

SUGGESTED ANSWERS OF TEST 6

Instructions for Checking:

1. There may be a different presentation of Working Notes, don't deduct the marks for different presentation if answer and working is matching

Solution of Q1

Statement Showing the Computation of Value of Closing Inventory & Value of Closing Finished Goods

Particulars	Amount (Rs.)
Cost of Raw Material consumed (20,400 units X Rs. 20 per kg)	4,08,000
Direct Labour	3,06,000
Fixed Overheads (Rs. 3,00,000/30,000 x 20,400)	2,04,000
Cost of Production	9,18,000
Cost of Closing Inventory of Finished Goods per unit (Rs. 9,18,000/20,400)	45
Net Realizable Value (NRV) per unit	40

Since net realizable value is less than cost, closing inventory of Finished Goods will be valued at Rs. 40 per unit

Value of Closing Raw Materials

As NRV of finished goods is less than its cost, the relevant raw material will be valued at its replacement cost, which is the best available measure of its NRV i.e., @ Rs. 19 per kg.

Therefore, value of closing inventory would be as under:

Finished Goods 2,400 units @ Rs. 40 per unit	Rs. 96,000
Raw Materials 1,800 kg @ Rs. 19 per kg	Rs. 34,200
Total	Rs. 1,30,200

Working Note:

Calculation of raw material consumed during the year

Particulars	Unit (Kg)
Opening Inventory	2,200
Purchases	20,000
Less: Closing Inventory	(1,800)
Raw Material Consumed	20,400

Solution of Q2

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 an 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 1 st May)
Investment income on temporary investment of the loan proceeds	(100)	offset against the amount capitalized
Demolition cost recognised as a provision	<u>920</u>	Where an obligation must recognise as part of the initial cost at PV.
Total cost of Land & Building	<u>19,912.50</u>	
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	$9,912.50 \times 30\% \times 1/20 \times 4/12$ $9,912.50 \times 70\% \times 1/40 \times 4/12$
Total depreciation	107.38	
Computation of carrying amount	<u>19,805.12</u>	19,912.50 - 107.38

Solution of Q3:

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

		No.	Amount			No.	Amount
			₹				₹
1.4.20X1	To Bal	30,000	4,50,000	31.10.	By Bank	—	10,000
22.6.20X1	b/d	5,000	80,000	20X1	(dividend on shares acquired on 22.6.20X1)		
	To Bank						
10.8.20X1	To Bonus	5,000	—				
30.9.20X1	To Bank (Rights Shares)	10,000	1,50,000				
15.11.20X1	To P&L A/c (Profit on sale of shares)		32,000	15.11.20X1	By Bank (Sale of shares)	20,000	3,00,000
				31.3.20X2	By Bal. c/d	30,000	4,02,000
		50,000	7,12,000			50,000	7,12,000

Working Notes:

- (1) **Bonus Shares** = $(30,000 + 5,000) / 7 = 5,000$ shares
- (2) **Right Shares** = $(30,000 + 5,000 + 5,000) / 8 \times 3 = 15,000$ shares
- (3) **Rights shares sold** = $15,000 \times 1/3 = 5,000$ shares
- (4) **Dividend received** = $30,000 \times 10 \times 20\% = ₹ 60,000$ will be taken to P&L statement
- (5) Dividend on shares purchased on 22.6.20X1
 $= 5,000 \times 10 \times 20\%$
 $= ₹ 10,000$ is adjusted to Investment A/c
- (6) Profit on sale of 20,000 shares = Sales proceeds - Average cost
Sales proceeds = ₹ 3,00,000
Average Cost = $(4,50,000 + 80,000 + 1,50,000 - 10,000) / 50,000 \times 20,000 = ₹ 2,68,000$
Profit = ₹ 3,00,000 - ₹ 2,68,000 = ₹ 32,000.
- (7) Cost of shares on 31.3.20X2
 $(4,50,000 + 80,000 + 1,50,000 - 10,000) / 50,000 \times 30,000 = ₹ 4,02,000$
- (8) Sale of rights amounting ₹ 10,000 (₹ 2 × 5,000 shares) will not be shown in investment A/c but will directly be taken to P & L statement.

Solution of Q4:

As per para 6 of AS 16 'Borrowing Costs', borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset should be capitalised as part of the cost of that asset. Other borrowing costs should be recognised as an

expense in the period in which they are incurred.

A qualifying asset is an asset that necessary takes a substantial period of time* to get ready for its intended use or sale.

The treatment for total interest amount of ₹52.20 lakhs can be given as:

Purpose	Nature	Interest to be capitalised	Interest to be charged to profit and loss account
		₹ in lakhs	₹ in lakhs
Modernisation and renovation Of plant and machinery	Qualifying asset	* *52.20 × 406/580 = 36.54 * *52.20 × 58/580 = 5.22	52.20 × 116/580 = 10.44
Advance to supplies for additional assets	Qualifying asset		
Working Capital	Not a qualifying asset		
		41.76	10.44

*A substantial period of time primarily depends on the facts and circumstances of each case. However, ordinarily, a period of twelve months is considered as substantial period of time unless a shorter or longer period can be justified on the basis of the facts and circumstances of the case.

** It is assumed in the above solution that the modernisation and renovation of plant and machinery will take substantial period of time (i.e., more than twelve months). Regarding purchase of additional assets, the nature of additional assets has also been considered as qualifying assets. Alternatively, the plant and machinery and additional assets may be assumed to be non-qualifying assets on the basis that the renovation and installation of additional assets will not take substantial period of time. In that case, the entire amount of interest, ₹52.20 lakhs will be recognised as expense in the profit and loss account for year ended 31st March, 20X2.

Solution of Q5:

(i) Computation of average accumulated expenses

		Rs.
Rs.3,00,000 × 12/12	=	3,00,000
Rs.2,40,000 × 10/12	=	2,00,000
Rs.4,00,000 × 8/12	=	2,66,667
Rs.3,60,000 × 3/12	=	90,000
		<u>8,56,667</u>

(ii) Calculation of average interest rate other than for specific borrowings

Amount of loan (₹)	Rate of interest	Amount of interest (Rs.)
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4,00,000	9%	=	36,000
5,00,000	12%	=	60,000
3,00,000	14%	=	42,000
			1,38,000
Weighted average rate of interest $1,38,000 / 12,00,000 \times 100$		=	11.5%

(iii) Amount of interest to be capitalized

		Rs.
Interest on average accumulated expenses:		
Specific borrowings (Rs.2,00,000 x 8%)	=	16,000
Non-specific borrowings (Rs.6,56,667* x 11.5%)	=	75,517
Amount of interest to be capitalized	=	91,517

(iv) Total expenses to be capitalised for building

	Rs.
Cost of building Rs. (3,00,000+2,40,000+4,00,000+3,60,000)	13,00,000
Add: Amount of interest to be capitalized	91,517
	13,91,517

(v) Journal Entry

Date	Particulars		Dr. (Rs.)	Cr. (Rs.)
31.3.2018	Building A/c To Building WIP A/c To Borrowing costs A/c (Being amount of cost of building and borrowing cost thereon capitalised)	Dr.	13,91,517	13,00,000 91,517

Solution of Q6:

As per AS 26 'Intangible Assets'

(i) Carrying value of intangible asset as on 31.03.2009

At the end of financial year, on 31st March 2009, the production process will be recognized (i.e., carrying amount) as an intangible asset at a cost of Rs. 28 (50-22) lacs (expenditure incurred since the date the recognition criteria were met, i.e., from 1st December, 2009).

(ii) Expenditure to be charged to Profit and Loss account for the year ended 31.03.2010

	(Rs. in lacs)
Carrying Amount as on 31.03.2009	28
Expenditure during 2009-2010	80
Book Value	108
Recoverable Amount	(72)

Impairment loss	36
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Rs. 36 lakhs to be charged to Profit and loss account for the year ending 31.03.2010.

(iii) Carrying value of intangible asset as on 31.03.2010

	(Rs. in lacs)
Book Value	108
Less: Impairment loss	(36)
Carrying amount as on 31.03.2010	72

Solution of Q7:

An intangible asset is an identifiable non-monetary asset, without physical substance, held for use in the production or supply of goods or services, for rental to others, or for administrative purposes. Below are the 3 key ingredients to be satisfied to cover an item as an intangible asset under this standard:

- Identifiability,
- Control over a resource and
- Expectation (i.e. probable - 50% plus) of future economic benefits flowing to the enterprise.

The recognition of an item as an intangible asset requires an enterprise to demonstrate that the item meets the definition of an intangible asset and recognition criteria set out as below:

- It is probable that the future economic benefits that are attributable to the asset will flow to the enterprise; and
- The cost of the asset can be measured reliably.

Solution of Q8:

In the given case, Mithya Ltd. concurrently agreed to repurchase the same goods from Satya Ltd. on 1st February, 2024. Also the re-selling price is pre-determined and covers purchasing and holding costs of Satya Ltd. Hence, the transaction between Mithya Ltd. and Satya Ltd. on 1st February, 2024 should be accounted for as financing rather than sale. The resulting cash flow of ` 9.60 lakh received by Mithya Ltd., cannot be considered as revenue as per AS 9 "Revenue Recognition".

JOURNAL ENTRIES IN THE BOOKS OF MITHYA LTD.

1.2.2024	BANK A/C DR. TO ADVANCE FROM SATYA LTD. Being advance received under sale and repurchase agreement (8 Lakhs + 20% of 8 Lakhs)	9.60 LAKHS 9.60 LAKHS
31.3.2024	FINANCE CHARGES A/C DR. TO SATYA LTD. (Finance Charges for 2 months) $(10.80 - 9.60) \times 2/6$	0.40 LAKHS 0.40 LAKHS
31.3.2024	PROFIT AND LOSS A/C DR. TO FINANCE CHARGES A/C	0.40 LAKHS 0.40 LAKHS

	(Being amount of Finance charges transfer to P&L)	
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