particulars	₹ in Crores
1.	Contract Price (given)	215.00
2.	Cost incurred till date (Work Certified + Work to be Certified)	135.00
3.	Further Costs to be incurred to complete the Contract	90.00
4.	Total Contract Costs (2) + (3)	225.00
5.	Expected Loss on Contract (1) - (4)	(10.00)
6.	Percentage of Completion based on Costs = $\frac{\text{Cost Incurred till date}}{\text{Estimated Total Costs}}$	60%
7.	Contract Revenue recognized (1) × (6)	129.00
8.	Contract Costs recognized (as per 2)	135.00
9.	Contract Profit / (Loss) (7) - (8)	(6.00)
10.	Expected Loss to be recognized (as per 5)	10.00
11.	Additional Provision required (9) - (10)	4.00

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AS 7: Construction Contracts

Student Notes

Question 15 (RTP May 18, RTP Nov 20)

Uday Constructions undertake to construct a bridge for the Government of Uttar Pradesh. The construction commenced during the financial year ending 31.03.2016 and is likely to be completed by the next financial year. The contract is for a fixed price of ₹ 12 crores with an escalation clause. The costs to complete the whole contract are estimated at ₹ 9.50 crores of rupees. You are given the following information for the year ended 31.03.2016: Cost incurred upto 31.03.2016 ₹ 4 crores .

Cost estimated to complete the contract ₹ 6 crores

Escalation in cost by 5% and accordingly the contract price · is increased by 5 %.

You are required to identify the state of completion and Calculate the revenue and profit to be recognized for the year as per AS 7.

RCP = 12.6 (12 + 5%)

RCC = ~~10 + 5%~~

SOC = $\frac{4}{4+6}$ = 40%

CR = 12.6 × 40%

= 5.04

CC = 4

P = 1.04

Answer:

Cost of construction of bridge incurred 31.3.16	4.00
Add: Estimated future cost	6.00
Total estimated cost of construction	10.00
Contract Price (12 crore x 1.05)	12.60 crore

Stage of completion:

Percentage of completion till date to total estimated cost of construction = (4/10)x100 = 40%

Revenue and Profit to be recognized for the year ended 31st March, 2016 as per AS 7.

Proportion of total contract value recognized as revenue = Contract price x percentage of completion
=₹ 12.60 crore x 40% =₹ 5.04 crore

Profit for the year ended 31st March, 2016 = ₹ 5.04 crore less ₹ 4 crore = 1.04 crore

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Student Notes

Answer:

Calculation of foreseeable loss for the year ended 31st March, 2019 (as per AS 7 "Construction Contracts")

Cost incurred till 31st March, 2019	83.99
Prudent estimate of additional cost for completion	36.01
Total cost of construction	120.00
Less: Contract price	(108.00)
Foreseeable loss	12

According to para 35 of AS 7 (Revised 2002) "Construction Contracts", when it is probable that total contract cost will exceeds total contract revenue; the expected loss should be recognized as an expense immediately. Therefore, amount of ₹ 12 lakhs is required to be provided for in the books of Sampath Construction Company for the year ended 31st March, 2019 .

Question 18 (RTP May 20)

A construction contractor has a fixed price contract for ` 9,000 lacs to build a bridge in 3 years time frame. A summary of some of the financial data is as under:

	(Amount ₹ in lacs)		
	Year 1	Year 2	Year 3
Initial Amount for revenue agreed in contract.	9,000	9,000 9200	9,000 9200
Variation in revenue (+)	-	200	200
Contracts costs incurred up to the reporting date	2,093	6,168 *	8,100 ** = +100
Estimated profit for the whole contract	950	1,000	1,000

TC = 9000 - 950 = 8050 ETC = 8200 TC = 8200

CR = 9000/-
Cost = 3500/-
4500/-
10000/-
CR = 12 + 5% = 12.6
× SOC
Rev. Recog.

Includes ` 100 lacs for standard materials stored at the site to be used in year 3 to complete the work.

***Excludes ` 100 lacs for standard material brought forward from year 2.*

The variation in cost and revenue in year 2 has been approved by customer.

Compute year wise amount of revenue, expenses, contract cost to complete and profit or loss to be recognized in the Statement of Profit and Loss as per AS-7 (revised).

Question 18:- **Year 1**

$$SOC = \frac{2093}{8050} = 26\%$$

CR = 9000 × 26% = 2340
CC = 8050 × 26% = 2093
P = 247

Year 2

$$SOC = \frac{CI}{TC} = \frac{6168-100}{8200} = 74\%$$

CR	= 9200 × 74%	= 6808	− Y1 recog.	− 2340	=	4468
CC	= 8200 × 74%	= 6068		− 2093	=	3975
P		= 740				493
		Total in 2 years		Year 1 already recogn.		To be recog in Y2.

Year 3

$$SOC = \frac{CI}{TC} = \frac{8200}{8200} = 100\%$$

CR	= 9200 × 100%	= 9200	− 6808	=	2392
CC		= 8200	− 6068	=	2132
P		= 1000			260
		Total in 3 years	Y1 & Y2 already recogn.		To be recog in Y3.